

**ALASKA STATE LEGISLATURE
HOUSE RESOURCES STANDING COMMITTEE**

March 17, 2006

12:38 p.m.

MEMBERS PRESENT

Representative Jay Ramras, Co-Chair
Representative Ralph Samuels, Co-Chair
Representative Jim Elkins
Representative Carl Gatto
Representative Gabrielle LeDoux (via teleconference)
Representative Kurt Olson
Representative Paul Seaton
Representative Harry Crawford
Representative Mary Kapsner

MEMBERS ABSENT

All members present

COMMITTEE CALENDAR

HOUSE BILL NO. 488

"An Act repealing the oil production tax and gas production tax and providing for a production tax on the net value of oil and gas; relating to the relationship of the production tax to other taxes; relating to the dates tax payments and surcharges are due under AS 43.55; relating to interest on overpayments under AS 43.55; relating to the treatment of oil and gas production tax in a producer's settlement with the royalty owner; relating to flared gas, and to oil and gas used in the operation of a lease or property, under AS 43.55; relating to the prevailing value of oil or gas under AS 43.55; providing for tax credits against the tax due under AS 43.55 for certain expenditures, losses, and surcharges; relating to statements or other information required to be filed with or furnished to the Department of Revenue, and relating to the penalty for failure to file certain reports, under AS 43.55; relating to the powers of the Department of Revenue, and to the disclosure of certain information required to be furnished to the Department of Revenue, under AS 43.55; relating to criminal penalties for violating conditions governing access to and use of confidential information relating to the oil and gas production tax; relating to the deposit of money collected by the Department of Revenue under AS 43.55; relating to the calculation of the gross value at the point of production of oil or gas; relating to the determination of the net value of taxable oil and gas for purposes of a production

tax on the net value of oil and gas; relating to the definitions of 'gas,' 'oil,' and certain other terms for purposes of AS 43.55; making conforming amendments; and providing for an effective date."

- MOVED CSHB 488(RES) OUT OF COMMITTEE

PREVIOUS COMMITTEE ACTION

BILL: HB 488

SHORT TITLE: OIL AND GAS PRODUCTION TAX

SPONSOR(S): RULES BY REQUEST OF THE GOVERNOR

02/21/06	(H)	READ THE FIRST TIME - REFERRALS
02/21/06	(H)	RES, FIN
02/22/06	(H)	RES AT 12:30 AM HOUSE FINANCE 519
02/22/06	(H)	Heard & Held
02/22/06	(H)	MINUTE(RES)
02/23/06	(H)	RES AT 12:30 AM HOUSE FINANCE 519
02/23/06	(H)	Heard & Held
02/23/06	(H)	MINUTE(RES)
02/24/06	(H)	RES AT 12:30 AM HOUSE FINANCE 519
02/24/06	(H)	Heard & Held
02/24/06	(H)	MINUTE(RES)
02/25/06	(H)	RES AT 10:00 AM SENATE FINANCE 532
02/25/06	(H)	Joint with Senate Resources
02/27/06	(H)	RES AT 12:30 AM CAPITOL 124
02/27/06	(H)	Heard & Held
02/27/06	(H)	MINUTE(RES)
02/28/06	(H)	RES AT 12:30 AM CAPITOL 124
02/28/06	(H)	Heard & Held
02/28/06	(H)	MINUTE(RES)
03/01/06	(H)	RES AT 12:30 AM CAPITOL 124
03/01/06	(H)	Heard & Held
03/01/06	(H)	MINUTE(RES)
03/02/06	(H)	RES AT 12:00 AM CAPITOL 124
03/02/06	(H)	Heard & Held
03/02/06	(H)	MINUTE(RES)
03/03/06	(H)	RES AT 12:30 AM CAPITOL 124
03/03/06	(H)	Heard & Held
03/03/06	(H)	MINUTE(RES)
03/04/06	(H)	RES AT 2:00 PM HOUSE FINANCE 519
03/04/06	(H)	Heard & Held
03/04/06	(H)	MINUTE(RES)
03/06/06	(H)	FIN AT 12:30 AM HOUSE FINANCE 519
03/06/06	(H)	Presentation by Legislative Consultant
03/06/06	(H)	RES AT 12:30 AM HOUSE FINANCE 519

03/06/06	(H)	Testimony by legislative consultant
03/07/06	(H)	RES AT 12:30 AM CAPITOL 124
03/07/06	(H)	Heard & Held
03/07/06	(H)	MINUTE(RES)
03/08/06	(H)	RES AT 12:30 AM CAPITOL 106
03/08/06	(H)	-- Meeting Canceled --
03/09/06	(H)	RES AT 12:30 AM CAPITOL 106
03/09/06	(H)	-- Meeting Canceled --
03/10/06	(H)	RES AT 12:30 AM CAPITOL 106
03/10/06	(H)	Heard & Held
03/10/06	(H)	MINUTE(RES)
03/11/06	(H)	RES AT 10:00 AM CAPITOL 106
03/11/06	(H)	-- Meeting Canceled --
03/13/06	(H)	RES AT 10:00 AM CAPITOL 124
03/13/06	(H)	Heard & Held
03/13/06	(H)	MINUTE(RES)
03/14/06	(H)	RES AT 12:30 AM CAPITOL 124
03/14/06	(H)	Heard & Held
03/14/06	(H)	MINUTE(RES)
03/15/06	(H)	RES AT 1:15 PM CAPITOL 124
03/15/06	(H)	Heard & Held
03/15/06	(H)	MINUTE(RES)
03/16/06	(H)	RES AT 12:30 AM CAPITOL 124
03/16/06	(H)	Heard & Held
03/16/06	(H)	MINUTE(RES)
03/17/06	(H)	RES AT 12:30 AM CAPITOL 124

WITNESS REGISTER

ROBERT MINTZ, Assistant Attorney General
Oil, Gas & Mining Section
Civil Division
Department of Law
Anchorage, Alaska
POSITION STATEMENT: Answered questions on HB 488.

DAN DICKINSON, Consultant
to the Office of the Governor
Anchorage, Alaska
POSITION STATEMENT: Answered questions on HB 488.

ACTION NARRATIVE

CO-CHAIR RALPH SAMUELS called the House Resources Standing Committee meeting to order at 12:40:41 PM. Representatives Ramras, Samuels, Kapsner, Olson, Gatto, Seaton, Crawford, and

Elkins were present at the call to order. Representative LeDoux was on teleconference.

HB 488-OIL AND GAS PRODUCTION TAX

[12:40:57 PM](#)

CO-CHAIR SAMUELS announced that the only order of business would be HOUSE BILL NO. 488, "An Act repealing the oil production tax and gas production tax and providing for a production tax on the net value of oil and gas; relating to the relationship of the production tax to other taxes; relating to the dates tax payments and surcharges are due under AS 43.55; relating to interest on overpayments under AS 43.55; relating to the treatment of oil and gas production tax in a producer's settlement with the royalty owner; relating to flared gas, and to oil and gas used in the operation of a lease or property, under AS 43.55; relating to the prevailing value of oil or gas under AS 43.55; providing for tax credits against the tax due under AS 43.55 for certain expenditures, losses, and surcharges; relating to statements or other information required to be filed with or furnished to the Department of Revenue, and relating to the penalty for failure to file certain reports, under AS 43.55; relating to the powers of the Department of Revenue, and to the disclosure of certain information required to be furnished to the Department of Revenue, under AS 43.55; relating to criminal penalties for violating conditions governing access to and use of confidential information relating to the oil and gas production tax; relating to the deposit of money collected by the Department of Revenue under AS 43.55; relating to the calculation of the gross value at the point of production of oil or gas; relating to the determination of the net value of taxable oil and gas for purposes of a production tax on the net value of oil and gas; relating to the definitions of 'gas,' 'oil,' and certain other terms for purposes of AS 43.55; making conforming amendments; and providing for an effective date."

[Before the committee was the committee substitute (CS) for HB 488, version 24-GH2052\Y, Chenoweth, 3/15/06.]

[12:41:12 PM](#)

REPRESENTATIVE KAPSNER moved to adopt Amendment 9, as follows [original punctuation provided]:

Delete Sec 27, page 16, line 23 through page 17, line 17.

REPRESENTATIVE KAPSNER said Amendment 9 deletes what used to be Section 20 in the original bill, and for the CS, it deletes Section 27. Those sections added new subsections to AS 43.55.150, and a number of people thought the new language was not essential to the bill. She noted that some people felt that it was Christmas tree language regarding the royalty settlement methodology. She said the consultant expressed concern that there would be ways that the state could lose money with this section in the bill. She said it is not crucial to the proposed profit-based petroleum production tax (PPT).

[12:42:30 PM](#)

DAN DICKINSON, Consultant to the Office of the Governor, said he is the former director of the tax division in the Department of Revenue. He said Representative Kapsner is right that the provision is not essential to the PPT. "It is borne out of the frustration that I felt as an administrator that we have one group of very skillful folks sitting on the fifth floor and another group sitting on the eighth floor of the Atwood Building in Anchorage, and these dedicated folks spend their time looking at the exact same set of transactions, one with a set of royalty glasses on and one with a set of tax glasses on."

MR. DICKENSON said the royalty rules and tax rules are very similar; they are both trying to get to the actual cost of transportation between the market and the point of valuation. He said differences have emerged, "and so we have folks who are dedicated to pursuing those two paths. The reason this bill is in here, is it gives the commissioner the discretion through regulations to use other means of valuation other than the single standards set out in the law. ... The commissioner would make sure that they all met the tests that we have." He said if there is one set of transactions already being computed, and it meets the quality standards of the state, "we felt it was appropriate to simply do that calculation once as opposed to doing it twice." He said that with unlimited resources, a second check would be good, but it is useful to "kill two birds with one stone."

[12:44:40 PM](#)

CO-CHAIR SAMUELS surmised, "Your section takes what we use for royalty and just uses the same value for tax."

MR. DICKINSON said it gives the commissioner the authority to use that second royalty value. The commissioner could write regulations incorporating aspects or all of the royalty valuations, he stated.

[12:45:12 PM](#)

REPRESENTATIVE GATTO said on page 16, line 25 states that the department may allow the producer to decide, not the commissioner.

MR. DICKINSON said that is right. "What we say here is that the commissioner will set up the rules and then presumably they'll present an election to the taxpayer who can then opt to do it under one or the other set."

[12:45:58 PM](#)

REPRESENTATIVE SEATON asked for an estimate of the financial difference between the two sets of numbers.

MR. DICKINSON said he believed they would be very close. He said "the problem in comparing them is, and one of the reasons why we had all these rules for the commissioner is, when the royalty settlement agreements were entered into in the early 1990s they only covered existing leases. So we've had a bunch of production on the North Slope that isn't covered by them. When you set your averages in, you'd have to be careful that you were comparing apples and oranges." He said:

I think they're fundamentally, if I can quickly identify for you the major differences, one of them is, under law for tax under 020 (f) we set the tax value either at what the oil and gas is sold for or the prevailing value. Under the royalty settlement agreements that are now in existence, the starting point is simply a spot price—a fair value of the crude as defined by ... national markers. That is a difference. Clearly, whenever you have a 'higher of' as we have in the tax statute, you're probably going to come up with a higher number than you do when you simply have one value applied consistently. My argument to you on that would be, the differences are not large, and I believe that the provisions for 020 (f) were written before there were transparent markers, and I believe that looking at a transparent marker and trying to use that to value petroleum when

it has landed on the West Coast, makes a lot of sense. That is one potential difference. If the commissioner felt that the marker was not doing as it could, that could be one of the standards that he could write in and say, 'we will not accept a royalty value if that marker's not good.' The second difference has to do with vessels and how the return on and of a vessel is captured. A vessel is a long-lived asset...you are going to use it for 20 years. The mechanics of that are different between the two. And then the third difference, of course, is when we have to correct for ... field costs, [which] are a portion of a royalty settlement. They are not part of the tax. We would make sure that they did not come in through the royalty settlement agreements.

[12:48:37 PM](#)

REPRESENTATIVE SEATON surmised that the current system is taking the higher number, and under the new system, it is up to the commissioner to let the producer choose.

MR. DICKINSON said that under current tax law, 020 (f), the department may use the higher prevailing value or the sales price; it is not required to. The regulations create a safe harbor so if the price that it is sold for is only a few cents less than the marker, the adjustment won't be made. "If it was \$2 less, clearly we would go in and substitute the prevailing value for that transaction. So that is how 020 (f) works under current statute. What would be replaced is a system where, if we decided to allow--if the commissioner decided to allow--a royalty valuation all the way down to destination, at least as I envision it--it clearly could be other things--the commissioner would say 'as long as that royalty settlement agreement is in place you may elect to use either that or this set of tax rules, you cannot switch back and forth month to month, you can't, every month, see which one is the higher and use that.' Now, that's not in here. Clearly the commissioner could decide, 'we'll have it be every month'. I can't imagine that happening. But what we tried to do is set out the broad outlines, and the commissioner, by regulation, would establish the methodologies."

[12:50:32 PM](#)

REPRESENTATIVE SEATON said he wants an estimated value difference between the two that are under the commissioner's authority. It is per producer, which could create a disparity,

and he said he doesn't want to put the commissioner in that position.

MR. DICKINSON said he doesn't have the numbers. He said the purpose of giving that discretion to the commissioner is to allow him or her to follow the market and to follow changing Department of Natural Resources settlements. He said, "There are re-opener processes in those so that things can be renegotiated. If parties can't renegotiate, they go to an arbitration." The Department of Law has been clear that the taxpayer can't decide what to pay. "Our notion was, if there's a method of calculating wellhead value that's already in place and already makes sense, why have a parallel system?"

[12:52:24 PM](#)

CO-CHAIR SAMUELS said he maintains his objection. He said he can't pretend that he knows more than people who do this for a living.

MR. DICKINSON said this will not affect the royalty value.

[12:52:55 PM](#)

REPRESENTATIVE GATTO asked if it is better to have it set in concrete.

MR. DICKINSON said that is a constant tension. He said conditions change and he tried to strike the right balance. "Clearly, the kinds of decisions that a commissioner can make, just simply in terms of how much resources go to auditing, what you do with audits once you've gotten them, whether you're going to settle those audits or pursue them to the bitter end through all the court systems. Those kinds of decisions probably are going to have greater importance in the final analysis than the direction that is here in Section 27."

[12:54:45 PM](#)

REPRESENTATIVE KAPSNER asked if Mr. Dickinson said the provision is not fundamental to HB 488 and doesn't have to be in it.

MR. DICKINSON said, "The fundamental economic of encouraging exploration and then getting a piece of the high side...is not affected by this."

[12:55:22 PM](#)

REPRESENTATIVE SEATON said if this is defeated, he still wants the calculations.

12:55:47 PM

A roll call vote was taken. Representatives Crawford and Kapsner voted in favor of Amendment 9. Representatives Gatto, Olson, Ramras, Samuels, Seaton, Elkins and LeDoux voted against it. Therefore, Amendment 9 failed by a vote of 2-7.

12:57:26 PM

REPRESENTATIVE SEATON moved Amendment 14, 24-GH2052\Y.12, Chenoweth, 3/17/06, as follows [original punctuation provided]:

Page 18, line 31, through page 19, line 1:

Delete "April 1, 2006"

Insert "January 1, 2006"

Page 28, line 10, following "TRANSITIONAL PROVISIONS.":

Insert "(a) Notwithstanding any contrary provision of AS 43.55.024(a), enacted by sec. 14 of this Act, a producer or explorer may apply for a credit under AS 43.55.024 based on a qualified capital expenditure incurred on or after January 1, 2006."

Reletter the following subsections accordingly.

Page 29, line 21:

Delete "(f)(1)"

Insert "(g)(1)"

Page 29, line 23:

Delete "(f)(2)"

Insert "(g)(2)"

Page 29, line 25:

Delete "(f)(1)"

Insert "(g)(1)"

Page 29, line 26:

Delete "(g)(1)"

Insert "(h)(1)"

Page 30, following line 16:

Insert a new bill section to read:

"* **Sec. 46.** The uncodified law of the State of Alaska is amended by adding a new section to read:

RETROACTIVITY OF CERTAIN EXPENDITURES USED TO SUPPORT PRODUCTION TAX CREDIT CLAIM AND DETERMINATION OF PRODUCTION TAX VALUE OF OIL AND GAS. AS 43.55.160(c)(1), enacted by sec. 28 of this Act, applies to allow a producer to claim as lease expenditures certain expenditures incurred on or after January 1, 2006, and before the effective date of AS 43.55.160, added by sec. 28 of this Act, and sec. 43(a) of this Act applies to authorize a producer or explorer to apply for a credit under AS 43.55.024, enacted by sec. 14 of this Act, based on a qualified capital expenditure incurred on or after January 1, 2006, and before the effective date of AS 43.55.024, enacted by sec. 14 of this Act. To the extent these provisions give legal effect to prior conduct, they are retroactive to January 1, 2006."

Renumber the following bill sections accordingly.

Page 30, line 19:

Delete "sec. 48"

Insert "sec. 49"

Page 30, line 22:

Delete "46"

Insert "47"

Page 30, line 24:

Delete "sec. 47"

Insert "sec. 48"

CO-CHAIR SAMUELS objected.

REPRESENTATIVE SEATON said Amendment 14 allows the deduction of expenses and the generation of credits based on a calendar year. He said, "It allows the entire calendar year from January 1, 2006 to be used for those expenses and deductions."

[12:57:30 PM](#)

CO-CHAIR SAMUELS removed his objection. Hearing no further objections, Amendment 14 carried.

[12:58:13 PM](#)

REPRESENTATIVE SEATON moved Amendment 15, 24-GH2052\Y.13, Chenoweth, 3/17/06, as follows [original punctuation provided]:

Page 4, line 8:

Delete "(g) of"

Page 4, lines 13 - 19:

Delete all material.

Insert "index as determined under this subsection. The oil price index for a month is the number equal to the average United States Gulf Coast price determined under (h) of this section for that month of West Texas Intermediate crude oil in dollars per barrel, less 50. If the average price determined under (h) of this section is not more than \$50 per barrel, the oil price index is zero.

(g) Notwithstanding calculation of the rate of tax under (f) of this section, if the average price determined under (h) of this section is at least \$110 per barrel, the rate of tax under (f) of this section is 37.5 percent."

CO-CHAIR SAMUELS objected.

REPRESENTATIVE SEATON said Amendment 15 tries to get to the intent that at very high oil prices there will be an equal split between the state and the producers. The crux is in lines 11 through 13, he noted. He said the way the surtax is calculated is deductible against the PPT, so it will equal 80 percent of the increasing percentage rate. To get to 50 percent of the net, "we actually have the total percentage going to 37.5, and that equals 30 percent of the net. So the 20 percent plus 30 percent means the state will get half and the producers would get half. And this takes place at \$110 a barrel, so this would leave in the existing 3/10 of 1 percent per dollar escalating, starting at \$50. And would not affect the deductibility of those from the PPT but would start at 110 and immediately go to the equal split of net."

[12:59:47 PM](#)

REPRESENTATIVE KAPSNER said the amendment should say lines 14 through 19.

REPRESENTATIVE SEATON said this is a conceptual amendment based on Version Y, as well as the previous amendment, because the committee has been amending Version Y.

CO-CHAIR SAMUELS said the drafter will fix that.

REPRESENTATIVE KAPSNER said, "If we delete line 13, it will cut out a section."

CO-CHAIR SAMUELS said the drafter will take care of that.

CO-CHAIR SAMUELS removed his objection. Hearing no further objections, Amendment 15 carried.

[1:00:59 PM](#)

REPRESENTATIVE CRAWFORD moved Amendment 16, 24-GH2052\Y.14, Chenoweth, 3/17/06, as follows [original punctuation provided]:

Page 4, following line 31:

Insert a new subsection to read:

"(i) Notwithstanding any other provision of this chapter, except as to oil or gas described in (e) of this section, tax credits that are authorized against the tax due under this section by this title, AS 38.05.180, and AS 41.09 may not be applied to reduce the producer's total tax due under this section on oil and gas produced during a calendar year to less than six percent of the production tax value of the taxable oil and gas produced by the producer from all leases or properties in the state, based on the gross value of the oil and gas at the point of production and determined without reference to adjustments authorized by AS 43.55.160. In making the determination required by this subsection, the department shall exclude oil and gas produced, the ownership or right to which is exempt from taxation."

REPRESENTATIVE CRAWFORD said he tried to make the amendment several times, and he has problems getting exactly what he wants because there is such a difference between a severance tax and a net profits tax. He said his intent is to create safety and protection to the state at low oil prices. He wants a minimum floor or a minimum tax of 6 percent so the state has protection when it needs it the most. He said from 1986 to 1989 the state was in a serious bind, and went to the Economic Limit Factor system (ELF), but it didn't fix the problem when oil is below

\$20 to \$30 per barrel. Mr. Dickinson said this amendment still doesn't get us there, so he wants the amendment to conceptually state that there is a 6 percent floor.

CO-CHAIR SAMUELS asked if that will be on gross values.

REPRESENTATIVE CRAWFORD said it would be the gross value at the point of production.

[1:03:35 PM](#)

CO-CHAIR RAMRAS said he bought some restaurants out of bankruptcy. The most onerous part of the problem was the lease contained a percentage rent provision. There was a minimal rent due, or the building owner would need to participate in the income when it exceeded 7.5 percent of sales. The shopping mall got the minimum when times were bad and got more money when times were good. He said he has a fundamental objection to one-way transactions. He said "this committee has been mindful of its responsibility to participate to a significant extent when times are good, and sharing windfalls that are generated by the oil and gas industry." He said he wants to make sure that the committee doesn't break the partnership by excluding the state's participation when times are bad. At \$22.50, BP said it loses money on a barrel of oil, which is partially the tariff from the Trans-Alaska Pipeline System that BP owns. If the state is going to share in the high prices, it needs to share risk at low oil prices.

[1:06:36 PM](#)

CO-CHAIR SAMUELS said he echoes that. When prices drop the state will take risks. He said the key is to not spend all the money the state makes when prices are high. He said the state is moving to a system that will take the royalty off the top, so it will still have that and the corporate income taxes, which will also deteriorate at low prices. A floor on taxes would mean that if cost recovery doesn't generate any profits, the industry will still be taxed. "I understand the problem of a future legislature...but if we're going take some of the high end, we can't take the high end and then take the low end also. He said he asked economists about a floor on the tax, and what would be the trade off at the high end over the long run. He said several answers, but none picked a figure, "but it was problematic. One of the answers that came back was at 70 actually. If you stopped the progressivity at 70 then put the

floor in. To me, I think that I would rather take some more of the risks rather than put in the floor."

1:09:10 PM

REPRESENTATIVE CRAWFORD said we have to look at the past and know that we are going to run into a problem. He said the legislature doesn't do a good job of saving money when the state is flush. Legislatures will be looking back and saying what were they thinking? "If we don't put protection for the state in at the low end, we will rue the day."

CO-CHAIR SAMUELS said he appreciates Representative Crawford bringing this issue forward. He said the committee never got into the substance of the risk and reward. He said the legislature needs to look at it as the bill moves forward.

1:10:51 PM

A roll call vote was taken. Representatives Crawford and Kapsner voted in favor of Amendment 16. Representatives Gatto, Olson, Ramras, Samuels, Seaton, Elkins and LeDoux voted against it. Therefore, Amendment 16 failed by a vote of 2-7.

CO-CHAIR SAMUELS said he will raise these issues for the legislature.

1:11:50 PM

CO-CHAIR RAMRAS noted Representative Kapsner's issue on the energy fund. He said were oil to hit the \$110 price, the people of Alaska would be in trouble.

1:12:24 PM

REPRESENTATIVE CRAWFORD moved Conceptual Amendment 17 as follows [original punctuation provided]:

Delete inclusion of gas in the new production tax;
retain current tax on gas.

REPRESENTATIVE CRAWFORD said oil and gas are two separate animals, and leaving gas in the bill will severely damage Alaska's competitiveness. He said he doesn't know if the legislature will get to the next step, which was promised by the administration. He said he was told that it would arrive and make everything clear, "and I haven't seen anything yet." He

said he is skeptical about what is coming and when. He said when he is told not to worry, that is the time to worry. It will be a difficult amendment to write, but he wants to leave gas in the current tax system.

[1:14:47 PM](#)

CO-CHAIR SAMUELS said there have been many discussions. The basic concept of cost recovery becomes extremely difficult because gas and oil come from the same hole. "How do you allocate the costs between the two without getting gamed?" he asked. He said some gas is reinjected, and how does on value that? He said another amendment, Amendment 19, will address some of Representative Crawford's concern.

[1:16:06 PM](#)

A roll call vote was taken. Representatives Crawford and Kapsner voted in favor of Amendment 17. Representatives Gatto, Olson, Ramras, Samuels, Seaton, Elkins and LeDoux voted against it. Therefore, Amendment 17 failed by a vote of 2-7.

[1:16:56 PM](#)

CO-CHAIR SAMUELS said Amendment 18 was discussed yesterday in the form of Amendment 11a.

REPRESENTATIVE CRAWFORD moved Amendment 18, 24-GH2052\Y.10, Chenoweth, 3/16/06, as follows [original punctuation provided]:

Page 19, line 7, following "AS 38.05.132":

Insert ", and do not include, in connection with a catastrophic oil discharge into the marine or inland water of the state, the containment and clean up expenses incurred by the producer, the incremental expenses of transportation of oil due to loss or damage incurred by the producer, and any damages or penalties imposed on the producer"

CO-CHAIR SAMUELS objected.

REPRESENTATIVE CRAWFORD said he doesn't believe the state should subsidize, in any way, a catastrophic oil spill similar to the Exxon Valdez. The language leaves lots of room for smaller oil spills; this if for a big one, he said. The state should not be subsidizing the oil industry's mistakes, he stated.

[1:18:13 PM](#)

CO-CHAIR SAMUELS asked about companies that invest in oil spill cleanup booms, boats and other contingency equipment. "Are you suggesting that we don't allow them to be written off?" He also asked about the definition of catastrophic. The instance of someone shooting a hole in the pipe was not the fault of TAPS owners, he said, but there are those expenses. He assumes the owners should be able to recoup their cost from that cleanup.

REPRESENTATIVE CRAWFORD said it is not his intent to change current law, but just to make sure it is include in the new form of taxation being discussed now. He said it wasn't his intent to say a company couldn't charge off expenses for acts of god or a shot to the pipeline. He told the drafter of Amendment 18 not to change the current law.

[1:20:18 PM](#)

CO-CHAIR SAMUELS asked how the amendment relates to another Exxon Valdez oil spill. He said he tends to agree with Representative Crawford, but the devil is in the details.

[1:20:58 PM](#)

MR. DICKINSON said, "The way that we currently administer, and again this will be downstream, is Clean Seas or a similar organization would be an allowable deduction. In other words, what you spend to be ready...clearly it was not intended to make that more expensive." He said, "Where we have gotten into issues is how those co-ops work when payments are made in and when receipts come back. So there have been some audit issues, but the fundamental notion here is those co-ops, the funding of them, is a deductible expense." For Alyeska Pipeline Service Company, "those costs will then get bundled into the tariff for future years. The things that Alyeska does currently for prevention or for mitigation...will be part of the tariff."

[1:22:05 PM](#)

CO-CHAIR SAMUELS surmised that if someone shoots a hole in the pipeline, the tariff goes up, causing a rise in the transportation costs.

MR. DICKINSON said that is how the situation is set up, "that your actual costs will become part of the tariff adjustment. I cannot speak for the specifics if there's; a shipper has to come

in and ask for that. Or a carrier has to come in and ask for those costs to be brought in. Those can be reviewed by regulatory bodies, but, in general, I can't imagine them disallowing an actual cost."

[1:22:41 PM](#)

CO-CHAIR SAMUELS asked about another Exxon Valdez-type incident, and how that relates to Alyeska and the deduction of costs under the amendment.

MR. DICKINSON said, "My recollection is that there were issues about whether this was in the...whose bailiwick the spill occurred in, and I'm not going to speak to that because I'm not sure. But, in general, if it is a downstream cost and it's a catastrophic oil spill, which I believe is 100,000 barrels or more, this would say you could not deduct those for calculating your gross, and now this would extend it to say you cannot use it for calculating your net as well."

[1:23:37 PM](#)

REPRESENTATIVE GATTO asked if a catastrophic spill related to an earthquake or terrorism would be treated the same.

MR. DICKINSON said yes, and it could include a spill that was less than 100,000 barrels but determined catastrophic under the discretion of the governor.

[1:24:17 PM](#)

REPRESENTATIVE SEATON noted that it is in marine and inland waters only.

MR. DICKINSON that is correct, but inland water of the state can be expansive.

[1:24:47 PM](#)

CO-CHAIR SAMUELS removed his objection. Hearing no further objections, Amendment 18 carried.

[1:24:59 PM](#)

CO-CHAIR RAMRAS moved Amendment 19, 24G-2, 3/17/06, 12:05 P.M., which reads as follows [original punctuation provided]:

Page 4, following line 31:

Insert the following material:

"(i) In addition to the taxes levied under (a), (e), and (f) of this section, for each month for which the gas price index determined under (j) of this section is greater than zero, there is levied upon the producer of gas a tax for all gas produced during that month from each lease or property in the state, less any gas the ownership or right to which is exempt from taxation. The tax is equal to two percent of the gross value at the point of production of the gas multiplied by the gas price index as determined under (j) of this section.

(j) The gas price index for a month is the number equal to the average Henry Hub gas price determined under (k) of this section for that month in dollars per million British thermal units, less eight, except that if the average price determined under (k) of this section is

(1) not more than \$8 per million British thermal units, the gas price index is zero; and

(2) more than \$23 per million British thermal units, the gas price index is 15.

(k) For purposes of (i) and (j) of this section, the department may calculate the average price or may, by regulation, specify the method by which the average price shall be calculated with reference to one or more published sources of price information. If, in the department's judgment, reliable published sources of Henry Hub gas price information cease, or appear likely to soon cease, to be available, or if, in the department's judgment, the Henry Hub gas price ceases, or appears likely to soon cease, to be a reliable indicator of the general price level of gas, the department shall, by regulation, specify a substitute formula for computing the gas price index. The substitute formula specified by the department under this subsection must bear, as nearly as is reasonably possible, the same relationship to the general price level of gas as did the Henry Hub gas price."

Page 6, line 26:

Delete "and (f)"

Insert ", (f), and (i)"

Page 6, line 31:

Delete "and (f)"

Insert "(f), and (i)"

Page 17, line 24, following "AS 43.55.011(f)":

Insert "and (i)"

Page 29, line 12:

Delete "and (f)"

Insert ", (f), and (i)"

CO-CHAIR SAMUELS objected.

[1:25:16 PM](#)

CO-CHAIR RAMRAS said yesterday the committee made an excellent decision to separate the progressivity of oil from gas. He spoke of recent changes in gas and oil prices. He said he consulted with Pedro van Meurs to get a formula for the progressivity of natural gas tied to market conditions. He distributed the formula, and said the amendment adopts the same type of progressivity adopted for oil prices, but at different numbers. Alaska may have natural gas for sale in large quantities in the next 15 years. He said the stress price for gas has been noted as being \$3.50 per million BTUs [British Thermal Unit], and now natural gas is in the low \$7.00 range, and after Hurricane Katrina the price went well over \$15.00. He selected \$8.00 per million BTU and tied it to the Henry Hub, which is a standard for natural gas prices. He removed the dollar increment and converted it into a number to create a formula, he stated. So it is the Henry Hub minus \$8.00. He said this would increase, by 2 percent for every dollar from \$8.00 through \$9.00, requiring to reach the next dollar prior to the trigger. The ratio is generally one to six between oil and gas, he said. "So a \$1.00 move in the price of 1 million BTUs of gas would be the equivalent of \$6.00 in the movement of the price of a barrel of oil."

[1:30:53 PM](#)

CO-CHAIR RAMRAS said for every dollar increase, there would be a multiplier of 2 percent until achieving a 30 percent tax, "which would kick in at \$23 per million BTUs. That would get us to the 50 percent equivalent that would have been in the equivalent at \$150 per barrel." He said Representative Seaton may want to look at it. He thinks it protects the state, giving the House Finance Committee the opportunity to explore the ramifications of a progressivity formula for natural gas.

[1:32:20 PM](#)

CO-CHAIR SAMUELS asked if it would operate the same way as oil except the trigger point is \$8.00 Henry Hub.

CO-CHAIR RAMRAS said yes; the tax paid on the progressivity of natural gas would become a deductible expense against the PPT.

[1:32:46 PM](#)

REPRESENTATIVE OLSON asked if line 14 should read "less than" instead of "not more than".

[1:33:20 PM](#)

MR. MINTZ said he followed the same format as the prior bill; it comes out the same.

[1:34:11 PM](#)

REPRESENTATIVE SEATON asked if prices are stated in BTUs or MCF [million cubic feet].

MR. MINTZ said the Henry Hub prices are related to BTUs. He said he was initially concerned because the production tax statutes measure gas in cubic feet, but Henry Hub price is only used for the index, and the index only affects the tax rate; therefore, there is no problem in having two different units.

The committee took an at-ease from [1:35:21 PM](#) to [1:43:57 PM](#).

CO-CHAIR RAMRAS said he feels more strongly about Amendment 19.

[1:44:21 PM](#)

CO-CHAIR SAMUELS removed his objection. Hearing no further objections, Amendment passed.

[1:44:51 PM](#)

CO-CHAIR RAMRAS moved Amendment 20, 24G-2, 3/17/06, 11:58 P.M., which reads as follows [original punctuation provided]:

Page 24, line 9:
Delete "\$10,000,000"
Insert "\$12,000,000"

Page 24, line 10:
Delete "\$2,500,000"
Insert "\$3,000,000"

Page 28, line 28:
Delete "\$10,000,000"
Insert "\$12,000,000"

Page 28, line 29:
Delete "\$7,500,000"
Insert "\$9,000,000"

CO-CHAIR SAMUELS objected.

CO-CHAIR RAMRAS said he is grateful to the committee and happy with the bill, but he is troubled by heavy oil, Cook Inlet and other issues not addressed by the committee. He said, "We were so careful to incentivize the explorers, and that in many of the improvements that we crafted to the governor's piece of legislation, I'm afraid that we may have taken a backward step with the explorers." He said Amendment 20 adds "a couple million dollars per full year and then some fractional amounts for 2006 and 2016 to the credit, the tax credit that is produced annually." He said he recognizes it benefits producers and explorers, but it sends the right signals to Anadarko Petroleum Corporation and Pioneer. It moves the annual credit from \$10 million up to \$12,000 per year, he explained.

[1:46:29 PM](#)

CO-CHAIR SAMUELS said this is in reference to the change to the \$73 million allowance.

REPRESENTATIVE SEATON asked, "So this takes an equivalence of an allowance on what amount?"

CO-CHAIR RAMRAS said it would be equivalent to a \$60 million credit down from the \$73 million that was in the governor's bill, and would get the explorers back to a better place. "It puts a smile on the explorers faces; a \$2 million-a-year smile."

[1:47:47 PM](#)

REPRESENTATIVE SEATON noted that this credit is available to every producer.

CO-CHAIR RAMRAS said, for better or for worse, everybody benefits equally.

CO-CHAIR SAMUELS said it is non-transferable and can't be carried forward.

REPRESENTATIVE GATTO asked what is special about the year 2016.

CO-CHAIR SAMUELS said there is a 10-year sunset on the provision, and the amount represents the fraction of the final year.

[1:48:48 PM](#)

CO-CHAIR SAMUELS removed his objection. Hearing no further objections, Amendment 20 passed.

[1:49:02 PM](#)

REPRESENTATIVE SEATON moved Amendment 21, which, from handwritten notes read:

Page 1, line 16
Delete 23
Insert 18

Page 1, line 17
Delete 15
Insert 18.75

CO-CHAIR SAMUELS objected.

REPRESENTATIVE SEATON said Amendment 21 "is basically an amendment to Amendment 19 that we just passed, and...it mirrors what we did for oil in the progressivity. It changes the line from 23 to 18, which was the equivalent of the 110-barrel, in BTU amounts per oil. And it changes the next line; that the index at 15...since it's deductible, to the 18.75, which gives the equal split."

CO-CHAIR SAMUELS removed his objection. Hearing no further objections, Amendment 21 passed.

[1:50:14 PM](#)

REPRESENTATIVE KAPSNER said she didn't move Amendment 13, which would have taken the tax and credit ratio up to 25/20. She said

she drafted the amendment to recognize the many hours of testimony from economists who said that a 25/20 ratio would not deter investment, and it would bring in \$600 million more to the state per year when oil is at \$60 a barrel. But Representative Seaton's Amendment 15 brings the tax rate up to 37.5 percent when the price of oil is \$110 per barrel. She said that was a good concession, and she didn't have the votes for her amendment anyway.

[1:52:26 PM](#)

REPRESENTATIVE GATTO moved to report HB 488, version 24-GH2052\Y, Chenoweth, 3/15/06, as amended, out of committee with individual recommendations and the accompanying fiscal notes.

[1:52:46 PM](#)

CO-CHAIR SAMUELS objected.

[1:52:51 PM](#)

REPRESENTATIVE CRAWFORD said his past comments show where he stands; he doesn't agree with the taxation system. He didn't agree with the fact that the governor negotiated an oil tax with the oil industry. He said he didn't think the governor had the authority to do so, "if fact he had explicit instructions not to negotiate oil taxes in the context of a gas pipeline." He noted that the Chair has explained that HB488 is separate, "but in a few weeks we will understand all the other pieces when we see the gas contract." He said he hasn't seen the other pieces and he does not understand the whole picture. He doesn't agree with a net profit based tax because it is not easily verifiable and sets the state up for years of litigation. He noted that the state went through years of litigation when it set up the severance tax, and it is still going through court battles after all these years. The efforts that the committee are making is simply putting perfume or lipstick on a pig, and it is still a pig. "I just don't agree with going away from something easily verifiable." He said the world-renowned consultants promoted a progressive severance tax because it is so much more easily verifiable, and that would have been the way to go. He said the committee is doing the best job it can, given the parameters the governor gave them, "but I am opposed to it and will remain opposed to it."

[1:56:27 PM](#)

CO-CHAIR SAMUELS said he regrets that the committee didn't address incentivizing heavy oil. He said he doesn't agree with everything in the CS, but he tried to find a balance. It is a long process, and he shares Representative Crawford's concerns regarding cost allocation. He will present those concerns and will make sure the bill is tightened up as it moved forward. He said the state needs to focus on a long-term fiscal plan. He thanked his staff.

[1:58:46 PM](#)

CO-CHAIR SAMUELS removed his objection.

[1:58:53 PM](#)

A roll call vote was taken. Representatives Gatto, Olson, Ramras, Samuels, Seaton, Kapsner, and Elkins voted in favor of CSHB 488, version 24-GH2052\Y, Chenoweth, 3/15/06, as amended, and Representative Crawford voted against it. Therefore, CSHB 488(RES) passed out of the House Resources Standing Committee by a vote of 7 to 1. [Representative LeDoux was on teleconference and therefore not allowed to vote.]

CO-CHAIR SAMUELS canceled the House Resources Standing Committee meeting on the following Saturday and Monday.

[2:00:39 PM](#)

ADJOURNMENT

There being no further business before the committee, the House Resources Standing Committee meeting was adjourned at [2:00 PM](#).