

HOUSE FINANCE COMMITTEE
June 2, 2006
5:14 p.m.

CALL TO ORDER

Co-Chair Meyer called the House Finance Committee meeting to order at [5:14:17 PM](#).

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

MEMBERS ABSENT

Representative Carl Moses
Representative Bruce Weyhrauch

ALSO PRESENT

Representative Paul Seaton; Representative Norm Rokeberg;
Representative David Guttenberg; Dan Dickinson, Consultant,
Tax Division, Department of Revenue; Robynn Wilson,
Director, Division of Tax, Department of Revenue; Robert
Mintz, Assistant Attorney General, Department of Law

PRESENT VIA TELECONFERENCE

There were no teleconference testifiers.

SUMMARY

CSSB 2001 (FIN)

"An Act relating to the production tax on oil and gas and to conservation surcharges on oil; relating to criminal penalties for violating conditions governing access to and use of confidential information relating to the production tax; amending the definition of 'gas' as that definition applies in the Alaska Stranded Gas Development Act; making conforming amendments; and providing for an effective date."

HCS CSSB 2001 (FIN) was REPORTED out of Committee with a "do pass" recommendation and with a new

fiscal impact note by the Department of Revenue
and previously published zero fiscal note: #1 REV.

#hb2001

CS FOR SENATE BILL NO. 2001(FIN)

"An Act relating to the production tax on oil and gas and to conservation surcharges on oil; relating to criminal penalties for violating conditions governing access to and use of confidential information relating to the production tax; amending the definition of 'gas' as that definition applies in the Alaska Stranded Gas Development Act; making conforming amendments; and providing for an effective date."

[5:16:22 PM](#)

Co-Chair Chenault MOVED to ADOPT Amendment 6. Representative Hawker OBJECTED.

ROBERT MINTZ, ASSISTANT ATTORNEY GENERAL, DEPARTMENT OF LAW, explained Amendment 6, which creates special provisions for the tax rate on oil and gas produced south of the Brooks Range and outside of the Cook Inlet basin.

[5:17:35 PM](#)

Mr. Mintz He explained that the amendment also amends AS 33.55.170 on page 28. A new tax credit would be add a new tax credit of up to \$6 million a year for oil and gas produced in this area, in addition to the current \$12 million dollar credit. There is no production in this area currently. He explained that for up to 10 years from when production would started, as long as it started no later than May 1, 2016, a producer could take a tax credit of up to \$500,000 per month against tax liability under AS 43.55.011 (e), which is the basic PPT.

Mr. Mintz added that the sunset is either 2016 or 10 years from when commercial production starts (in the case of a producer that doesn't currently have production.) There is a potential 20 year period in which the credit could apply.

Mr. Mintz noted that the amendment also amends 43.55.011 (k) and (l). The amendment exempts Cook Inlet oil from the requirement that any benefit a producer receives from the Cook Inlet tax cap be netted out against tax credits that would otherwise be applicable to Cook Inlet oil and gas. The amendment eliminates the provisions as they apply to Cook Inlet oil. The requirement would only apply to Cook Inlet gas.

[5:21:25 PM](#)

DAN DICKINSON, CONSULTANT, TAX DIVISION, DEPARTMENT OF REVENUE, created a portrait of the four regions being created. The first would be North Slope oil and gas, which accounts for 90 percent of the oil and gas production, and 97 percent of the tax. The 20/20 PPT will apply to the North Slope, credits will be generated and there will be no restrictions on where they can be used. There are no special restrictions for this portion, which constitutes the majority.

Mr. Dickinson observed that both oil and gas in an area that doesn't fall within the other three regimes was referred to as everywhere else. This covers Bristol Bay and the Nenana Basin and other places that are prospective but have no current production. There is currently no production or taxes in this area. The 20/20 PPT would apply and all credits generated could be used against current production anywhere in the state. There is an additional credit of up to \$6 million a year, which could be applied against production that comes from this area.

Mr. Dickinson noted that the next area would be Cook Inlet oil, which constitutes less than two percent of total production in Alaska and zero percent of the production tax because there is zero tax on Cook Inlet currently under the economic limit factor (ELF). There is a look back to prior taxes. Cook Inlet oil would be taxed at the PPT rate or the previous year's tax rate whichever is less. With the production tax now zero there will be no PPT on Cook Inlet oil. Credits can still be generated and applied elsewhere in Alaska. Ways of parsing out oil and gas will need to be generated through regulation. He noted that the costs would have to be "somewhat arbitrarily" divided up.

Mr. Dickinson observed that the last arena is Cook Inlet gas. The PPT base would be compared to a baseline of taxes being currently paid or paid for the past year to form a cap. Credits generated from Cook Inlet investments would first be applied against the cap created. He observed that if there were a tax liability under the PPT \$5 million and there was a look back tax liability of \$3 million there would be a \$2 million difference applied if credit is available. Credits must be used within other Cook Inlet gas arenas to the degree that they are limited. "IF in fact you had a credit you could have used without the cap, that can be used across the state in any area." Cook Inlet gas constitutes about eight percent of the total production in Alaska and about three percent of current production taxes: \$35 million annually.

[5:26:06 PM](#)

Representative Holms asked if there limitations on the "everywhere else" portion. He questioned if there should be a sunset of 10 or 20 years. Mr. Dickinson observed that any limitation that would apply under 33.55.170 also applies. There is a sunset provision. There is a 10-year window. The only additional restriction is that credits would expire at the end of the year and are not transferable or sellable.

[5:27:17 PM](#)

In response to a question by Representative Kelly, Mr. Dickinson clarified that if the discovery was made on the last day of the 10-year period, the credit would apply for the following 10 years (allowing for a 20 year period).

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Representative Hawker WITHDREW his OBJECTION. There being NO OBJECTION, Amendment 6 was adopted.

Co-Chair Chenault MOVED to ADOPT Amendment 7. Representative Hawker OBJECTED for the purpose of discussion.

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Mr. Mintz explained Amendment 7, which would fix some gaps in the current legislation. The amendment addresses the progressivity tax on page 4 of the legislation: AS 43.55.011 (g) and (h). He observed that these provisions could open up a potential for manipulation of timing by allowing costs to be moved between months. The amendment requires that annualized costs be used for the year (one-twelfth of the annual cost each month). The same timing problem cost pertains to both the upstream lease expenditure costs and downstream transportation costs. The amendment requires that when the gross value of oil and gas at the point of production is calculated, the gross value is calculation for the transportation costs are done with the monthly average of the transportation costs.

Mr. Mintz referred to page 27, which requires the department to adopt regulations to provide for the monthly averaging of transportation costs.

[5:31:08 PM](#)

Mr. Mintz observed that the amendment also addresses a mathematical error on page 13, transitional investment expenditure credits. The 2-for-1 principle was adopted for credits for transitional investments (look back provision), which allows for credit over time for capital investments in

oil and gas that were made during the five years before the new tax region goes into effect. The 2-for-1 look-back provision would require a producer to make \$2 dollars of new investment for every \$1 credit. The current language would have allowed five times the credit rate intended by the 2-for-1 look-back principle. He explained the mechanism that would allow the \$2 for \$1 provision on line 10, page 13.

[5:33:42 PM](#)

Mr. Mintz observed that amendment addresses the tax return filing requirement and fixes an ambiguity in how the statute of limitations for tax assessments would work under the new tax regime. The ambiguity arises because every month oil and gas is produced gives rise to an obligation to file two tax returns: the monthly tax return triggered by the obligation to pay at least 95 percent of the tax levied by the PPT provision and "true up" provision required March 31st, which is triggered by the obligation to pay the remaining 5 percent of the tax.

[5:35:18 PM](#)

Mr. Mintz explained that there would be two tax filings required. The statute of limitations states that the Department of Revenue has three years from a date a tax return is filed to issue an assessment of the tax deficiency. The amendment clarifications that the March 31st date triggers the three year statute of limitation.

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Mr. Mintz referred to page 22, line 11, which provides for a complete parallel construction of the language. He explained that when "ordinary and necessary" was moved to the definition of lease expenditures, it highlighted the fact that there are two types of situations being addressed. The first is exploration, developing or production oil or gas lease or properties. The second is when exploration is occurring on un-leased land. The intent is to have totally parallel construction to clarify that all of the key elements of "lease expenditures" apply to both situations.

[5:36:52 PM](#)

Mr. Mintz explained that the final portion requires that year annualized transportation costs be used in calculating production tax value when the progressivity tax is triggered.

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Representative Hawker WITHDREW his OBJECTION. There being NO OBJECTION, Amendment 7 was adopted.

Representative Foster MOVED to report HCS CSSB 2001 (FIN) out of Committee with the accompanying fiscal notes. HCS CSSB 2001 (FIN) was REPORTED out of Committee with a "do pass" recommendation and with a new fiscal impact note by the Department of Revenue and previously published zero fiscal note: #1 REV.

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ADJOURNMENT

The meeting was adjourned at 5:40 PM