

**ALASKA STATE LEGISLATURE**  
**HOUSE SPECIAL COMMITTEE ON FISHERIES**

January 25, 2008

8:39 a.m.

**MEMBERS PRESENT**

Representative Paul Seaton, Chair  
Representative Kyle Johansen  
Representative Gabrielle LeDoux  
Representative Peggy Wilson  
Representative Bryce Edgmon  
Representative Lindsey Holmes

**MEMBERS ABSENT**

Representative Craig Johnson

**COMMITTEE CALENDAR**

HOUSE BILL NO. 321

"An Act relating to the salmon product development tax credit; providing for an effective date by amending an effective date in sec. 7, ch. 57, SLA 2003, as amended by sec. 4, ch. 3, SLA 2006; and providing for an effective date."

- MOVED CSHB 321(FSH) OUT OF COMMITTEE

**PREVIOUS COMMITTEE ACTION**

BILL: HB 321

SHORT TITLE: SALMON PRODUCT DEVELOPMENT TAX CREDIT

SPONSOR(S): REPRESENTATIVE(S) THOMAS

01/16/08	(H)	READ THE FIRST TIME - REFERRALS
01/16/08	(H)	FSH, FIN
01/25/08	(H)	FSH AT 8:30 AM BARNES 124

**WITNESS REGISTER**

IAN FISK, Staff  
Representative Bill Thomas  
Alaska State Legislature  
Juneau, Alaska

**POSITION STATEMENT:** Presented HB 321 on behalf of the sponsor, Representative Thomas.

TIM COTTONGIM, Fish Group Manager  
Juneau Office  
Tax Division  
Department of Revenue (DOR)  
Juneau, Alaska

**POSITION STATEMENT:** During hearing of HB 321, answered questions.

MARY MCDOWELL, Vice President  
Pacific Seafood Processors Association (PSPA)  
Juneau, Alaska

**POSITION STATEMENT:** Testified in support of HB 321.

MARK PALMER, President  
Ocean Beauty Seafoods, Inc.  
Seattle, Washington

**POSITION STATEMENT:** Characterized HB 321 as a real incentive for companies to invest in a seasonal operation.

TOM SUNDERLAND, Marketing Director  
Ocean Beauty Seafoods, Inc.  
Seattle, Washington

**POSITION STATEMENT:** Testified that the tax credit in HB 321 helps with the decision to make an investment.

TIM BLOTT, Manager  
Cook Inlet Processing Plant  
Ocean Beauty, Inc.  
Kodiak, Alaska

**POSITION STATEMENT:** During hearing of HB 321, testified as to the impact of the tax credit at the Cook Inlet Processing Plant.

JULIE DECKER, Representative  
Wrangell Seafoods, Inc.  
Wrangell, Alaska

**POSITION STATEMENT:** During hearing of HB 321, urged the committee to extend the tax credit.

#### **ACTION NARRATIVE**

**CHAIR PAUL SEATON** called the House Special Committee on Fisheries meeting to order at [8:39:16 AM](#). Representatives Seaton, Johansen, LeDoux, and Edgmon were present at the call to order. Representatives Holmes and Wilson arrived as the meeting was in progress.

HB 321-SALMON PRODUCT DEVELOPMENT TAX CREDIT

8:39:42 AM

CHAIR SEATON announced that the first order of business would be HOUSE BILL NO. 321 "An Act relating to the salmon product development tax credit; providing for an effective date by amending an effective date in sec. 7, ch. 57, SLA 2003, as amended by sec. 4, ch. 3, SLA 2006; and providing for an effective date."

8:41:36 AM

IAN FISK, Staff, Representative Bill Thomas, Alaska State Legislature, offered to provide the committee with a brief summary of HB 321.

REPRESENTATIVE EDGMON moved to adopt CSHB 321, Version 25-LS1285\M, Kane, 1/23/08, as the working document. There being no objection, Version M was before the committee.

MR. FISK explained that the salmon product development tax credit is basically an incentive to add value to Alaska salmon in Alaska. The credit will expire on December 31, 2008, and thus this legislation would extend that credit to December 31, 2011. The credit applies to the fisheries business tax, which is a tax levied on the ex-vessel value of fisheries resources at the point of first sale. The point of sale is usually when the fish is transferred from a fishing vessel and purchased by a processor. The program allows a claim of up to 50 percent of the cost of qualified investments in new property. He noted that there are several restrictions, including that the property must be new, used predominantly for salmon, and used for value-added salmon.

MR. FISK reminded the committee that this credit was implemented in 2003 when there was a severely depressed salmon market, which was mainly due to the influx of farmed salmon. He opined that this credit is a critical part of helping the industry retool and modernize. For example, less product is going into the older tall cans and more are left in fillets. Furthermore, there has been an increased diversity of products, which is important with customer acceptance of salmon. He highlighted other important trends, as follows: increase in the average value; increase in state revenues from the fisheries business tax, and an increase of permit values for salmon. Therefore,

the sponsor strongly believes the credit should be renewed for an additional three years, he related.

MR. FISK then turned to Version M and directed the committee's attention to the new language on page 2, lines 11-15, which includes conveyors as a type of eligible equipment. This new language will allow [the credit to be used for] conveyors that meet the other qualifications for equipment and specifically used in the act of producing salmon value-added products. The Department of Revenue (DOR) wanted to be sure there is no confusion, and thus requested the inclusion of language specifying that conveyors not used specifically in the act of producing value-added salmon are ineligible. Mr. Fisk then pointed out that Version M in Section 3 on page 2 inserts a new subsection such that a processor can obtain a preliminary determination of eligibility from DOR when that processor considers the purchase of new equipment.

[8:46:59 AM](#)

CHAIR SEATON related his understanding that the change related to conveyors is meant to be a change going forward not a retroactive change.

MR. FISK answered that is his understanding. In further response to Chair Seaton, Mr. Fisk confirmed that the sponsor's intent is for this change related to conveyors to be in place from this point forward.

REPRESENTATIVE JOHANSEN inquired as to the reasoning behind the preliminary determination of eligibility, and asked if there have been problems.

MR. FISK, recalling conversations with those in the industry, related that it has occasionally been an issue and thus the preliminary determination of eligibility is a logical clarification.

[8:48:36 AM](#)

CHAIR SEATON highlighted that the committee packet includes information regarding the salmon product development tax from the Tax Division. He directed attention to the second page in which the salmon product development expenditure categories relate that the fillet line is a non-qualified expenditure. He inquired as to the sponsor's view of that.

MR. FISK related that the sponsor would consider that the fillet line should be a qualified expenditure.

8:50:05 AM

TIM COTTONGIM, Fish Group Manager, Juneau Office, Tax Division, Department of Revenue (DOR), pointed out that the first page of his document titled "Salmon Product Development Tax Credits" reflects the total number of companies that have claimed the credit through 2006. The document also specifies the total development expenditures as well as the total development credits, which amount to approximately 50 percent of that amount being claimed on the fisheries business tax return. He pointed out that the numbers related to the credits denied at audit are tentative numbers as there are some ongoing audits. The second page titled "Salmon Product Development Expenditure Categories" relates the Tax Division's interpretation of existing statute as related to qualified expenditures versus non-qualified expenditures. With regard to the filleting line, the sponsors discussed the intent for the credit to be used to encourage new investments and new value-added salmon products. He related his understanding from the original language that the credit was for equipment that performed the functions of processing, packaging, and product finishing. The renewal of the credit in 2006 was referred to as a need to modernize the industry. Therefore, the division considered only the equipment performing the processing, packaging, and product finishing functions as qualifying for the credit. Mr. Cottongim explained that when the division refers to a filleting line it refers to non-machines; it refers to a conveyor belt or table of some sort where individuals are hand filleting. As mentioned earlier, the filleting line would be a non-qualified expenditure whereas a filleting machine would be a qualified expenditure. He then directed attention to the page titled "Salmon Product Development Tax Credits Denied", which relates general reasons why the credit was denied.

MR. COTTONGIM turned his attention to Version M, specifically related to conveyors. He stated his appreciation for Chair Seaton's clarification that this will simply be a change going forward. However, he expressed concern with regard to the lack of specificity as it would likely result in some confusion by taxpayers. Therefore, expressed the division's willingness to work with the committee to make the language more specific as to the meaning of conveyors as used in the legislation.

REPRESENTATIVE JOHANSEN inquired as to the process used to determine whether an expenditure is qualified or non-qualified. He further inquired as to how often this occurs and how it's coordinated with the processors.

[8:56:14 AM](#)

MR. COTTONGIM, in response to Representative Johansen, explained that the division inspects processing equipment, it determines how the equipment is used, requests information about the amount of products produced as well as for which types of species the equipment is used. The division checks the manufacture date on the equipment in order to confirm it is new and compare it to invoices and shipping documents to confirm that it was first placed in service in Alaska. The division, he related, determines whether it's a qualified or non-qualified expenditure based on whether the equipment isn't performing a processing, packaging, or product finishing function. In further response to Representative Johansen, Mr. Cottongim said that the determination of what [expenditures] are qualified or non-qualified is reviewed on a case-by-case basis in each audit. The division recognizes that each company has unique equipment and processing. Therefore, the division hasn't really attempted to fit a particular item into a compartment and leave it there. The list provided is a running list, he noted.

[8:58:30 AM](#)

REPRESENTATIVE EDGMON inquired as to what Mr. Cottongim would suggest to make the language related to conveyors more concise.

MR. COTTONGIM clarified that the division's concern is in regard to what is meant by the language "in the act of producing" on page 2, line 15. "Whether or not you consider the act of producing and where that starts and where that ends." For example, totes are an item that folks have wanted to claim as a credit. The reasoning was that the totes are necessary to move the fish to the processing lines, and thus totes are important in the act of producing the value-added salmon product.

CHAIR SEATON recalled his time sitting on the Joint Legislative Salmon Task Force which referred to value-added as the product and doing something to the fish in order to achieve a value-added processing, not merely eliminating people in the process. He opined that the [goal] is to achieve quality, diversity in the product line, and more employment in Alaska, although the law seems to indicate that [value-added] only counts if people

are eliminated. The credit is trying to stimulate behavior in which a company invests in equipment that changes the product from an unfinished product to a finished product or changes the product. In fact, he opined that a company that develops a value-added product would ultimately employ more Alaskans over a longer period of time. The aforementioned, he further opined, is the most desirable end in value-added processing. "It's not just for a company, it's the effect of taking that round product and further processing it in Alaska, for Alaskans in Alaskan communities," he commented.

CHAIR SEATON then pointed out the photos included in the committee packet. These photos are of a fillet line in a plant in Kasilof. He drew the committee's attention to the photos of the conveyor belt upon which the fillets can be cut. As the photos illustrate, the conveyor belt is used in conjunction with hydraulic stools that adjust to the various heights of the employees. Although this provides a value-added product, this setup would be denied as a conveyor belt due to the interpretation of conveyor belt. Therefore, the language in HB 321 attempts to clarify that even when people are used with equipment specifically designed for the value-added processing if it's integral to the value-added process, it's a qualified expenditure.

[9:05:11 AM](#)

MR. COTTONGIM related that the fillet line, conveyor system language Chair Seaton spoke of would be helpful to the department.

REPRESENTATIVE JOHANSEN commented that lawmakers are frustrated when the department has broad leeway with regard to the interpretation of statute and writing regulations. In this case, Representative Johansen opined that if the department is going to review [the expenditures] on a case-by-case basis, the existing language is fine.

REPRESENTATIVE EDGMON stated that the terms "specifically" and "in the act of producing" seem to provide the division with the aforementioned leeway. He asked if it would be simpler to say "conveyors used to produce value-added salmon product".

[9:08:36 AM](#)

CHAIR SEATON interjected that the intent of the legislation [is to qualify the expenditure] for something that is integral to

the value-added product processing, such as conveyors with specialized cutting belts.

CHAIR SEATON noted that the committee packet includes letters of support from Wrangell Seafoods, Alaska General Seafoods, Icicle Seafoods, Peter Pan Seafoods Inc., Alaska Glacier Seafoods Inc, and Inlet Fish Producers, Inc.

REPRESENTATIVE JOHANSEN asked if Version M was drafted on behalf of the sponsor's request.

CHAIR SEATON relayed that the sponsor's staff indicated that to be the case.

[9:10:38 AM](#)

MARY MCDOWELL, Vice President, Pacific Seafood Processors Association (PSPA), informed the committee that PSPA is a trade association that has been in existence since 1914 to represent Alaska seafood processing companies. Peter Pan Seafoods Inc., Alaska General Seafoods, and North Pacific Seafoods, all members of PSPA, are salmon processors that have made use of the tax credit program to develop and expand new and value-added salmon products, to help Alaska's salmon products keep pace with evolving consumer demands, and keep Alaska's fisheries competitive in world markets. The legislature constructed this tax credit very tightly in order to specifically meet certain goals. However, there remains much more to do to maintain the momentum and ensure that Alaska's products are holding their place in the world market. Currently, the skyrocketing cost of energy is a large impediment for companies trying to make investments [to achieve value-added products]. For the most part processors operate in rural Alaska, where energy costs and needs are the highest. Those energy costs are eroding much of the profit margins that could otherwise go into this activity. Therefore, this tax credit bridges that gap so that the companies can make the investment and value to every pound of processed salmon.

MS. MCDOWELL acknowledged that the legislature is grappling with how to best use and invest the increased revenues the state has at this time. She opined that the extension of the salmon tax credit is the type of investment the state should make with those increased revenues. Ms. McDowell emphasized that HB 321 promotes economic diversification, preparing for the future, ensuring that Alaska's products are competitive worldwide, all while making the best possible use of the state's natural

resources. She characterized this investment as one that would provide high returns for the state in the future. In conclusion Ms. McDowell related support for HB 321 and its quick passage.

CHAIR SEATON asked if the PSPA generally agrees that value-added product is desired "or only if it's mechanically done."

MS. MCDOWELL said that although she hasn't had that specific [discussion] with PSPA members, everyone would fully agree that adding value is the intent whether people or machines are used to do so. She remarked that the idea of employing more people in the industry has a benefit to the state.

[9:17:13 AM](#)

MARK PALMER, President, Ocean Beauty Seafoods, Inc., informed the committee that Ocean Beauty Seafoods, Inc. (Ocean Beauty) is an Alaskan corporation with seven processing plants in Alaska operating from Southeast Alaska through Bristol Bay. The core product of the company is salmon. Recently, 50 percent of the company has been acquired by the Bristol Bay Economic Development Corporation (BBEDC), and therefore the company is a partner with the community development quota (CDQ) group. With regard to adding value, particularly in relation to salmon, there are many competing interests regarding where that can be achieved. "It's a big decision for a company to make to invest in a value-added product line; it's very much the tip of the iceberg when you make a decision to invest in value-added product in Alaska," he related. In fact, this summer Ocean Beauty will put a fillet line in its Naknek facility, the cost of which will be over \$2.5 million. The cost is for the equipment as well as the 45 more employees required to operate the fillet line. Furthermore, additional space in bunkhouses and mess halls will have to be constructed. Most of the facilities are in remote locations where the company generates its own power at the site. Therefore, extra power has to be generated when new equipment is installed. All of the aforementioned, he pointed out, fall outside the scope of this legislation. This legislation, however, is a real incentive for companies to invest in a seasonal operation.

MR. PALMER noted that although the intent with HB 321 is to add value to the salmon and benefit harvesters, it has impacted the type of folks companies employ and the training provided. The [credit] has worked wonderfully, but Ocean Beauty still has facilities that haven't directly benefitted from this [credit]. This legislation expedites many of the plans Ocean Beauty would

like to do. Mr. Palmer opined that Ocean Beauty has had a positive impact on the market with regard to new products, such as with prepared frozen foods and smoked products. The aforementioned has made a difference as the industry was really struggling five years ago when pink salmon was an albatross. Although the last two years have been big pink salmon years, there has been no carry-over can pack and the value has tripled to the harvester.

REPRESENTATIVE WILSON related her understanding that it's often difficult to fill the conveyor jobs with Alaskans. She then inquired as to how many of Ocean Beauty's [conveyor positions] are filled by Alaskans.

MR. PALMER informed the committee that Department of Labor & Workforce Development data specifies that of the major [companies in the industry], Ocean Beauty had the highest percentage of Alaska hire. He noted that Ocean Beauty lists over 300 jobs with the department, which was able to fill a large percentage of those.

[9:22:36 AM](#)

REPRESENTATIVE JOHANSEN said it's important to recognize the impact of the construction and creation of facilities, which reach beyond the fishing industry as electricians and carpenters are hired.

MR. PALMER confirmed that [Ocean Beauty] does hire many contractors for support.

REPRESENTATIVE LEDOUX asked if any of the new equipment is creating new jobs.

MR. PALMER explained that this past summer Ocean Beauty was awarded a step grant from DLWD and flew two technicians from Germany to conduct training for resident Alaskan employees. Therefore, there are at least four new jobs in Kodiak as a result of the aforementioned. He then related that the locations where certain equipment has been installed has required the training and hiring of staff to perform the maintenance. He noted that the aforementioned are good paying jobs that require skills that translate well to other fisheries around the state beyond salmon.

REPRESENTATIVE LEDOUX recalled that the technicians mentioned earlier earn \$100,000 annually. She asked if regular processors can be trained to perform that work.

MR. PALMER answered that for the most the work force comes from machinists for which there is an apprenticeship program.

[9:25:46 AM](#)

TOM SUNDERLAND, Marketing Director, Ocean Beauty Seafoods, Inc., explained that he is responsible for reviewing the market and what Ocean Beauty manufactures in order to determine how the two align. For many years the salmon industry in Alaska was well aligned. However, it's always changing. In fact, there have been many changes over the past 5-10 years. Mr. Sunderland related that his job is to be prepared in advance of these [changes] and determine the direction the company should take. He explained that innovation in industrial manufacturing almost always means more money is necessary due to the need for equipment, labor, or both. As the market changes, [companies] are forced to innovate and thus spend money. The salmon business, in particular, is a seasonal business and thus there the difficult question regarding how much investment makes sense arises. Over the past 15 years, many companies have struggled and failed. He highlighted that the market for pink salmon is doing extremely well. The growth in the pink salmon value has been coincidental with this tax credit. However, much of Ocean Beauty's ability to make a product that the market responds to is the result of the investment; the tax credit helps with the decision to make the investment.

[9:29:32 AM](#)

MR. SUNDERLAND related that [with the tax credit] Ocean Beauty can take the necessary steps to innovate. That innovation requires jobs with high pay and transferable skills. Mr. Sunderland then showed the committee various new products of Ocean Beauty, which he opined couldn't have existed before. The tax credit has helped the company's ability to be ahead of the market in regard to what consumers are demanding. He opined that although the market conditions for salmon are better, the industry is still quite fragile. Therefore, it's reason to continue the tax credit, he remarked. Moreover, the tax credit does generate an excellent return on the investment for the state.

[9:33:03 AM](#)

REPRESENTATIVE LEDOUX inquired as to how much Ocean Beauty has invested in this new equipment in order to produce the product he showed the committee. She also inquired as to how much the company would've invested had the tax credit not been available.

MR. SUNDERLAND deferred to Mr. Palmer with regard to the exact number of dollars. However, he said that without these tax credits and the ability to install equipment and thus change the method of cutting fish, the product would simply not exist.

REPRESENTATIVE LEDOUX questioned why Ocean Beauty wouldn't, without the credit, have installed the equipment since the market is calling for the product.

MR. SUNDERLAND answered that the company wouldn't have had the ability to do it because the company wouldn't have the ability to fill the orders to treat the fish in a certain manner without having the equipment in place. The difficulty for the company is if the market demands something that the company can't afford. If the company can't afford to purchase and install the equipment, the company can't meet the market demands. In the past 10-15 years that's been the case in the salmon business. To simply manufacture the product and to change the processes comes at a large initial cost. Furthermore, amortizing the cost over a short fishery is difficult to justify. This legislation provides a much better chance at a payoff.

[9:36:12 AM](#)

TIM BLOTT, Manager, Cook Inlet Processing Plant, Ocean Beauty, Inc., informed the committee that he has been plant manager at the Cook Inlet Processing Plant for six years now. He recalled that when he first arrived, the plant was a traditional salmon packer. In the last three to four years, the plant has progressively expanded production such that the plant began doing fillets with high-tech pin bone removal equipment. Last year, the plant began producing skinless, boneless, canned salmon. This year, the plant will produce skinless, boneless, vacuum-packed salmon. The aforementioned is what the tax credit has allowed. With regard to whether the aforementioned would've been done without the tax credit, he opined that it probably would have since it's market driven. The tax credit, however, has allowed the companies to get into the market faster. He then recalled questions regarding labor, and related that the plant still produces traditional canned salmon, it merely has added new lines that also require a labor force. Therefore, the

labor force has expanded. The equipment for the new lines is highly technical and step grants have been received in order to train staff. Furthermore, there is an ongoing apprentice program from which the staff from the machinists train [on the new equipment] and processing staff train to go into the machinist ranks. Kodiak is fortunate in that [the plant] has 100 percent local hire. To the question of the conveyors, Mr. Blott informed the committee that the conveyor is used only for salmon.

CHAIR SEATON surmised that the tax credit has allowed for a faster change in behavior than the industry would have otherwise.

MR. BLOTT noted his agreement.

[9:40:30 AM](#)

MR. BLOTT, in response to Representative Edgmon, speculated that the conveyor belt language was included to specifically address the conveyor currently used in the Cook Inlet Processing Plant. He confirmed that the conveyor belt is used only for value-added salmon products.

[9:41:29 AM](#)

JULIE DECKER, Representative, Wrangell Seafoods, Inc., informed the committee that Wrangell Seafoods, Inc. is a smaller processor for which this tax credit can be even more important, in terms of the ability to make these investments. She related that the vast majority of Wrangell Seafoods, Inc. revenue is from salmon. In 2007, Wrangell Seafoods, Inc. invested in a complete overhaul of its plant in order to update and expand its equipment to produce value-added product in conjunction with Wrangell's new cold storage facility. Ms. Decker urged the committee to extend the tax credit as there is still much room to grow for the processors in Alaska.

CHAIR SEATON noted that the committee packet includes Ms. Decker's letter.

[9:43:26 AM](#)

CHAIR SEATON, upon determining that no one else wished to testify, closed public testimony.

[9:43:44 AM](#)

CHAIR SEATON noted that the committee hasn't received any adverse comments on HB 321. He then asked if Mr. Cottongim needs any further clarification with regard to the intent of the language related to conveyors.

MR. COTTONGIM responded that he doesn't need further clarification. He remarked that any remaining gray areas could be addressed in regulation after working with Chair Seaton's office.

[9:45:38 AM](#)

CHAIR SEATON turned the committee's attention to the predetermination language, and asked if the documentation and drawings submitted prior to an investment is problematic to Mr. Cottongim.

MR. COTTONGIM answered, "I don't think so." He said that the details could be worked out when the procedures and regulations are created. He noted that it would take approximately 120 days to get regulations in place, but upon the effective date of the legislation some procedures could be created for use until the regulations are in place.

[9:47:46 AM](#)

REPRESENTATIVE EDGMON related his support for moving the legislation out of committee.

[9:47:54 AM](#)

REPRESENTATIVE JOHANSEN moved to report CSHB 321, Version 25-LS1285\M, Kane, 1/23/08, out of committee with individual recommendations and the accompanying fiscal notes. There being no objection, CSHB 321(FSH) was reported from the House Special Committee on Fisheries.

[9:48:36 AM](#)

#### **ADJOURNMENT**

There being no further business before the committee, the House Special Committee on Fisheries meeting was adjourned at [9:48:44 AM](#).