

**ALASKA STATE LEGISLATURE
HOUSE STATE AFFAIRS STANDING COMMITTEE**

August 1, 2006

8:06 a.m.

MEMBERS PRESENT

Representative Paul Seaton, Chair
Representative Carl Gatto, Vice Chair
Representative Jim Elkins
Representative Bob Lynn
Representative Jay Ramras
Representative Berta Gardner
Representative Max Gruenberg

MEMBERS ABSENT

All members present

OTHER LEGISLATORS PRESENT

Representative Mark Neuman

COMMITTEE CALENDAR

HOUSE BILL NO. 3005

"An Act providing for an additional production tax on oil when the price index on oil is above a certain amount; and providing for an effective date."

- MOVED HB 3005 OUT OF COMMITTEE

PREVIOUS COMMITTEE ACTION

BILL: HB3005

SHORT TITLE: PROGRESSIVE TAX ON OIL

SPONSOR(S): STATE AFFAIRS

07/25/06	(H)	READ THE FIRST TIME - REFERRALS
07/25/06	(H)	STA, FIN
07/26/06	(H)	STA AT 10:00 AM CAPITOL 106
07/26/06	(H)	Heard & Held
07/26/06	(H)	MINUTE(STA)
08/01/06	(H)	STA AT 8:00 AM CAPITOL 106

WITNESS REGISTER

CHERIE NIENHUIS, Petroleum Economist
Tax Division
Juneau Office
Department of Revenue
Juneau, Alaska

POSITION STATEMENT: Answered questions during the hearing on HB 3005.

ACTION NARRATIVE

CHAIR PAUL SEATON called the House State Affairs Standing Committee meeting to order at [8:06:03 AM](#). Representatives Seaton, Lynn, Gardner, Gruenberg (via teleconference), Gatto, and Elkins were present at the call to order. Representative Ramras arrived as the meeting was in progress.

HB3005-PROGRESSIVE TAX ON OIL

[8:06:10 AM](#)

CHAIR SEATON announced that the only order of business was HOUSE BILL NO. 3005, "An Act providing for an additional production tax on oil when the price index on oil is above a certain amount; and providing for an effective date."

CHAIR SEATON mentioned that there are several packets of materials plus amendments in the committee packet. He reviewed that at the last meeting the committee had looked at HB 3005 and what it meant with regard to the retroactivity clause as it relates to the progressivity of .35 percent per dollar above the West Texas Intermediate (WTI) price of \$50, capped out at \$150 WTI. The tax was not applied to the index, but rather the wellhead value.

[8:08:39 AM](#)

REPRESENTATIVE LYNN asked how HB 3005 would mesh together with any of the various proposals related to the production profits tax (PPT) that are before the legislature.

CHAIR SEATON explained that HB 3005 only looks at the progressivity element of a comprehensive tax bill. If it appears that the legislature is having problems coming to a consensus on a complete rewrite of the tax package, he said, HB 3005 would allow the state to recover part of the value that has been realized from high [oil] prices, and to do so retroactively. The bill does not change either the economic

limit factor (ELF) or the 15 percent tax rate. The proposed legislation could be incorporated into either a net or gross tax plan. He said the bill is not meant to supplant or supersede or curtail other discussions, but rather to act as a fallback position.

8:12:23 AM

CHAIR SEATON directed attention to a multi-page handout in the committee packet, which shows "progressivity schemes" - all the progressivity for all the proposals that have come before the legislature to date. He highlighted some examples of various bills' plans. The last bill shown on the second page of the handout is HB 3005, which Chair Seaton reviewed would pertain to oil over \$50 a barrel WTI, and the calculation would be: $(.35\% \times \text{WTI} - 50) \times \text{gross}$; at \$150 WTI the surcharge caps at 35 %."

8:17:01 AM

CHAIR SEATON said most of the ensuing pages in the handout are "recaps of those actual languages." He turned to the last [5] pages of the handout, which shows the PowerPoint presentation on Alaska PPT to the House Resources Standing Committee, March 13, 2006, by Barry Pulliam and Dr. Tony Finizza of Econ One. The assumption shown is 0.25 percent per dollar over \$45 per barrel WTI, with sliding scale tax. He reviewed that the proposal in the committee packet from the last hearing is by Pedro van Meurs, Ph.D., and, as "Option 2," shown thus: "Basic Tax Rate = $(\text{WTI} - 50.00) \times 0.25\%$." He reminded the committee that HB 3005 is a standalone bill that would not modify the lower tax.

8:19:11 AM

[Following was a brief discussion regarding what has occurred with the various bills on this issue that have come before the legislature thus far this year.]

8:21:50 AM

CHERIE NIENHUIS, Petroleum Economist, Tax Division, Juneau Office, Department of Revenue, directed attention to a matrix in the committee packet, entitled, "[HB] 305 Tax Rate with \$50 WTI per Barrel Trigger Point." She noted that the matrix shows the Alaska North Slope (ANS) [and WTI] oil prices [from \$50 to \$25, top to bottom at the left of the page]. She said the \$50 ANS price basically equates to a \$52 WTI - an historical differential that can change at times. She explained that [also

on the matrix, in columns] are various progressive surcharge rates, all the way down to 0.175 percent and as high as 0.45 percent. Below each rate is shown the actual percentages of the tax with those various prices and various progressive surcharge rates. Ms. Nienhuis pointed out where the 35 percent cut off rate appears throughout the matrix [color highlighted on the page]. She said that is a feature of the matrix that she provided in response to the committee's request from the last hearing.

CHAIR SEATON noted that the occurrence shown at the bottom-right corner of the matrix - where the amount of 90.90 percent is a result of the progressive surcharge rate of 0.45 percent and an ANS oil sales price of \$250 - would not take place under HB 3005, because of the bill would impose a cap of 35 percent. He indicated that the cap shows along "the top of the shaded line."

[8:25:08 AM](#)

MS. NIENHUIS, in response to Representative Gatto, concurred that as the state begins to produce more heavy oil, the aforementioned differential could become greater. She said, "A lot has to do with what the benchmark is, as well." She surmised that the alternative would be to "base it on ANS price." She remarked that she has noticed that most of the bills coming out of committees have been based on ANS price. She guessed that that might be "a little safer, as far as on down the road," but she specified that she cannot provide comment on what the committee should choose.

MS. NIENHUIS, in response to Chair Seaton, confirmed his summation that the value of the "basket of oil" is based on the actual value of the oil, and if it is heavy oil, that would presumably bring down the value. She noted that over the past month the differential has dropped somewhat to around \$1.60-\$1.80.

CHAIR SEATON asked if gas liquids injected as oil into the pipelines would change the mixture.

MS. NIENHUIS replied that she does not know for certain, but can find out.

[8:28:41 AM](#)

MS. NIENHUIS, in response to a question from Representative Gatto, offered her understanding that heavy oil has more

components that need to be removed from the oil, thus the processing is more expensive and the value of what is left is decreased.

REPRESENTATIVE GATTO indicated that he would like to know more about heavy oil.

[8:30:08 AM](#)

CHAIR SEATON suggested that an expert in the field may better offer that information.

[8:30:30 AM](#)

CHAIR SEATON directed attention to the committee's own draft memorandum in the committee packet with two attached amendments, one relating to "185 exploration credit" and the other to heavy oil credits addressed in the bill. He said he would like the committee to consider the amendments and decide if it would like to recommend the bill move forward to the House Finance Committee with the amendments. He explained that the committee has heard a lot of concern about heavy oil, and if the lower tax rate changes are not made, there is nothing in [the bill] to indicate that the committee is concerned about investment in heavy oil. He said the "185 credits" are exploration credits, "where you have to be over three miles away from another well." He relayed that all the bills the legislature has sent forward have extended those credits for 10 years. Chair Seaton said he does not want to complicate the bill by incorporating the amendments at present, but would like to see them ready for the House Finance Committee. He stated, "If ... the structure of our bill was incorporated with another tax rewrite, it's already going to have some provisions on heavy oil and ... exploration credits in there, so it would complicate the bill and need to be pulled out. If it would be a standalone backup position, then I'd like the committee to consider whether they want to forward these to [the House Finance Committee] for consideration so that the bill ... not only raises taxes but also extends those credits."

[8:35:43 AM](#)

REPRESENTATIVE GATTO said he has spoken with some Senators who support the bill.

REPRESENTATIVE MARK NEUMAN, Alaska State Legislature, commented that he likes the standalone feature of the bill, and he opined that it is a piece of legislation worthy of being passed on.

CHAIR SEATON expressed an interest in receiving a motion to send the amendments and cover letter along with the bill.

[8:37:23 AM](#)

REPRESENTATIVE GARDNER asked Chair Seaton to clarify what the advantage is in moving the bill out of committee without the amendments being adopted into it.

CHAIR SEATON explained:

The idea ... is: we have a very simple progressivity bill that could be incorporated with any other tax changes. If we incorporate these two amendments into the bill, it becomes more complicated. And any other bill that has been going forward is going to incorporate ... the credit portions, and then we would have to be pulling things out and adding them back in.

[8:38:19 AM](#)

CHAIR SEATON, in response to a request from Representative Gruenberg, read the letter of intent, which read as follows [original punctuation provided]:

Attached to this memorandum are two amendments that were reviewed by the House State Affairs Committee. The first amendment provides financial incentives for companies to develop their heavy oil resources. This amendment is based upon the concept presented in HB 498 sponsored by Representative Rokeberg during the regular session and worked on extensively by the House Resources committee.

The second amendment provides for an extension of the 185 exploration credits included in nearly every version of the PPT legislation to date.

These amendments were not adopted by the House State Affairs Committee, as an effort was made to keep HB 3005 as straightforward as possible. However, the amendments are being passed along with HB 3005 in the event that a more complete PPT package does not appear

likely to emerge during this special session. The House State Affairs Committee believes that heavy oil incentives, and the 185 credits should be included in whatever tax package finally passes the legislature, and would respectfully request the House Finance Committee to consider these amendments as another tool in the toolbox should they be needed.

8:39:58 AM

REPRESENTATIVE GRUENBERG said he was under the impression that the amendments would only be included "if this progressivity bill passes as a standalone bill." He said the letter is drafted in a such a way that sounds like the committee would like the amendments incorporated "regardless of whatever form the legislation takes." He concluded, "I thought that we were considering the main bill itself as a standalone bill, and so, if we do that and that's our premise, then we should only say that these amendments would be included if we only pass the main bill - the progressivity bill - and nothing else. Am I wrong in what I'm thinking we're doing here?"

8:41:21 AM

CHAIR SEATON responded that he thinks that is the intended effect. To address continued concern from Representative Gruenberg, he highlighted the sentence: "However, the amendments are being passed along with HB 3005 in the event that a more complete PPT package does not appear likely to emerge during this special session."

8:42:03 AM

REPRESENTATIVE GATTO raised the issue of possibly having to repeal legislation in the future.

CHAIR SEATON pointed out every time new legislation is considered, language that has come before is modified and/or deleted.

8:44:31 AM

REPRESENTATIVE GATTO moved that HB 3005 be forwarded to the House Finance Committee accompanied with a cover letter and amendments labeled, "24-LS1990\G.2, Bullock, 7/28/06" and "24-LS1990\G.3, Bullock, 7/28/06." There being no objection, the motion carried.

CHAIR SEATON noted that in the committee packet is a letter from the bill drafter that address a concern stated at a previous meeting regarding the bill's language.

CHAIR SEATON mentioned questions posed during the last bill hearing, and he drew attention to a handout in the committee packet that addressed the questions. The first question is: "Does progressivity 'take away all the upside?'" The handout explains the reason that the answer to that question is no, and Chair Seaton reviewed the answer with the committee. The second question is: "What is the purpose of HB 3005?" He reviewed the answer by reiterating his previous statements regarding the reason for HB 3005.

[8:50:10 AM](#)

CHAIR SEATON clarified that the previous motion that passed had been to send along the amendments and cover letter with the bill; it was not a motion to move the bill out of committee.

[8:50:41 AM](#)

REPRESENTATIVE GATTO moved to report HB 3005, as amended, out of committee with individual recommendations and the accompanying fiscal notes, along with the amendments and the letter.

CHAIR SEATON reminded Representative Gatto that the amendments that would accompany the bill to the House Finance Committee were not adopted, therefore the bill had not been amended. [Representative Gatto's motion was considered withdrawn].

REPRESENTATIVE GRUENBERG noted that HB 3005 does not deal with the repeal of ELF, thus he asked if the cover letter might also include a recommendation that "if they can't pass anything else, at least they repeal ... or do something with the ELF."

CHAIR SEATON said that would be beyond the scope of HB 3005. He indicated that other committee members concurred, stating, "I see a lot of heads shaking no here."

[8:52:11 AM](#)

REPRESENTATIVE GATTO moved to report HB 3005 out of committee with individual recommendations and the accompanying fiscal notes, along with the aforementioned attached amendments and

cover letter. There being no objection, HB 3005 was reported out of the House State Affairs Standing Committee.

8:52:46 AM

REPRESENTATIVE GRUENBERG stated that although he was not able to vote [due to his participating via teleconference], he would like the record to reflect that his "comments on the report sheet would have been a 'No recommendation.'"

8:53:22 AM

ADJOURNMENT

There being no further business before the committee, the House State Affairs Standing Committee meeting was adjourned at 8:53 a.m.