

**ALASKA STATE LEGISLATURE**  
**SENATE RESOURCES STANDING COMMITTEE**

March 27, 2006

3:42 p.m.

**MEMBERS PRESENT**

Senator Thomas Wagoner, Chair  
Senator Ralph Seekins, Vice Chair  
Senator Ben Stevens  
Senator Fred Dyson  
Senator Bert Stedman  
Senator Kim Elton  
Senator Albert Kookesh

**MEMBERS ABSENT**

All members present

**COMMITTEE CALENDAR**

SENATE BILL NO. 305

"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."

HEARD AND HELD

#### PREVIOUS COMMITTEE ACTION

BILL: SB 305

SHORT TITLE: OIL AND GAS PRODUCTION TAX

SPONSOR(S): RULES BY REQUEST OF THE GOVERNOR

02/21/06	(S)	READ THE FIRST TIME - REFERRALS
02/21/06	(S)	RES, FIN
02/22/06	(S)	RES AT 3:30 PM BUTROVICH 205
02/22/06	(S)	Heard & Held
02/22/06	(S)	MINUTE(RES)
02/23/06	(S)	RES AT 3:30 PM BUTROVICH 205
02/23/06	(S)	Heard & Held
02/23/06	(S)	MINUTE(RES)
02/24/06	(S)	RES AT 3:30 PM BUTROVICH 205
02/24/06	(S)	Heard & Held
02/24/06	(S)	MINUTE(RES)
02/25/06	(S)	RES AT 9:00 AM BUTROVICH 205
02/25/06	(S)	-- Reconvene from 02/24/06 --
02/25/06	(H)	RES AT 10:00 AM SENATE FINANCE 532
02/25/06	(S)	Heard & Held
02/25/06	(S)	MINUTE(RES)
02/27/06	(S)	RES AT 3:30 PM BUTROVICH 205
02/27/06	(S)	Heard & Held
02/27/06	(S)	MINUTE(RES)
02/28/06	(S)	RES AT 3:30 PM BUTROVICH 205
02/28/06	(S)	Heard & Held
02/28/06	(S)	MINUTE(RES)
03/01/06	(S)	RES AT 3:30 PM BUTROVICH 205
03/01/06	(S)	Heard & Held
03/01/06	(S)	MINUTE(RES)
03/02/06	(S)	RES AT 1:30 PM BUTROVICH 205
03/02/06	(S)	Heard & Held
03/02/06	(S)	MINUTE(RES)
03/02/06	(S)	RES AT 3:30 PM BUTROVICH 205
03/02/06	(S)	Heard & Held
03/02/06	(S)	MINUTE(RES)
03/03/06	(S)	RES AT 3:30 PM BUTROVICH 205
03/03/06	(S)	-- Meeting Canceled --
03/04/06	(S)	RES AT 10:00 AM SENATE FINANCE 532
03/04/06	(S)	Presentation by Legislative Consultants
03/06/06	(S)	RES AT 3:30 PM SENATE FINANCE 532

03/06/06 (S) Heard & Held  
 03/06/06 (S) MINUTE(RES)  
 03/07/06 (S) RES AT 3:30 PM BUTROVICH 205  
 03/07/06 (S) Heard & Held  
 03/07/06 (S) MINUTE(RES)  
 03/08/06 (S) RES AT 3:30 PM BUTROVICH 205  
 03/08/06 (S) -- Meeting Canceled --  
 03/09/06 (S) RES AT 3:30 PM BUTROVICH 205  
 03/09/06 (S) -- Meeting Canceled --  
 03/10/06 (S) RES AT 3:30 PM BUTROVICH 205  
 03/10/06 (S) -- Meeting Canceled --  
 03/11/06 (H) RES AT 10:00 AM CAPITOL 106  
 03/11/06 (H) -- Meeting Canceled --  
 03/13/06 (S) RES AT 3:30 PM BUTROVICH 205  
 03/13/06 (S) Heard & Held  
 03/13/06 (S) MINUTE(RES)  
 03/14/06 (S) RES AT 3:30 PM BUTROVICH 205  
 03/14/06 (S) Heard & Held  
 03/14/06 (S) MINUTE(RES)  
 03/15/06 (S) RES AT 3:30 PM BUTROVICH 205  
 03/15/06 (S) Heard & Held  
 03/15/06 (S) MINUTE(RES)  
 03/16/06 (S) RES AT 3:30 PM BUTROVICH 205  
 03/16/06 (S) -- Meeting Canceled --  
 03/17/06 (S) RES AT 3:30 PM BUTROVICH 205  
 03/17/06 (S) Heard & Held  
 03/17/06 (S) MINUTE(RES)  
 03/18/06 (H) RES AT 10:00 AM CAPITOL 124  
 03/18/06 (H) -- Meeting Canceled --  
 03/19/06 (S) RES AT 1:00 PM BUTROVICH 205  
 03/19/06 (S) Heard & Held  
 03/19/06 (S) MINUTE(RES)  
 03/20/06 (S) RES AT 3:30 PM BUTROVICH 205  
 03/20/06 (S) Heard & Held  
 03/20/06 (S) MINUTE(RES)  
 03/21/06 (S) RES AT 3:30 PM BUTROVICH 205  
 03/21/06 (S) -- Meeting Canceled --  
 03/22/06 (S) RES AT 10:00 AM BUTROVICH 205  
 03/22/06 (S) -- Testimony <Invitation Only> --  
 03/23/06 (S) RES AT 10:00 AM BUTROVICH 205  
 03/23/06 (S) Above Bill continued from 03/22/06 Mtg  
 03/24/06 (S) FIN AT 9:00 AM SENATE FINANCE 532  
 03/24/06 (S) <Pending Referral>  
 03/24/06 (S) RES AT 10:00 AM BUTROVICH 205  
 03/24/06 (S) Heard & Held  
 03/24/06 (S) MINUTE(RES)  
 03/25/06 (S) FIN AT 10:00 AM SENATE FINANCE 532

03/25/06 (S) -- Meeting Canceled --  
03/27/06 (S) RES AT 3:30 PM BUTROVICH 205

**WITNESS REGISTER**

JOE BALASH  
Staff to the Legislative Budget & Audit Committee  
Alaska State Capitol  
Juneau, AK 99801-1182  
**POSITION STATEMENT:** Commented on CSSB 305(RES).

**ACTION NARRATIVE**

**CHAIR THOMAS WAGONER** called the Senate Resources Standing Committee meeting to order at [3:42:20 PM](#). Present were Senators Ben Stevens, Stedman, Seekins, Dyson, Kookesh, Elton and Chair Wagoner.

**SB 305-OIL AND GAS PRODUCTION TAX**

CHAIR THOMAS WAGONER announced SB 305 to be up for consideration.

SENATOR STEDMAN moved to adopt CSSB 305(RES), Version I.

SENATOR BEN STEVENS objected.

CHAIR WAGONER said he didn't intend to adopt the CS today anyway and wanted to go through it thoroughly. He said they needed to finalize Administrative Amendment 1.

[3:45:24 PM](#)

SENATOR STEDMAN moved to adopt Amendment Y [sic].

**AMENDMENT Y**

OFFERED IN THE SENATE TO CSSB 305(RES), Version24-GS2052\I BY SENATOR WAGONER

Page 19, line 19-23: delete all material, insert:  
the use by another person of a production facility in which the producer has an ownership interest or the management by the producer of a production facility under a management agreement providing for the producer to receive a management fee;

Page 20, line 2: replace (o) with (n) and after "2006;" insert:

For purposes of this subsection, if a producer removes from the state, for use outside the state, an asset described in this subparagraph, the value of the asset at the time it is removed is considered a payment received by the producer for the transfer of the asset;

Page 22, line 13: insert "(b)," at the beginning of the line

Page 22, line 14: delete "or(d)(2)(0)"

Page 22, line 16: delete "(d)(2)(N) or (d)(2)(0)" and insert (e)(3)(A)

Page 22, lines 27 - 28: after due: delete all material and insert:

If a producer fails to comply with a request under this paragraph, there shall be added to any underpayment determined by the department under this section a penalty in the amount of 5 percent of the underpayment.

Page 22, line 29, through Page 23, line 11: delete all material and reorder

Page 23, lines 12 - 14: delete all material and insert:

(n) For purposes of determining the amount of the adjustment by subtraction that must be made to a producer's lease expenditures as a result of the producer's receiving a payment or credit under (e)(3)(A) of this section,

Page 23, lines 22 - 26: delete all material and reorder

SENATOR BEN STEVENS objected for a point of order and asked if they were adopting an amendment to a work draft that hadn't been adopted yet.

CHAIR WAGONER said he was correct.

SENATOR STEDMAN withdrew his motion.

SENATOR BEN STEVENS asked if the amendment addressed Version I.

3:46:44 PM

JOE BALASH, staff to the Legislative Budget & Audit Committee, replied that was correct. "What you have in front of you is Administrative Amendment 1 as approved and with the references corrected to correspond to the I version of the CS."

3:47:14 PM

SENATOR BEN STEVENS called a point of order saying that it looked like Version I already incorporated the changes.

CHAIR WAGONER said that was right even though that wasn't requested. He asked Mr. Balash if that was his recollection.

MR. BALASH replied that two references were corrected in Version I from revised Administrative Amendment 1 on lines 3 - 8 without direction. The rest of the items the committee did not take action on were not addressed in the course of drafting. He said the page and lines are different, but the text is the same.

SENATOR BEN STEVENS said he needed time to comprehend what had been done.

3:53:19 PM

CHAIR WAGONER said the amendment he was offering was similar to Senator Stevens' amendment that he offered on March 24. The only difference is he inserted the following language:

If the commissioner completes a detailed fiscal analysis and determines that an election by a producer under this subsection would serve the long-term fiscal interests of the state.

He said it leaves the RSAs [royalty settlement agreements] in the process and goes back to the language in the governor's bill.

SENATOR BEN STEVENS compared page 14, line 7 of Version I, with line 9 of the amendment and said that language in (1) and (2) seemed redundant.

CHAIR WAGONER said he tried to use the text in Senator Stevens' amendment [Y.23].

SENATOR ELTON said he didn't think they could amend an amendment to a bill they hadn't adopted.

CHAIR WAGONER explained that Senator Stevens asked for a review of the amendments.

SENATOR STEDMAN said his amendment, I.2, addressed the progressivity formula and that, "if the ANS West Coast price per barrel of oil during the month exceeds \$40" was the trigger for the escalator. That language clarifies that it's an average price per month. Line 13 had a drafting error in the definition of what the PPT is and said "property tax" instead of "profit tax".

[4:04:42 PM](#)

SENATOR SEEKINS asked if the motion is to adopt this as a working document, not a final document.

CHAIR WAGONER replied yes, and then they would put the two amendments into it. That would be part of the final presentation.

SENATOR STEDMAN went to page 21, line 8, [of Version I] that referenced the 55,000 barrels, and asked the committee to carefully consider the formula on line 14. He asked them to remember that the escalator calculation imbedded on line 14 is an after tax rate. So members should make sure that the bill doesn't create an ability to get a double deduction on the escalator portion, because it's already built into the formula.

CHAIR WAGONER said he had found another problem and they would talk about it on Wednesday.

SENATOR SEEKINS called the question on adopting the working draft.

SENATOR BEN STEVENS objected. Senators Dyson, Stedman, Elton, Kookesh, Seekins, and Wagoner voted yea; Senator Ben Stevens voted nay; so CSSB 305(RES), Version I, was adopted as a working draft.

[4:09:03 PM](#)

SENATOR SEEKINS moved to adopt amendment I.1.

24-GS2052\I.1  
Chenoweth

AMENDMENT I.1

OFFERED IN THE SENATE

BY SENATOR WAGONER

TO: CSSB 305(RES), Draft Version "I"

Page 14, lines 3 - 27:

Delete all material and insert:

"(d) Under regulations adopted by the department, if the commissioner completes a detailed fiscal analysis and determines that an election by a producer under this subsection would serve the long-term fiscal interests of the state, the department may allow a producer, subject to limitations prescribed by the department as to the frequency of making elections, to elect prospectively to calculate the gross value at the point of production of oil or gas based in whole or part on

(1) a royalty value determined under a royalty settlement agreement between the producer and the state, with adjustments if appropriate;

(2) a formula prescribed by the department that uses, with adjustments if appropriate, a royalty value or valuation methodology accepted by the

(A) Department of Natural Resources under AS 38.05, in the case of oil and gas produced from a lease issued by the Department of Natural Resources or produced from a lease or property that is part of a unit approved by the Department of Natural Resources; or

(B) United States Department of the Interior under applicable federal oil and gas leasing statutes, in the case of oil and gas produced from a lease issued by the United States Department of the Interior that is not part of a unit approved by the Department of Natural Resources, or produced from a lease or property that is part of a unit approved by the United States Department of the Interior but not approved by the Department of Natural Resources; or

(3) another formula prescribed by the Department of Revenue that reasonably estimates a value for the oil or gas at a specific geographical location such as the point of tender or delivery into a common carrier pipeline; the formula may use factors such as published price indices for oil or gas in or outside the state, quality differentials for oil or gas, transportation costs between markets, and inflation adjustments."

CHAIR WAGONER objected.

SENATOR BEN STEVENS moved a friendly amendment to delete lines 9 and 10 on page 1 of Amendment I.1 because they are redundant and then renumber appropriately. There were no objections and the motion carried.

CHAIR WAGONER noted there was no further discussion and he removed his objection to Amendment I.1. Without further objection Amendment I.1 am was adopted.

[4:11:53 PM](#)

SENATOR SEEKINS moved Amendment I.2.

24-GS2052\I.2  
Chenoweth

### AMENDMENT I.2

OFFERED IN THE SENATE

BY SENATOR STEDMAN

TO: CSSB 305(RES), Draft Version "I"

Page 4, lines 15 - 23:

Delete all material and insert:

"(g) In addition to the taxes levied under (e) and (f) of this section, if the average ANS West Coast price per barrel of oil during a month exceeds \$40, there is levied on the producer of oil a tax for oil produced during that month from each lease or property in the state, less any oil the ownership or right to which is exempt from taxation. The tax levied under this subsection is equal to

[((ANS West Coast price - \$40) x .002) x [ANS  
wellhead price x (1 - PPT rate)]]  
x (total taxable barrels of oil at the point of  
production)

where

(1) "ANS wellhead price" means the prevailing value for oil produced in the Alaska North Slope area; and

(2) the PPT, or production property tax, rate is 25 percent."

CHAIR WAGONER objected for discussion.

SENATOR STEDMAN explained how the intent was to clarify what was already in the bill, so they could focus on the escalator, its trigger and slope. He said line 3 of the amendment inserts new language that says, "if the average ANS West Coast price per barrel of oil during a month exceeds \$40," and the \$40 is the trigger. Also the formula had some potential differences of opinion on what it applied to; so, on line 9 the formula was added after the dollar amount of tax was calculated, so one can see exactly what it applies to, which is total taxable barrels of oil at the point of production. Brackets were added so that mathematics were cleaner. A drafting error on line 13 was corrected where the word "property" was inadvertently used in the definition of PPT instead of "profit".

SENATOR SEEKINS stated for the record that his motion included inserting "profit" instead of "property" on line 13 and that he was voting for the amendment to establish the formula, not necessarily to establish the values on lines 4, 8, and 13.

SENATOR STEDMAN said that they were working on the structure and clearly until the bill is finished the tax rate, the trigger dollar amount and the slope were all open for discussion.

SENATOR BEN STEVENS maintained his objection because line 8 used the ANS wellhead price as the taxation on the PPT rate versus the ANS West Coast price. He argued, "Again if we're going to use a tax derived from a tax, it should be based on the same valuation methodology." He also opposed continuing to calculate the progressivity clause as tax deductible, but there is no provision written in the amendment or bill that makes the additional tax derived under Section 011(g) tax deductible from the PPT.

SENATOR STEDMAN said on line 8 it says "(1-PPT rate)"; that is where you get the effect of the tax deductibility. In other words it is imbedded in the formula; so it can't be deducted again.

SENATOR BEN STEVENS said he didn't interpret it that way; he saw the formula was calculated to say that it is deductible, but the director of the Tax Division stated on Friday that it wasn't deductible. He still maintained his objection, which he said he had registered earlier.

[4:17:37 PM](#)

SENATOR SEEKINS said he wanted someone from the Department of Revenue to assure him that deductibility was being accounted for in the formula.

SENATOR SEEKINS moved to table the amendment until Wednesday. Senators Ben Stevens and Seekins voted yea; Senators Elton, Kookesh, Dyson and Stedman voted nay; so the motion failed.

CHAIR WAGONER said the voted didn't preclude that from happening and he would get someone to do that.

4:20:17 PM

CHAIR WAGONER asked if there was further discussion on Amendment I.2. He asked for a roll call vote. Senators Kookesh, Dyson, Stedman, Elton, and Wagoner voted yea; Senators Ben Stevens and Seekins voted nay; so Amendment I.2 was adopted.

4:22:00 PM

CHAIR WAGONER said that Senator Ben Stevens asked to bring up Amendments Y.18 and Y.24 at a later date. He noted that Y.18 is on page 10, line 25-27 of Version I and in conjunction with that, a memo from Don Shepler dated March 19.

SENATOR BEN STEVENS noted, as a point of procedure, the date of the memo is March 19 and this is the first time anyone has seen it.

CHAIR WAGONER responded that's why he thought they might want to wait and take this amendment up with the administrative amendment.

SENATOR BEN STEVENS said again that he needed more time to absorb this language.

CHAIR WAGONER said it would be okay to set Amendment Y.18 aside until Wednesday.

SENATOR SEEKINS tried to understand the question, which he thought was if the construction costs of the gas treatment plant are allowed to be deducted under the PPT, could those same costs be used in establishing a tariff on the downstream construction of a pipeline provided that the same entity owns the pipe and is the builder of the gas treatment plant that was applying for a tariff rate from FERC.

4:26:45 PM

SENATOR BEN STEVENS agreed with Senator Seekins' understanding of the question, but he thought section (h) needed clarification on page 10, line 11. It said:

(h) A producer or explorer may not elect to take a tax credit under this section for a lease expenditure under AS 43.55.160 that is an expenditure incurred for - directly related to a pipeline facility or assets that's regulated by either FERC or the RCA."

He wanted to know how many assets on the North Slope are currently under FERC or the RCA and if in inserting this provision the state is excluding a large part of the infrastructure that is already there or will be built for future oil production from the 20 percent credit.

That's why I have concern over this - if we're going to exclude facilities from the 20 percent credit. I don't have the answer to that because it's my understanding that there are several feeder lines from satellite fields that are regulated under the RCA for existing production. And if they are there for existing production, then they will probably be there if we bring on new satellite fields for oil and not just oil, but also gas....

SENATOR SEEKINS added that reflected his concern as well. He wanted to determine where the PPT starts and stops as well as where the tariff starts. He wasn't sure which assets fell in the category under lines 25-27 on page 10 [Version I].

CHAIR WAGONER said the other amendment was Y.24 and that was now on page 18, line 10 of Version I.

SENATOR BEN STEVENS said in Version I, Amendment Y.24 deals with language that is inserted all the way down to page 24, line 8 where the 470 Fund begins. He said the new version has substantial new language and he would like time to see it - specifically new language in section (i) on page 21, line 20, and sections (n) and (o) on pages 22 and 23.

SENATOR DYSON asked Senator Stevens to summarize what he intended to accomplish with this amendment.

SENATOR BEN STEVENS replied his intent was to take the provisions back to the original version of SB 305, which says the costs for third-party transactions or arm's length

transactions are allocated under ordinary and necessary costs provided under the U.S. IRS provision. The current limitation says there is already a system in place that says how arm's length transactions are dealt with. The evolving language is all about arm's length transactions and relates to some IRS code and it's more restrictive and he questioned whether it was more effective.

He highlighted again that (n) on page 22 and (o) on page 23 had been substantially changed and the definition of "necessary and ordinary" in section (p) had been entirely removed. He stated that Mr. Chenoweth's memo said (p) was removed from the bill, but in reality, language on page 16, line 12, allows necessary and ordinary costs for exploring for gas deposits, but not for producing. "Again there is some delineation between costs associated with production versus costs associated with ongoing development or production."

[4:36:19 PM](#)

CHAIR WAGONER related a thumbnail sketch of why the legislature went through the process it did. One of the legislature's hired tax consultants said that these changes were necessary in order to give the administration another tool in its toolbox to stop any gaming in the tax area of different processes they can go through for pieces of equipment et cetera.

[4:36:59 PM](#)

SENATOR DYSON said it was his intention for the legislature to do the best it can to give incentives for new production and new exploration and not allow producers to write off work they do that just maintains old production.

[4:38:38 PM](#)

CHAIR WAGONER said the administration sent a letter to the legislature that addressed that and he distributed it in the last meeting. He felt the changes just allowed the administration more tools in the toolbox to avoid that from happening and it was the legislature's policy call.

SENATOR DYSON recalled it was the administration's intent to not give incentives for maintaining existing production.

CHAIR WAGONER said he couldn't say one way or the other.

SENATOR BEN STEVENS said his interpretation of the bill is that investments for maintaining production do qualify. There is no difference between enhanced oil recovery production, a

development of an existing field or exploration for the 20 percent credit.

SENATOR SEEKINS agreed with Senator Stevens' interpretation.

SENATOR BEN STEVENS went back to page 20, line 31, through page 21, lines 1 - 3 and said it was his understanding that was going to be deleted. He explained that it was a limitation on the \$40 in the transition.

CHAIR WAGONER replied yes, he was right. On another note, he said the report came back from DEC showing what the different funding levels do in the 470 Fund.

[4:43:35 PM](#)

SENATOR ELTON said he had a feeling that Y.18 and Y.24 were going to be offered again and asked if the committee could have the new line references on Wednesday.

CHAIR WAGONER agreed.

SENATOR BEN STEVENS said the entire sections of (h) through (o) in Version Y are changed substantially in Version I. He said his amendments would address the previous version, since Version I hadn't been adopted, and would take the bill back to the original version.

CHAIR WAGONER noted there was no further discussion and recessed the meeting at [4:45:40 PM](#) to a call of the chair on Wednesday.