

ALASKA STATE LEGISLATURE
SENATE JUDICIARY STANDING COMMITTEE

November 3, 2007

9:06 a.m.

MEMBERS PRESENT

Senator Hollis French, Chair
Senator Charlie Huggins, Vice Chair
Senator Bill Wielechowski
Senator Lesil McGuire
Senator Gene Therriault

MEMBERS ABSENT

All members present

COMMITTEE CALENDAR

SENATE BILL NO. 2001

"An Act relating to the production tax on oil and gas and to conservation surcharges on oil; relating to the issuance of advisory bulletins and the disclosure of certain information relating to the production tax and the sharing between agencies of certain information relating to the production tax and to oil and gas or gas only leases; amending the State Personnel Act to place in the exempt service certain state oil and gas auditors and their immediate supervisors; establishing an oil and gas tax credit fund and authorizing payment from that fund; providing for retroactive application of certain statutory and regulatory provisions relating to the production tax on oil and gas and conservation surcharges on oil; making conforming amendments; and providing for an effective date."

MOVED CSSB 2001(JUD) OUT OF COMMITTEE

PREVIOUS COMMITTEE ACTION

BILL: SB2001

SHORT TITLE: OIL & GAS TAX AMENDMENTS

SPONSOR(s): RULES BY REQUEST OF THE GOVERNOR

10/18/07	(S)	READ THE FIRST TIME - REFERRALS
10/18/07	(S)	RES, JUD, FIN
10/19/07	(S)	RES AT 9:00 AM BUTROVICH 205
10/19/07	(S)	Heard & Held
10/19/07	(S)	MINUTE(RES)
10/20/07	(S)	RES AT 8:00 AM BUTROVICH 205

10/20/07 (S) Heard & Held
10/20/07 (S) MINUTE(RES)
10/21/07 (S) RES AT 1:00 PM HOUSE FINANCE 519
10/21/07 (S) Heard & Held
10/21/07 (S) MINUTE(RES)
10/22/07 (S) RES AT 11:30 AM BUTROVICH 205
10/22/07 (S) Heard & Held
10/22/07 (S) MINUTE(RES)
10/23/07 (S) RES AT 9:00 AM BUTROVICH 205
10/23/07 (S) Heard & Held
10/23/07 (S) MINUTE(RES)
10/24/07 (S) RES AT 10:00 AM BUTROVICH 205
10/24/07 (S) Heard & Held
10/24/07 (S) MINUTE(RES)
10/25/07 (S) RES AT 10:00 AM BUTROVICH 205
10/25/07 (S) Heard & Held
10/25/07 (S) MINUTE(RES)
10/26/07 (S) RES AT 1:30 PM BUTROVICH 205
10/26/07 (S) Heard & Held
10/26/07 (S) MINUTE(RES)
10/27/07 (S) RES AT 9:00 AM BUTROVICH 205
10/27/07 (S) Moved CSSB2001(RES) Out of Committee
10/27/07 (S) MINUTE(RES)
10/28/07 (S) RES AT 0:00 AM BUTROVICH 205
10/28/07 (S) -- MEETING CANCELED --
10/29/07 (S) RES RPT CS 1NR 6AM NEW TITLE
10/29/07 (S) NR: GREEN
10/29/07 (S) AM: HUGGINS, MCGUIRE, STEVENS, STEDMAN,
WIELECHOWSKI, WAGONER
10/29/07 (S) JUD AT 9:30 AM BUTROVICH 205
10/29/07 (S) Heard & Held
10/29/07 (S) MINUTE(JUD)
10/30/07 (S) JUD AT 9:00 AM BUTROVICH 205
10/30/07 (S) Heard & Held
10/30/07 (S) MINUTE(JUD)
10/31/07 (S) JUD AT 9:00 AM BUTROVICH 205
10/31/07 (S) Heard & Held
10/31/07 (S) MINUTE(JUD)
11/01/07 (S) JUD AT 9:00 AM BUTROVICH 205
11/01/07 (S) Heard & Held
11/01/07 (S) MINUTE(JUD)
11/02/07 (S) JUD AT 5:00 PM BUTROVICH 205
11/02/07 (S) -- Testimony <Invitation Only> --
11/03/07 (S) JUD AT 9:00 AM BUTROVICH 205

WITNESS REGISTER

PATRICK GALVIN, Commissioner
Department of Revenue (DOR)
Anchorage, AK

POSITION STATEMENT: Offered perspective on SB 2001

ROBERT MINTZ, Attorney
Kirkpatrick & Lockhart Preston Gates Ellis, LLP (K&L Gates)

POSITION STATEMENT: Explained conceptual Amendment 4 for SB 2001

JOHN MESSENGER, Staff to Representative Kerttula
Juneau, AK

POSITION STATEMENT: Explained conceptual Amendment 5 for SB 2001

DONALD BULLOCK, Attorney
Legislative Legal and Research Services Division
Legislative Affairs Agency
Juneau, AK

POSITION STATEMENT: Offered perspective on SB 2001

NANETTE THOMPSON
Division of Oil & Gas
Department of Natural Resources
Anchorage, AK

POSITION STATEMENT: Explained Amendment 11 for SB 2001

ACTION NARRATIVE

CHAIR HOLLIS FRENCH called the Senate Judiciary Standing Committee meeting to order at [9:06:57 AM](#). Present at the call to order were Senators Therriault, Wielechowski, McGuire, Huggins, and Chair French.

SB 2001-OIL & GAS TAX AMENDMENTS

[9:07:12 AM](#)

CHAIR FRENCH announced the consideration of SB 2001. Before the committee was CSSB 2001, labeled 25-GS0014\K. He asked Commissioner Galvin to describe the fiscal note process.

[9:07:35 AM](#)

PATRICK GALVIN, Commissioner, Department of Revenue (DOR), Anchorage, Alaska, informed the committee that a draft fiscal note should be completed within the hour. Two adjustments that are recognized at this time include a distinction for lease expenditures having to be incurred within the state and an adjustment to the personal services for exempt employees.

CHAIR FRENCH stated that the first technical amendment addresses a drafting error on page 25, line 22, that Mr. Bullock spoke about yesterday.

SENATOR HUGGINS moved Amendment 1, labeled 25-GS0014\K.8.

A M E N D M E N T 1

OFFERED IN THE SENATE

To CSSB 2001(JUD), Draft Version "K"

Page 25, line 22:

Delete "10"

Insert "20"

CHAIR FRENCH announced that without objection Amendment 1 is passed.

CHAIR FRENCH said Amendment 2 appears on page 25, line 10. It's clean up language that was referred to yesterday during the discussion of the penalty provisions of the bill. He recalls that the suggestion was to add language saying, "In addition to other penalties prescribed by law," to make certain that this isn't the only penalty for understatement of tax. In response to a question, he said the amendment is not drafted.

COMMISSIONER GALVIN suggested the committee either insert the clause as a lead-in that applies to both subsections or add the clause to each subsection separately because it is intended to modify both subsection (a) and (b).

CHAIR FRENCH moved Amendment 2 as follows:

Amendment 2

Page 25, line 10 following (a):

Insert: "In addition to other penalties
prescribed by law,"

Page 25, line 14 following (b):

Insert: "In addition to other penalties
prescribed by law,"

CHAIR FRENCH announced that without objection Amendment 2 is passed.

[9:13:21 AM](#)

CHAIR FRENCH moved Amendment 3 as suggested by Mr. Bullock.

AMENDMENT 3

Page 27, lines 11-12 following "appropriation":

Delete: "for the purpose from penalties collected by the department under this chapter,"

CHAIR FRENCH announced that without objection, Amendment 3 is passed.

[9:15:38 AM](#)

SENATOR THERRIAULT referred to page 27, line 30 and asked about Mr. Bullock's suggestion to change the word "conditions" to the singular.

CHAIR FRENCH said that is part of transportation piece that will be addressed in part of the "Nan Thompson amendment." [Amendment 11]

CHAIR FRENCH asked Mr. Mintz to comment on conceptual Amendment 4.

[9:16:56 AM](#)

ROBERT MINTZ, Attorney, Kirkpatrick & Lockhart Preston Gates Ellis, LLP (K&L Gates), clarified that although he styled the amendment conceptual, it does contain the exact language that is intended. He said it addresses an inconsistency in annual versus monthly tax calculations. There are two components to the tax rate under the bill--the basic tax rate of 25 percent and the additional progressivity tax rate, which depends on a monthly determination. Basically there are three ways to handle this. The original PPT legislation had an annual calculation of the base rate and an additional monthly tax under progressivity. The ACES bill had both the base rate and progressivity as an annual rate. He understands that the judiciary committee substitute (CS) intends that both the base rate and the progressivity rate would be calculated on a monthly basis. The point of the proposed amendment is to make the numbers work. There would also be conforming changes in other parts of the bill, he stated.

MR. MINTZ said although the tax calculations are done on a monthly basis, the amendment does preserve the basic aspect of the legislation, which is that it's an annual tax. This is important because a lot of the other provisions specifically involving tax credits are done on an annual basis. Totally

reverting to a monthly tax would require much more extensive changes, he said.

[9:19:49 AM](#)

CHAIR FRENCH asked him to identify which page his amendment sections refer to.

MR. MINTZ said the first change, which repeals and reenacts AS 43.55.011(e), is on page 10, line 30, of version "K". It clarifies that the tax calculation of production tax value for oil and gas multiplied by the tax rate is done each month. The second sentence of subsection (e) preserves the annual aspect of the tax.

Page 11, line 7, Sec. 16, which repeals and reenacts AS 43.55.011(g), says that the tax rate is calculated for each month separately. The second sentence says that the tax rate may not be more than 50 percent.

Page 11, line 14, Sec. 17, amends AS 43.55.011(h). It clarifies the way the price index is calculated for a month is to add the production tax values of all the oil and gas produced in the state and divide that by the production.

CHAIR FRENCH noted that it's a minor change to Sec. 17.

[9:23:09 AM](#)

MR. MINTZ said on page 14, line 13, there is a conforming change to changes in AS 43.55.160. In general the reason is that there is no longer a need to have both an annual and a monthly production tax value of oil and gas since the base rate tax and the progressivity tax are now calculated on a monthly basis.

CHAIR FRENCH noted a typographical error on page 2, text line 6, of the amendment. Mr. Mintz agreed there is an extra "4" in the bolded and underlined statutory reference to AS 43.55.020(a)(2). It was removed.

[9:24:39 AM](#)

MR. MINTZ said the next change is in bill section 41, page 28, line 8, through page 29, line 5. It amends AS 43.55.160(a), which explains how to calculate the production tax value of oil and gas. In the bill the production tax value feeds into the application of the tax rate under AS 43.55.011(e) and in figuring out the monthly installment payments in AS 43.55.020(a)(2). The reference to Section 011(g) is deleted

because it was the previous monthly progressivity tax under current law.

COMMISSIONER GALVIN noted that the explanation covers page 28, line 8, through page 29, line 5.

MR. MINTZ again said the annual production tax values are no longer needed. In current law Section 160(a)(1) has four subparagraphs that explain how to calculate annual production tax value. Paragraph (2) on page 29 of the CS also has four paragraphs to explain how to calculate monthly production tax values. The calculations under paragraph (1) are no longer needed so all the language on page 28, line 8, through page 29, line 5 can be deleted from the existing statute.

[9:27:18 AM](#)

COMMISSIONER GALVIN asked for clarification that the language is not to be deleted from the bill. It should be shown to be deleted from the statute.

MR. MINTZ said yes, but since Sec. 41 of the CS already amends Section 160(a), proposed Amendment 4 would make another change in Section 160(a), which is to delete subparagraphs (A), (B), (C), and (D).

CHAIR FRENCH asked him how Section 160(a) would read if the amendment were adopted.

MR. MINTZ clarified that new text is bolded and underlined and deleted text is capitalized and bracketed and then read from page 28, line 7, and page 29, line 5 of the CS as follows:

- (a) Except as provided in (b) of this section, for the purposes of [(2)] **AS 43.55.011(e) and AS 43.55.020(a)(2)**, the [MONTHLY] production tax value of the taxable"

CHAIR FRENCH reread the proposed subsection (a).

MR. MINTZ said the next change is to renumber on page 29, subparagraphs (A), (B), (C), and (D) to become paragraphs (1), (2), (3), and (4). Again, the reason for the change is that there no longer a need for an annual production tax value.

[9:31:05 AM](#)

COMMISSIONER GALVIN said this characterization may confuse the drafter.

At ease from [9:31:28 AM](#) to [9:37:43 AM](#). Sound is missing until 9:40:19 AM.

COMMISSIONER GALVIN suggested the committee amend the amendment.

CHAIR FRENCH moved an amendment to the amendment as follows:

Page 28, line 8, bracket "(1)" and leave the reference to "AS 43.55.011(e)" and insert "and". Bracket "," and all material through "(2)" on page 29, line 5. Leave the reference to "AS 43.55.020(a)(2)". Leave the bracket that's in place for "[43.55.011(g)]". Leave ", the", bracket "monthly" and leave "production tax value of the taxable".

Finding no objection, he announced that the amendment to the amendment is adopted.

[9:41:14 AM](#)

MR. MINTZ said the next change is to conform AS 43.55.160(c) to the changes that have been discussed previously in terms of calculating a monthly production tax value rather than an annual alternative.

COMMISSIONER GALVIN stated agreement with the provision.

[9:43:08 AM](#)

MR. MINTZ said the next change would amend AS 43.55.160(e). The subsection is not addressed in the CS so it would be a new bill section. This conforming change removes the reference to an annual production tax value.

COMMISSIONER GALVIN stated agreement with the provision.

MR. MINTZ said the next change would amend AS 43.55.170(b). The subsection, which deals with adjustments to lease expenditures, is not addressed in the CS, but it is conforming to the changes made in Section 160.

[9:45:20 AM](#)

MR. MINTZ said the final change would remove the reference to Section 160(c) from the repealer on page 37.

CHAIR FRENCH found no further comments or discussion on the proposed amendment and asked for a motion.

SENATOR WIELECHOWSKI moved [conceptual] Amendment 4. [Original punctuation and the amendment to the amendment included]

AMENDMENT 4

Conceptual Amendment to CSSB 2001(JUD) version "K"

Repeal and reenact AS 43.55.011(e) to read:

(e) There is levied on the producer of oil or gas a tax for all oil and gas produced each calendar year from each lease or property in the state, less any oil and gas the ownership or right to which is exempt from taxation or constitutes a landowner's royalty interest. Except as otherwise provided under (f), (j) and (k) of this section, the tax is equal to the sum, over all months in the calendar year, of each month's production tax value of the taxable oil and gas as calculated under AS 43.55.160 multiplied by the tax rate of the month determined under (g) of this section.

Repeal and reenact AS 43.55.011(g) to read:

(g) The tax rate applied to the production tax value of oil and gas under (e) of this section is 25 percent plus, for a month for which the price index determined under (h) of this section is greater than zero, 0.40 multiplied by the price index determined under (h) of this section. However, a tax rate calculated under this subsection may not be more than 50 percent.

Amend AS 43.55.011(h) to read:

(h) For purposes of (g) of this section, the price index for a month is calculated by subtracting 30 [40] from the number that is equal to the quotient of the total [MONTHLY] production tax values [VALUE] of the taxable oil and gas produced by the producer from all leases or properties in the state during that month, as calculated under AS 55.160, divided by the total amount of that [THE TAXABLE] oil and gas produced by the producer during that month, in BTU equivalent barrels. However, a price index calculated under this subsection may not be less than zero.

Page 14, line 13 of the CS: delete "AS 43.55.160(a)(2)" and insert "AS 43.55.160"

AS 43.55.160(a) is amended to read:

(a) Except as provided in (b) of this section, for the purposes of

[(1)] AS 43.55.011(e) and AS 43.55.020(a)(2) [, THE ANNUAL PRODUCTION TAX VALUE OF THE TAXABLE

(A) OIL AND GAS PRODUCED DURING A CALENDAR YEAR FROM LEASES OR PROPERTIES IN THE STATE THAT INCLUDE LAND NORTH OF 68 DEGREES NORTH LATITUDE IS THE GROSS VALUE AT THE POINT OF PRODUCTION OF THE OIL AND GAS TAXABLE UNDER AS 43.55.011(e) AND PRODUCED BY THE PRODUCER FROM THOSE LEASES OR PROPERTIES, LESS THE PRODUCER'S LEASE EXPENDITURES UNDER AS 43.55.165 FOR THE CALENDAR YEAR APPLICABLE TO THE OIL AND GAS PRODUCED BY THE PRODUCER FROM THOSE LEASES OR PROPERTIES, AS ADJUSTED UNDER AS 43.55.170;

(B) OIL AND GAS PRODUCED DURING A CALENDAR YEAR FROM LEASES OR PROPERTIES IN THE STATE OUTSIDE THE COOK INLET SEDIMENTARY BASIN, NO PART OF WHICH IS NORTH OF 68 DEGREES NORTH LATITUDE, IS THE GROSS VALUE AT THE POINT OF PRODUCTION OF THE OIL AND GAS TAXABLE UNDER AS 43.55.011(e) AND PRODUCED BY THE PRODUCER FROM THOSE LEASES OR PROPERTIES, LESS THE PRODUCER'S LEASE EXPENDITURES UNDER AS 43.55.165 FOR THE CALENDAR YEAR APPLICABLE TO THE OIL AND GAS PRODUCED BY THE PRODUCER FROM THOSE LEASES OR PROPERTIES, AS ADJUSTED UNDER AS 43.55.170;

(C) OIL PRODUCED DURING A CALENDAR YEAR FROM A LEASE OR PROPERTY IN THE COOK INLET SEDIMENTARY BASIN IS THE GROSS VALUE AT THE POINT OF PRODUCTION OF THE OIL TAXABLE UNDER AS 43.55.011(e) AND PRODUCED BY THE PRODUCER FROM THAT LEASE OR PROPERTY, LESS THE PRODUCER'S LEASE EXPENDITURES UNDER AS 43.55.165 FOR THE CALENDAR YEAR APPLICABLE TO THE OIL PRODUCED BY THE PRODUCER FROM THAT LEASE OR PROPERTY, AS ADJUSTED UNDER AS 43.55.170;

(D) GAS PRODUCED DURING A CALENDAR YEAR FROM A LEASE OR PROPERTY IN THE COOK INLET SEDIMENTARY BASIN IS THE GROSS VALUE AT THE POINT OF PRODUCTION OF THE GAS TAXABLE UNDER AS 43.55.011(e) AND PRODUCED BY THE PRODUCER FROM THAT LEASE OR PROPERTY, LESS THE PRODUCER'S LEASE EXPENDITURES UNDER AS 43.55.165 FOR THE 14 CALENDAR YEAR APPLICABLE TO THE GAS PRODUCED BY THE PRODUCER FROM THAT LEASE OR PROPERTY, AS ADJUSTED UNDER AS 43.55.170; (2) AS 43.55.011(g)], the [MONTHLY] production tax value of the taxable

Page 29, lines 7, 14, 22, and 29: replace "(A)", "(B)", "(C)", and "(D)" with "(1)", and "(2)", "(3)", and "(4)", respectively

Amend AS 43.55.160(c) to read:

(c) Notwithstanding any contrary provision of AS 43.55.150, for purposes of calculating a [MONTHLY] production tax value under (a)[(a)(2)] of this section, the gross value at the point of production of the oil and gas taxable under AS 43.55.011(e) [AS 43.55.011(g)] is calculated under regulations adopted by the department that provide for using an appropriate monthly share of the producer's costs of transportation for the calendar year.

Amend AS 43.55.160(e) to read:

(e) Any adjusted lease expenditures under AS 43.55.165 and 43.55.170 that would otherwise be deductible by a producer in a calendar year but whose deduction would cause a [AN ANNUAL] production tax value calculated under (a) [(a)(1)] of this section of taxable oil or gas produced during the calendar year to be less than zero may be used to establish a carried-forward annual loss under AS 43.55.023(b). In this subsection, "producer" includes "explorer."

Amend AS 43.55.170(b) to read:

(b) Except as otherwise provided under this subsection, if one or more payments or credits subject to this section are received by a producer or by an operator acting for the producer during a calendar year and if either the total amount of the payments or credits exceeds the amount of the producer's applicable lease expenditures for that calendar year or the producer has no lease expenditures for that calendar year, the producer shall nevertheless subtract those payments or credits from the lease expenditures or from zero, respectively, and the producer's applicable adjusted lease expenditures for that calendar year are a negative number and shall be applied to the pertinent calculations [CALCULATION] under AS 43.55.160 AS [43.55.160(a)] as a negative number.

Delete 43.55.160(c) from the repeal in Sec. 49 of the bill.

CHAIR FRENCH announced that without objection Amendment 4 is adopted.

CHAIR FRENCH said Amendment 5 is by Senator Wielechowski and it relates to lease expenditures.

SENATOR WIELECHOWSKI explained that the idea of the amendment is to tighten the lease expenditure language. He worked on this with former Senator Guess and Mr. Messenger who is an oil and gas attorney.

JOHN MESSENGER, Staff to Representative Kerttula, Juneau, AK, informed the committee that he is a former deputy commissioner to the Department of Revenue. He also worked on tax matters when he was in the attorney general's office. Subsequently he entered private practice and in that capacity he represented the State of Alaska in oil and tax matters including audits.

[9:49:40 AM](#)

MR. MESSENGER said the first change on page 30 basically deletes lines 25-27 from the bill and would eliminate the deduction of overhead expenses as a direct cost of producing, exploring or developing oil and gas deposits.

[9:53:15 AM](#)

MR. MESSENGER said the second change is page 30, line 29 through page 31, line 30. It addresses a starting point for direct costs then leaves it to the department to identify additional direct costs. The language regarding typical industry practices is deleted because of the problems associated with developing regulations by relying on what industry has established in its unit agreements. The standard the department should use in adopting the regulation is addressed.

[9:58:02 AM](#)

MR. MESSENGER said the next change is on page 32, line 1, through page 35, line 12. It adds to the list of items that would not be allowable lease expenditures. Under paragraph (8), the additional disallowed costs include "lobbying, public relations, advertising, or policy advocacy". The basis for the change is that they are indirect costs rather than direct costs.

MR. MESSENGER said paragraph (12) on page 32, lines 23-24, deals with transactions between parties. Currently the onus is on the Department of Revenue to establish the fair market value of a

transaction between affiliated parties. The intent here is to shift the onus to the producer.

At ease from [10:02:27 AM](#) to [10:04:01 AM](#).

CHAIR FRENCH asked Commissioner Galvin to comment on the last two provisions. He's been assured that lobbying, public relations, advertising, and policy advocacy are not allowed through regulation, but he knows that the public is very interested in having this specifically spelled out in the bill.

COMMISSIONER GALVIN agreed that they are not deductible, but spelling them out in statute isn't a problem.

CHAIR FRENCH asked his view of the change to paragraph (12), on page 3, lines 24-25, of the proposed amendment.

COMMISSIONER GALVIN clarified he's just seen it for the first time, but it doesn't appear to include anything that's objectionable. The common goal is ensuring that any affiliated transactions are captured and that the producers have the burden to demonstrate that the cost is appropriate.

[10:05:26 AM](#)

MR. MESSENGER said the final change appears on page 6, lines 16-20, of the amendment. Paragraph (21) adds costs "relating to office buildings, fixtures and equipment, and real property that are not located on an oil or gas exploration, production, or development lease of property in the state". Paragraph (22) adds "overhead, office, or administrative expenses and all other indirect costs of oil or gas exploration, development, or production."

[10:07:49 AM](#)

CHAIR FRENCH asked Commissioner Galvin if he'd seen these concepts before and if he had a comment.

COMMISSIONER GALVIN said he's discussed the last idea, but most of the others are new. Beginning with the first suggested change, he said his understanding is that it is typical to have an allowance for deducting direct costs for overhead. It recognizes that there will be overhead costs associated with any direct costs. It's a straight percentage and that's what is currently allowed through regulations. Eliminating that is merely a statement that only direct costs will be allowed. "We're not going to allow for that extra 3 percent bump." That's a policy call. Our experience is based on having the allowance

so we'd have to adjust our expectation of the impact of tax if it were deleted, he said.

[10:10:21 AM](#)

COMMISSIONER GALVIN said the next primary change is captured by omission. Referring to the bottom of page 2 of the amendment, he said those provisions, which are in both the CS and the original bill, are included so the department can use company accounting systems to identify which costs are allowable, which are not, and which will be used during the auditing process. Before eliminating that language he wants to make sure it doesn't deny the auditors the opportunity to use certain tools.

COMMISSIONER GALVIN commented generally there are a number of changes that don't pick up the modifications that were made in the CS. That includes reference to costs incurred in the state and provisions from SB 80 that were discussed yesterday.

[10:12:20 AM](#)

COMMISSIONER GALVIN referred to paragraphs (21) and (22) on page 6 of the amendment and said it's a little narrow to think that all costs associated with oil and gas production will actually be on the leasehold. To develop the resources it's necessary to have engineers, geologists, computer systems, and certain infrastructure that's not on the North Slope. Don't ignore the contribution of folks working in Anchorage, he cautioned.

[10:14:26 AM](#)

SENATOR WIELECHOWSKI said the concern he's heard about overhead being a direct cost is that we don't know what we're allowing. Potentially it could be health club costs in Dallas Texas or steak dinners in Houston Texas. "People have a concern about that and this is a way for us to ratchet that up." The safety valve is on page 2, paragraph 7, so the department may include as direct costs things that may currently be overhead.

With regard to the industry standard provision, he said this makes it very clear what will be allowed and what will not be allowed. The political advertising and public relations change is very important and he said he's happy that the administration supports that.

[10:16:06 AM](#)

SENATOR WIELECHOWSKI asked Mr. Messenger to talk about the provision on limiting allowable deductions to activity that occurs within the state.

MR. MESSENGER said the proposed amendment uses a direct versus indirect approach for determining what's deductible rather than making a distinction between in-state and out-of-state. Generally it's up to the legislature to decide what deductions are allowed, but making a distinction between in-state and out-of-state brings up potential constitutional problems under the commerce clause. Although the CS has language that makes such a distinction, a more neutral approach is to narrow the deductions to what is directly involved in the production, exploration, and development of oil and gas. He suggested that it's better to tie the deductions between direct and indirect costs and treat all the producers the same way. The same category of expenses should be deductible regardless of where they are incurred, he stated.

[10:19:04 AM](#)

SENATOR WIELECHOWSKI asked if the language in SB 80 regarding corrosion is included.

MR. MESSENGER said it wasn't his intent to deal with the corrosion aspect.

SENATOR WIELECHOWSKI referred to paragraph (19) on page 5 of the amendment and noted that the CS contains language that would not allow improper maintenance. He suggested an amendment to the amendment.

CHAIR FRENCH said the amendment hasn't been moved yet.

COMMISSIONER GALVIN suggested it may be appropriate to address the different parts of the amendment separately.

CHAIR FRENCH said deleting that section of the amendment would leave the CS alone.

COMMISSIONER GALVIN said by doing that the administration wouldn't be concerned about the entire amendment. It has a lot of unintended consequences, he said.

[10:21:05 AM](#)

SENATOR WIELECHOWSKI moved Amendment 5, labeled 25-GS0014\K.7

25-GS0014\K.7
Bullard/Bullock

A M E N D M E N T 5

OFFERED IN THE SENATE

BY SENATOR WIELECHOWSKI

To: CSSB 2001(JUD), Draft Version "K"

Page 30, lines 6 - 27:

Delete all material and insert:

"(a) For purposes of this chapter, a producer's lease expenditures for a calendar year are costs, other than items listed in (e) of this section, that are

(1) incurred by the producer during the calendar year after March 31, 2006, to explore for, develop, or produce oil or gas deposits located within the producer's leases or properties in the state or, in the case of land in which the producer does not own an operating right, operating interest, or working interest, to explore for oil or gas deposits within other land in the state; and

(2) allowed by the department by regulation, based on the department's determination that the costs satisfy the following three requirements:

(A) the costs must be incurred upstream of the point of production of oil and gas;

(B) the costs must be ordinary and necessary costs of exploring for, developing, or producing, as applicable, oil or gas deposits; and

(C) the costs must be direct costs of exploring for, developing, or producing, as applicable, oil or gas deposits."

Page 30, line 29, through page 31, line 30:

Delete all material and insert:

"(b) For purposes of (a) of this section,

[(1)] direct costs include

(1) [(A)] an expenditure, when incurred, to acquire an item if the acquisition cost is otherwise a direct cost, notwithstanding that the expenditure may be required to be capitalized rather than treated as an expense for financial accounting or federal income tax purposes;

(2) [(B)] payments of or in lieu of

(A) property taxes [,] for properties on which oil and gas exploration, development, or production is taking place; and

(B) sales and use taxes, motor fuel taxes, and excise taxes related to transactions or activities

involving oil or gas exploration, development, or production;

(3) supplies to be used for oil or gas exploration, development, or production [(C) A REASONABLE ALLOWANCE, AS DETERMINED UNDER REGULATIONS ADOPTED BY THE DEPARTMENT, FOR OVERHEAD EXPENSES DIRECTLY RELATED TO EXPLORING FOR, DEVELOPING, AND PRODUCING OIL OR GAS DEPOSITS LOCATED WITHIN LEASES OR PROPERTIES OR OTHER LAND IN THE STATE];

(4) purchased fuel;

(5) routine maintenance;

(6) the wages and benefits of employees who are directly participating in exploration, development, or production operations; and

(7) other direct costs as may be established in regulations adopted by the department

[(2) AN ACTIVITY DOES NOT NEED TO BE PHYSICALLY LOCATED ON, NEAR, OR WITHIN THE PREMISES OF THE LEASE OR PROPERTY WITHIN WHICH AN OIL OR GAS DEPOSIT BEING EXPLORED FOR, DEVELOPED, OR PRODUCED IS LOCATED IN ORDER FOR THE COST OF THE ACTIVITY TO BE A COST UPSTREAM OF THE POINT OF PRODUCTION OF THE OIL OR GAS]."

Page 32, line 1, through page 35, line 12:

Delete all material and insert:

"(e) For purposes of this section, lease expenditures do not include

(1) depreciation, depletion, or amortization;

(2) oil or gas royalty payments, production payments, lease profit shares, or other payments or distributions of a share of oil or gas production, profit, or revenue;

(3) taxes based on or measured by net income;

(4) interest or other financing charges or costs of raising equity or debt capital;

(5) acquisition costs for a lease or property or exploration license;

(6) costs arising from fraud, wilful misconduct, [OR] gross negligence, violation of law, or failure to comply with an obligation under a lease, permit, or license issued by the state or federal government;

(7) fines or penalties imposed by law;

(8) costs of arbitration, litigation, [OR OTHER] dispute resolution activities, lobbying, public relations, advertising, or policy advocacy [THAT INVOLVE THE STATE OR CONCERN THE RIGHTS OR OBLIGATIONS AMONG OWNERS OF INTERESTS IN, OR RIGHTS TO PRODUCTION FROM, ONE OR MORE LEASES OR PROPERTIES OR A UNIT];

(9) costs incurred in organizing a partnership, joint venture, or other business entity or arrangement;

(10) amounts paid to indemnify the state; the exclusion provided by this paragraph does not apply to the costs of obtaining insurance or a surety bond from a third-party insurer or surety;

(11) surcharges levied under AS 43.55.201 or 43.55.300;

(12) an expenditure otherwise deductible under (b) of this section that is the result of [FOR A TRANSACTION THAT IS] an internal transfer, a transaction with an affiliate, or a transaction between related parties, or is otherwise not an arm's length transaction, unless the producer establishes to the satisfaction of the department that the amount of the expenditure does not exceed the [EXPENDITURES INCURRED THAT ARE IN EXCESS OF] fair market value of the expenditure;

(13) an expenditure incurred to purchase an interest in any corporation, partnership, limited liability company, business trust, or any other business entity, whether or not the transaction is treated as an asset sale for federal income tax purposes;

(14) a tax levied under AS 43.55.011;

(15) [THE PORTION OF] costs incurred for dismantlement, removal, surrender, or abandonment of a facility, pipeline, well pad, platform, or other structure, or for the restoration of a lease, field, unit, area, tract of land, body of water, or right-of-way in conjunction with dismantlement, removal, surrender, or abandonment [, THAT IS ATTRIBUTABLE TO PRODUCTION OF OIL OR GAS OCCURRING BEFORE APRIL 1, 2006; THE PORTION IS CALCULATED AS A RATIO OF THE AMOUNT OF OIL AND GAS PRODUCTION, IN BARRELS OF OIL EQUIVALENT, ASSOCIATED WITH THE FACILITY, PIPELINE, WELL PAD, PLATFORM, OTHER STRUCTURE, LEASE, FIELD, UNIT, AREA, BODY OF WATER, OR RIGHT-OF-WAY OCCURRING BEFORE APRIL 1, 2006, TO THE TOTAL AMOUNT OF OIL AND GAS PRODUCTION, IN BARRELS OF OIL EQUIVALENT,

ASSOCIATED WITH THAT FACILITY, PIPELINE, WELL PAD, PLATFORM, OTHER STRUCTURE, LEASE, FIELD, UNIT, AREA, BODY OF WATER, OR RIGHT-OF-WAY THROUGH THE END OF THE CALENDAR MONTH BEFORE COMMENCEMENT OF THE DISMANTLEMENT, REMOVAL, SURRENDER, OR ABANDONMENT]; a cost is not excluded under this paragraph if the dismantlement, removal, surrender, or abandonment for which the cost is incurred is undertaken for the purpose of replacing, renovating, or improving the facility, pipeline, well pad, platform, or other structure; [FOR THE PURPOSES OF THIS PARAGRAPH, "BARREL OF OIL EQUIVALENT" MEANS

(A) IN THE CASE OF OIL, ONE BARREL;

(B) IN THE CASE OF GAS, 6,000 CUBIC FEET;]

(16) costs incurred for containment, control, cleanup, or removal in connection with any unpermitted release of oil or a hazardous substance and any liability for damages imposed on the producer or explorer for that unpermitted release; this paragraph does not apply to the cost of developing and maintaining an oil discharge prevention and contingency plan under AS 46.04.030;

(17) costs incurred to satisfy a work commitment under an exploration license under AS 38.05.132;

(18) that portion of expenditures, that would otherwise be qualified capital expenditures, as defined in AS 43.55.023 [AS 43.55.023(k)], incurred during a calendar year that are less than the product of \$0.30 multiplied by the total taxable production from each lease or property, in BTU equivalent barrels, during that calendar year, except that, when a portion of a calendar year is subject to this provision, the expenditures and volumes shall be prorated within that calendar year;

(19) costs incurred for repair, replacement, or deferred maintenance of a facility, a pipeline, a structure, or equipment, other than a well, that results in or is undertaken in response to a failure, problem, or event that results in an unscheduled interruption of, or reduction in the rate of, oil or gas production; or costs incurred for repair, replacement, or deferred maintenance of a facility, a pipeline, a structure, or equipment, other than a well, that is undertaken in response to, or is otherwise associated with, an unpermitted release of a hazardous substance or of gas; however, costs under

this paragraph that would otherwise constitute lease expenditures under (a) of this section may be treated as lease expenditures if the department determines that the repair or replacement is solely necessitated by an act of war, by an unanticipated grave natural disaster or other natural phenomenon of an exceptional, inevitable, and irresistible character, the effects of which could not have been prevented or avoided by the exercise of due care or foresight, or by an intentional or negligent act or omission of a third party, other than a party or its agents in privity of contract with, or employed by, the producer or an operator acting for the producer, but only if the producer or operator, as applicable, exercised due care in operating and maintaining the facility, pipeline, structure, or equipment, and took reasonable precautions against the act or omission of the third party and against the consequences of the act or omission; in this paragraph,

(A) "costs incurred for repair, replacement, or deferred maintenance of a facility, a pipeline, a structure, or equipment" includes costs to dismantle and remove the facility, pipeline, structure, or equipment that is being replaced;

(B) "hazardous substance" has the meaning given in AS 46.03.826;

(C) "replacement" includes renovation or improvement;

(20) costs incurred to construct, acquire, or operate a refinery or crude oil topping plant, regardless of whether the products of the refinery or topping plant are used in oil or gas exploration, development, or production operations; however, if a producer owns a refinery or crude oil topping plant that is located on or near the premises of the producer's lease or property in the state and that processes the producer's oil produced from that lease or property into a product that the producer uses in the operation of the lease or property in drilling for or producing oil or gas, the producer's lease expenditures include the amount calculated by subtracting from the fair market value of the product used the prevailing value, as determined under AS 43.55.020(f), of the oil that is processed;

(21) costs relating to office buildings, fixtures and equipment, and real property that are not

located on an oil or gas exploration, production, or development lease or property in the state; and
(22) overhead, office, or administrative expenses and all other indirect costs of oil or gas exploration, development, or production."

CHAIR FRENCH asked if there is objection to Amendment 5.

SENATOR WIELECHOWSKI said he'd like to deal with the provision in paragraph (19).

[10:21:28 AM](#)

SENATOR THERRIAULT said, "Then I will object."

SENATOR WIELECHOWSKI said, "My intent is to have paragraph (19) and (20) as written in the CS transported into this amendment."

CHAIR FRENCH recapped the idea and Senator Wielechowski agreed it accomplishes the purpose.

[10:22:33 AM](#)

COMMISSIONER GALVIN noted that the corrosion fix would be deleted from the bill.

At ease from [10:22:44 AM](#) to [10:23:22 AM](#).

CHAIR FRENCH asked Mr. Bullock to help with the drafting issue.

DONALD BULLOCK, Attorney, Legislative Legal and Research Services Division, Legislative Affairs Agency, Juneau, AK, said he hadn't seen the amendment, but generally an amendment should only address the paragraphs that are involved. The problem with Amendment 5 is it deletes everything and then reinserts it in modified form rather than simply addressing the part of the existing language that is intended to be changed.

SENATOR WIELECHOWSKI began to suggest a fix.

[10:24:17 AM](#)

CHAIR FRENCH said, "We're on an amendment to an amendment and we either need to withdraw it or vote on it."

SENATOR WIELECHOWSKI withdrew the amendment to the amendment.

SENATOR WIELECHOWSKI read page 2 lines 29-30 of the amendment and suggested deleting all material from page 2, line 31,

through page 34, line 2. Delete from page 5 of the amendment lines 9-31, and page 6, line 15.

[10:25:13 AM](#)

MR. BULLOCK offered to redraft the amendment so it fits.

CHAIR FRENCH summarized the suggestion is to withdraw Amendment 5 for the time being so it can be redrafted.

MR. BULLOCK again advised that when drafting an amendment general practice is to only address the page and line numbers that are being changed.

SENATOR WIELECHOWSKI said, "I crafted an amendment, I sent it to Leg Legal and this is what I got back."

MR. BULLOCK suggested that he received what he asked for.

[10:26:55 AM](#)

SENATOR WIELECHOWSKI suggested the problem comes from working from the resources CS.

MR. BULLOCK offered his view that the amendment is inappropriate and it needs to be narrowed.

At ease from [10:27:17 AM](#) to [10:55:27 AM](#)

SENATOR WIELECHOWSKI withdrew Amendment 5.

[10:55:37 AM](#)

SENATOR THERRIAULT moved Amendment 6, labeled 25-GS0014\K.2. The purpose is to reinsert original bill sections 36-44 that dealt with exploration incentive credits (EIC) for seismic information. The administration wants to restructure some existing statutes and create a new class of 5 percent credit. It says that the state will participate in securing seismic information, but it wants a better process so the information is available to the public and other explorers, he said.

25-GS0014\K.2
Kane/Bullock

A M E N D M E N T 6

OFFERED IN THE SENATE BY SENATOR THERRIAULT
To: CSSB 2001(JUD), Draft Version "K"

Page 2, line 3:

Delete "sec. 37"

Insert "sec. 46"

Page 19, following line 7:

Insert new bill sections to read:

"* **Sec. 29.** AS 43.55.025(a) is amended to read:

(a) Subject to the terms and conditions of this section, a credit against the production tax levied by [DUE UNDER] AS 43.55.011(e) [OR (f)] is allowed for exploration expenditures that qualify under (b) of this section in an amount equal to one of the following:

(1) 20 percent of the total exploration expenditures that qualify only under (b) and (c) of this section;

(2) 20 percent of the total exploration expenditures [FOR WORK PERFORMED BEFORE JULY 1, 2007, AND] that qualify only under (b) and (d) of this section;

(3) 40 percent of the total exploration expenditures that qualify under (b), (c), and (d) of this section; or

(4) 40 percent of the total exploration expenditures that qualify only under (b) and (e) of this section.

* **Sec. 30.** AS 43.55.025(b) is amended to read:

(b) To qualify for the production tax credit under (a) of this section, an exploration expenditure must be incurred for work performed [ON OR] after December 31, 2007 [JULY 1, 2003], and before July 1, 2016, [EXCEPT THAT AN EXPLORATION EXPENDITURE FOR A COOK INLET PROSPECT MUST BE INCURRED FOR WORK PERFORMED ON OR AFTER JULY 1, 2005,] and

(1) may be for seismic or other geophysical exploration costs not connected with a specific well;

(2) if for an exploration well,

(A) must be incurred by an explorer that holds an interest in the exploration well for which the production tax credit is claimed;

(B) may be for either a [AN OIL OR GAS DISCOVERY] well that encounters an oil or gas deposit or a dry hole; [AND]

(C) must be for a well that has been completed or abandoned at the time the explorer claims the tax credit under (f) of this section; and

(D) must be for goods, services, or rentals of personal property reasonably required for the surface preparation, drilling, casing, cementing, and logging of an exploration well, and, in the case of a dry hole, for the expenses required for abandonment if the well is abandoned within 18 months after the date the well was spudded;

(3) may not be for testing, stimulation, or completion costs; administration, supervision, engineering, or lease operating costs; geological or management costs; community relations or environmental costs; bonuses, taxes, or other payments to governments related to the well; costs arising from gross negligence or violation of health, safety, or environmental statutes or regulations; or other costs that are generally recognized as indirect costs or financing costs; and

(4) may not be incurred for an exploration well or seismic exploration that is included in a plan of exploration or a plan of development for any unit on May 13, 2003.

* **Sec. 31.** AS 43.55.025(c) is repealed and reenacted to read:

(c) To be eligible for the 20 percent production tax credit authorized by (a)(1) of this section or the 40 percent production tax credit authorized by (a)(3) of this section, exploration expenditures must

(1) qualify under (b) of this section; and

(2) be for an exploration well, subject to the following:

(A) before spudding the well, (i) the explorer shall submit to the commissioner of natural resources the information necessary to determine whether the geological objective of the well is a potential oil or gas trap that is distinctly separate from any trap that has been tested by a preexisting well; and (ii) the commissioner of natural resources must make an affirmative determination on that question; the commissioner of natural resources shall decide whether to make that determination within 60 days after receiving all the necessary information from the explorer and based on the information received and on other information the commissioner of natural resources may consider relevant;

(B) for an exploration well other than a well to explore a Cook Inlet prospect, the well must be located and drilled in such a manner that the

bottom hole is located not less than three miles away from the bottom hole of a preexisting well drilled for oil or gas, irrespective of whether the preexisting well has been completed, suspended, or abandoned;

(C) after completion or abandonment of the exploration well, the commissioner of natural resources must determine that the well adequately achieved the explorer's stated geological objective.

* **Sec. 32.** AS 43.55.025(f) is amended to read:

(f) For a production tax credit under this section,

(1) an explorer shall, in a form prescribed by the department and, **except for a credit under (1) of this section,** within six months of the completion of the exploration activity, claim the credit and submit information sufficient to demonstrate to the department's satisfaction that the claimed exploration expenditures qualify under this section;

(2) an explorer shall agree, in writing,

(A) to notify the Department of Natural Resources, within 30 days after completion of seismic or geophysical data processing, completion of [A] well **drilling**, or filing of a claim for credit, whichever is the latest, for which exploration costs are claimed, of the date of completion and submit a report to that department describing the processing sequence and providing a list of data sets available; [IF, UNDER (c)(2)(B) OF THIS SECTION, AN EXPLORER SUBMITS A CLAIM FOR A CREDIT FOR EXPENDITURES FOR AN EXPLORATION WELL THAT IS LOCATED WITHIN THREE MILES OF A WELL ALREADY DRILLED FOR OIL AND GAS, IN ADDITION TO THE SUBMISSIONS REQUIRED UNDER (1) OF THIS SUBSECTION, THE EXPLORER SHALL SUBMIT THE INFORMATION NECESSARY FOR THE COMMISSIONER OF NATURAL RESOURCES TO EVALUATE THE VALIDITY OF THE EXPLORER'S CLAIM THAT THE WELL IS DIRECTED AT A DISTINCTLY SEPARATE EXPLORATION TARGET, AND THE COMMISSIONER OF NATURAL RESOURCES SHALL, UPON RECEIPT OF ALL EVIDENCE SUFFICIENT FOR THE COMMISSIONER TO EVALUATE THE EXPLORER'S CLAIM, MAKE THAT DETERMINATION WITHIN 60 DAYS;]

(B) to provide to the Department of Natural Resources, within 30 days after the date of a request, **unless a longer period is provided by the Department of Natural Resources,** specific data sets, ancillary data, and reports identified in (A) of this paragraph; **in this subparagraph,**

(i) a seismic or geophysical data set includes the data for an entire seismic survey, irrespective of whether the survey area covers nonstate land in addition to state land or land in a unit in addition to land outside a unit;

(ii) well data include all derivative products, results, and copies of data collected and data analyses for the well; well logs; sample analyses; geophysical and velocity data including vertical seismic profiles and check shot surveys; and tangible material including, for each whole core collected, a lengthwise cut slab that is at least 1/3 of the whole core volume, and representative samples, as specified by the Department of Natural Resources, of other gaseous, liquid, or solid material collected from drilling or testing the well;

(C) that, notwithstanding any provision of AS 38, information provided under this paragraph will be held confidential by the Department of Natural Resources

(i) in the case of well data, until the expiration of the 24-month period of confidentiality described in AS 31.05.035(c), without extension, after which the Department of Natural Resources [FOR 10 YEARS FOLLOWING THE COMPLETION DATE, AT WHICH TIME THAT DEPARTMENT] will release the information after 30 days' public notice;

(ii) in the case of seismic or other geophysical data, other than seismic data acquired by seismic exploration subject to (1) of this section, for 10 years following the completion date, at which time the Department of Natural Resources will release the information after 30 days' public notice;

(iii) in the case of seismic data obtained by seismic exploration subject to (1) of this section, only until the expiration of 30 days' public notice issued on or after the date the production tax credit certificates are issued under (5) of this subsection; and

(D) that, in the case of well data, the explorer will not make a request under AS 31.05.035(c) that the commissioner of natural resources keep the data confidential for longer than the 24-month period of confidentiality described in AS 31.05.035(c);

(3) if more than one explorer holds an interest in a well or seismic exploration,

(A) each explorer may claim an amount of credit that is proportional to the explorer's cost incurred;

(B) in the case of a well, each explorer holding an interest in the well shall agree, in writing, that the explorer will not make the request described in (2)(D) of this subsection;

(4) the department may exercise the full extent of its powers as though the explorer were a taxpayer under this title, in order to verify that the claimed expenditures are qualified exploration expenditures under this section; and

(5) if the department is satisfied that the explorer's claimed expenditures are qualified under this section and that all data required to be submitted under this section have been submitted, the department shall issue to the explorer two [A] production tax credit certificates, each [CERTIFICATE] for half of the amount of the credit to be allowed against production taxes levied by AS 43.55.011(e); the credit shown on one of the two certificates is available for immediate use; the credit shown on the second of the two certificates may not be applied against a tax for a calendar year earlier than the calendar year following the calendar year in which the certificate is issued, and the certificate must contain a conspicuous statement to that effect; notwithstanding any contrary provision of AS 38, AS 40.25.100, or AS 43.05.230, the following information is not confidential:

(A) the explorer's name;

(B) the date of the application;

(C) the location of the well or seismic exploration;

(D) the date of the department's issuance of the certificate; and

(E) the date on which the information required to be submitted under this section will be released [DUE UNDER AS 43.55.011(e) OR (f)].

* Sec. 33. AS 43.55.025(g) is amended to read:

(g) An explorer, other than an entity that is exempt from taxation under this chapter, may transfer, convey, or sell its production tax credit certificate to any person, and any person who receives a production tax credit certificate may also transfer, convey, or sell the certificate.

* Sec. 34. AS 43.55.025(h) is amended to read:

(h) A producer that purchases a production tax credit certificate may apply the credits against its production tax liability under AS 43.55.011(e) [OR (f)]. Regardless of the price the producer paid for the certificate, the producer may receive a credit against its production tax liability for the full amount of the credit, but for not more than the amount for which the certificate is issued. A production tax credit allowed under this section may not be applied more than once.

* **Sec. 35.** AS 43.55.025(i) is repealed and reenacted to read:

(i) For a production tax credit under this section,

(1) a credit may not be applied to reduce a taxpayer's tax liability under AS 43.55.011(e) below zero for a calendar year; and

(2) an amount of the production tax credit in excess of the amount that may be applied for a calendar year under this subsection may be carried forward and applied against the taxpayer's tax liability under AS 43.55.011(e) in one or more later calendar years.

* **Sec. 36.** AS 43.55.025(k) is amended by adding a new paragraph to read:

(4) "preexisting well" means a well that was spudded more than 540 days but less than 35 years before the date on which the exploration well to which it is compared is spudded.

* **Sec. 37.** AS 43.55.025 is amended by adding a new subsection to read:

(1) Subject to the terms and conditions of this section, if a claim is filed under (f)(1) of this section before January 1, 2016, a credit against the production tax levied by AS 43.55.011(e) is allowed in an amount equal to five percent of an eligible expenditure under this subsection incurred for seismic exploration performed before July 1, 2003. To be eligible under this subsection, an expenditure must

(1) have been for seismic exploration that

(A) obtained data that the commissioner of natural resources considers to be in the best interest of the state to acquire for public distribution; and

(B) was conducted outside the boundaries of a production unit; however, the amount of the expenditure that is otherwise eligible under this section is reduced proportionately by the portion of

the seismic exploration activity that crossed into a production unit; and

(2) qualify under (b)(3) of this section."

Renumber the following bill sections accordingly.

Page 37, line 28:

Delete "Sections 42 - 45 and 48"

Insert "Sections 51 - 54 and 57"

Page 37, line 30:

Delete "and 41"

Insert "34, 35, 37, and 50"

Page 38, line 1:

Delete "Sections 30 - 32"

Insert "Sections 39 - 41"

Page 38, line 2:

Delete "sec. 30"

Insert "sec. 39"

Page 38, line 3:

Delete "sec. 32"

Insert "sec. 41"

Page 38, line 4:

Delete "Section 36"

Insert "Section 45"

Page 38, line 5:

Delete "sec. 36"

Insert "sec. 45"

Page 38, line 6:

Delete "sec. 37"

Insert "sec. 46"

Page 38, line 8:

Delete "37"

Insert "46"

Page 38, following line 8:

Insert a new subsection to read:

"(f) Sections 29 - 32 and 36 of this Act apply to exploration expenditures incurred for work performed after December 31, 2007, that are the bases

of tax credits that may be claimed against taxes levied for oil and gas produced after December 31, 2007."

Page 38, line 25:

Delete "Sections 42 - 45 and 48"

Insert "Sections 51 - 54 and 57"

Page 38, line 27:

Delete "and 30"

Insert ", 29 - 32, 34 - 37, and 39"

Page 39, lines 13 - 14:

Delete "Sections 42 - 45 and 48"

Insert "Sections 51 - 54 and 57"

Page 39, line 15:

Delete "Sections 15 - 28, 30 - 32, and 49"

Insert "Sections 15 - 32, 34 - 37, 39 - 41, and 58"

Page 39, line 16:

Delete "sec. 55"

Insert "sec. 64"

[10:56:57 AM](#)

CHAIR FRENCH objected for discussion purposes.

COMMISSIONER GALVIN said the administration strongly supports all the amendments to the EIC program that were included in the original bill so they would support any that are reinserted here.

CHAIR FRENCH asked for clarification that the provisions were in version "A" and essentially they were written by the administration.

SENATOR THERRIAULT said that's correct; he asked the drafter to reinsert the provisions with no changes to the language.

CHAIR FRENCH withdrew his objection.

[10:58:19 AM](#)

SENATOR HUGGINS stated that he has supported the concept. His concern was that a public airing was needed. That's been done and he's pleased that Senator Therriault offered the amendment.

CHAIR FRENCH announced that without further objection Amendment 6 is adopted.

[10:59:03 AM](#)

SENATOR THERRIAULT moved Amendment 7, labeled 25-GS0014\ K.9.

25-GS0014\K.9
Cook/Bullock

A M E N D M E N T 7

OFFERED IN THE SENATE BY SENATOR THERRIAULT
To: CSSB 2001 (JUD), Draft Version "K"

Page 27, line 16, following "exceed":
Insert "the lesser of \$1,000,000 or"

CHAIR FRENCH objected for discussion purposes.

SENATOR THERRIAULT said the amendment stems from the committee discussion on the Qui Tam provision. When a whistleblower identifies a company that is not properly applying the tax and that results in additional money flowing to the state, there is a 10 percent provision for a reward. Because 10 percent of hundreds of millions of dollars could be a staggering amount of money, this places a \$1 million cap on the reward. Although he isn't wedded to the particular amount, it might not be out of line if somebody is willing risk their job to bring beneficial information to the state.

[11:00:21 AM](#)

SENATOR HUGGINS said he won't object to the \$1 million, but he does intend to discuss what the number ultimately should be in the Finance Committee.

CHAIR FRENCH said he has no objection to the concept of a cap. Now probably isn't the time to quibble about where to draw the line. Withdrawing his objection and finding no further objection, he announced that Amendment 7 is adopted.

[11:01:22 AM](#)

SENATOR MCGUIRE moved Amendment 8. [Original punctuation provided] She explained that the amendment levels the playing field and treats gas basins in any part of the state the same way that Cook Inlet is treated. She asked Commissioner Galvin to give his perspective.

AMENDMENT 8

AMENDMENT TO CSSB 2001(JUD)

Page 2, line 2 following "LEGISLATIVE INTENT." Through line 5:

Delete all material

Insert:

"It is the intent of the legislature that provisions of this Act will ensure a fair and equitable means of assessing and taxing Alaska's oil and gas resources; encourage the availability to Alaska's citizens of affordable gas produced, transported, and consumed within Alaska; and confirm by clarification the long-standing interpretation of AS 43.55.075(b), enacted by sec. 37 of this Act, relating to limitation of assessments for the production tax on oil and gas and conservation surcharges on oil."

Page 11, line 3:

Following "(j),":

Delete "and"

Following "(k),":

Insert "and (o)"

Page 11, following line 6:

Insert a new bill section to read:

"*Sec. 16. AS 43.55.011(f) to read:

(f) The levy of tax under this section on a producer of oil and gas produced north of 68 degrees North latitude, **other than gas subject to (o) of this section,** may not be less than

(1)four percent of the gross value at the point of production when the average price per barrel for Alaska North Slope crude oil for sale on the United States West Coast during the calendar year for which the tax is due is more than \$25;

(2)three percent of the gross value at the point of production when the average price per

barrel for Alaska North Slope crude oil for sale on the United States West Coast during the calendar year for which the tax is due is over \$20 but not over \$25;

(3)two percent of the gross value at the point of production when the average price per barrel for Alaska North Slope crude oil for sale on the United States West Coast during the calendar year for which the tax is due is over \$17.50 but not over \$20;

(4)one percent of the gross value at the point of production when the average price per barrel for Alaska North Slope crude oil for sale on the United States West Coast during the calendar year for which the tax is due is over \$15 but not over \$17.50; or

(5)zero percent of the gross value at the point of production when the average price per barrel for Alaska North Slope crude oil for sale on the United States West Coast during the calendar year for which the tax is due is \$15 or less."

Renumber the following bill sections accordingly.

Page 13, line 7:

Following "against":

Delete "the"

Insert "**that** [THE]

Following "tax":

Delete "levied by (e) of this section"

Insert "[LEVIED BY (e) OF THIS SECTION]"

Page 13, line 8:

Delete "for [ON] that gas"

Insert "[ON THAT GAS]"

Insert "and tax credits under AS 38.05.180(i), AS 41.09.010, AS 43.20.043, AS 43.55.024, and AS 43.55.025 that are allocated to gas subject to (o) of this section and that are available to be applied against a tax levied by (e) of this section for that gas during a calendar year may be applied only against that tax"

Page 13, line 9:

Following "basin":

Insert "or to gas subject to (o) of this section, respectively,"

Page 13, line 12:

Following "that":

Insert "respective"

Page 13, line 13:

Following "following":

Insert ", applied separately for the Cook Inlet sedimentary basin and for gas subject to (o) of this section, respectively"

Page 13, line 15:

Following "section" as first appearing:

Insert "or under (o) of this section"

Page 13, line 26:

Insert a new bill section to read:

"*Sec. 21. AS 43.55.011(n) is amended to read:

(n)Allocation of credits under (m) of this section shall be made under regulations adopted by the department that provide for reasonable methods of allocating tax credits to gas produced from leases or properties in the Cook Inlet sedimentary basin and to gas subject to (o) of this section. The method of allocating tax credits available under AS 43.55.024 shall be based in the number of BTU equivalent barrels produced from a lease or property."

Page 13, line 27:

Insert a new bill section to read:

"*Sec. 22. AS 43.55.011 is amended to read:

(o)For a calendar year before 2022, the tax levied by (e) of this section per 1,000 cubic feet of gas for gas produced from a lease or property outside the Cook Inlet sedimentary basin and used in the state may not exceed the amount of tax per 1,000 cubic feet of gas that as determined under section (j)(2) of this section."

Renumber the following bill sections accordingly.

Page 28, line 10:

Following "latitude":

Insert ", other than gas subject to AS 43.55.011(o),"

Page 28, line 18:

Following "latitude":

Insert "other than gas subject to AS 43.55.011(o),"

Page 29, line 8:

Following "latitude":

Insert ", other than gas subject to AS 43.55.011(o),"

Page 29, line 16:

Following "latitude":

Insert "other than gas subject to AS 43.55.011(o),"

Page 29, line 5:

Insert:

"(E) gas produced during a calendar year from a lease or property outside the Cook Inlet sedimentary basin and used in the state is the gross value at the point of production of that gas taxable under AS 43.55.011(e) and produced by the producer from that lease or property, less the producer's lease expenditures under AS 43.55.165 for the calendar year applicable to that gas produced by the producer from that lease or property, as adjusted under AS 43.55.170;"

Page 30, line 4, following "AS 43.55.170":

Insert: "i

"(E) gas produced during a month from a lease or property outside the Cook Inlet sedimentary basin and used in the state is the gross value at the point of production of that gas taxable under AS 43.55.011(e) and produced by the producer from that lease or property, less 1/12 of the producer's lease expenditures under AS 43.55.165 for the calendar year applicable to that

gas produced by the producer from that lease or property, as adjusted under AS 43.55.170"

Page 35, following line 12:

Insert: a new bill section to read:

"*Sec. 45. AS 43.55.165(h) is amended to read:

(h)The department shall adopt regulations that provide for reasonable methods of allocating costs between oil and gas **between gas subject to AS 43.55.011(o) and other gas,** and between leases or properties in those circumstances where the determination of the lease expenditures that are applicable to oil or to gas, **that are applicable to gas subject to AS 43.55.011(o) or to other gas,** or that are applicable to oil and gas produced from different leases or properties, requires an allocation of costs."

Renumber the following bill sections accordingly.

CHAIR FRENCH welcomed Senator Green, Senator Stevens and Senator Thomas to the committee.

[11:02:58 AM](#)

COMMISSIONER GALVIN relayed that different legislators were trying to address this in various ways depending on the particular interests in their areas, but there was a common theme. This amendment addresses the various interests and says that if gas is going to be produced for in-state purposes, it will be taxed for production tax purposes, under the calculation that's used for Cook Inlet. It provides what amounts to a ceiling for all in-state gas use under the production tax calculation.

[11:05:16 AM](#)

CHAIR FRENCH observed that it has the affect of treating Fairbanks consumers the same as Anchorage consumers.

COMMISSIONER GALVIN said yes with respect to gas and to the extent that the production tax is passed along to consumers.

SENATOR WIELECHOWSKI said he likes the concept but he wants to make sure it's tight enough. First he asked how "used in the state" is defined. Second he said, "If we get a gas pipeline from the North Slope and we're exporting huge amounts of gas in-

state, I'm assuming that that will be included in this. In other words, that we will not receive tax benefits from that."

COMMISSIONER GALVIN said that's correct. Any gas that's exported from the state has the regular production tax requirements. With regard to a definition for gas used in the state, he said that isn't included so by default it would be the common use of the term. Adding clarification he said first it has to be gas that's produced and used as a commodity and then it has to be used within the state. The gas that's currently being cycled is not going to be affected by this, he said.

CHAIR FRENCH asked if this differentiates between residential and industrial use.

COMMISSIONER GALVIN said no and there is no volume restriction.

[11:07:34 AM](#)

SENATOR THERRIAULT said this is potentially beneficial to the consumers in Fairbanks who have access to a limited but building distribution network for home heating. This amendment will help expand that network once more gas is available. He noted that different groups around the state are running into problems with the status quo, because they have to run all their economics knowing that the additional tax burden has to be passed along to the consumer. He said he's pleased that the administration has come up with something that appears to work for all areas although it's likely that the issue will need to be revisited once gas is exported.

[11:09:00 AM](#)

CHAIR FRENCH stated that Amendment 8 has been moved and he is objecting for the purpose of further discussion.

SENATOR HUGGINS stated, "I request upfront that we declare when we're going to deal with gas."

CHAIR FRENCH withdrew his objection to Amendment 8. Finding no further objection, he announced that Amendment 8 is adopted.

At ease from [11:10:42 AM](#) to [11:33:42 AM](#).

CHAIR FRENCH said asked for a motion to adopt Amendment 9 by Senator Wielechowski.

SENATOR WIELECHOWSKI moved Amendment 9, labeled 25-GS0014\K.1. [The amendment is conceptual with regard to the dates.]

A M E N D M E N T 9

OFFERED IN THE SENATE BY SENATOR WIELECHOWSKI
CSSB 2001(JUD), Draft Version "K"

Page 2, line 2, following "INTENT":
Insert "(a)"

Page 2, following line 5:
Insert a new subsection to read:
"(b) It is the intent of the legislature that the amount of money received by the state as a result of the retroactivity of certain provisions under sec. 54 of this Act that exceeds the amount the state would have received if those provisions had not been made retroactive will be appropriated to the budget reserve fund (art. IX, sec. 17, Constitution of the State of Alaska)."

Page 37, line 29:
Delete "March 31, 2006"
Insert "December 31, 2006"

Page 38, lines 25 - 26:
Delete "April 1, 2006"
Insert "January 1, 2007"

Page 39, line 2:
Delete "April 1, 2006"
Insert "January 1, 2007"

Page 39, line 14:
Delete "April 1, 2006"
Insert "January 1, 2007"

CHAIR FRENCH objected for discussion purposes.

SENATOR WIELECHOWSKI explained that this amendment will make the bill that's enacted retroactive to January 1, 2007, which will have a significant impact on the state treasury. Also, the intent language makes it clear that the additional money will be deposited in the Constitutional Budget Reserve Fund (CBR).

Deferring to Mr. Bullock for an explanation, he said the dates will need some conceptual changes.

[11:35:23 AM](#)

MR. BULLOCK said he has a question about the amendment. His understanding is that the provisions that would have otherwise been effective on January 1, 2008 will now become effective January 1, 2007 because other parts of the bill have earlier effective dates. For example, the corrosion amendments go back to March 31, 2006.

SENATOR WIELECHOWSKI stated, "The intent of this amendment is to have the production tax aspect of the bill retroactive to January 1, 2007."

MR. BULLOCK responded the deductibility of lease expenditures is a production tax related event that's retroactive to March 31, 2006. If that is changed to January 1, 2007, those deductions would be allowed during 2006. "I think what you're trying to do is the changes in the tax rate and the change in the floor and other changes that relate to the change in the tax structure after that that don't include the expenditures would now become effective January 1, 2007 rather than 2008." If that's correct, the substantive part of the tax, other than lease expenditures and provisions that are retroactive to March 31 or some date earlier than January 1, 2007 would continue with the earlier effective dates. The other provisions that would have come into effect after the end of this year would instead start at the beginning of this year.

SENATOR WIELECHOWSKI thanked him for the explanation.

MR. BULLOCK continued to say that the amendment only changes the provisions of the bill that would not otherwise have been effective until January 1, 2008. However, changing the tax back to January 1, 2007 brings up issues related to the installment payments that the taxpayers were supposed to be making during the year. Thus, applicability and transition language needs to be added in uncodified sections of the bill to give some direction to the Department of Revenue and the taxpayers. For example, consider whether the taxpayers should make true-up payments in the next few months. That's the kind of substantive decision you should be making, he said. Then language can be drafted to explain how this retroactive law will affect what's already happened this year.

[11:39:16 AM](#)

SENATOR WIELECHOWSKI stated his intent is not to penalize. "The appropriate method is to have this resolved at the next true-up." That's on or before April 1. Mr. Bullock and Commissioner Galvin agreed.

CHAIR FRENCH asked Senator Wielechowski if that's his intent.

SENATOR WIELECHOWSKI said yes.

MR. BULLOCK clarified that the conceptual part of the amendment will be to provide applicability in the transition language and provide for the true-up to incorporate the increased tax for 2007 that comes as a result of the retroactivity.

[11:40:06 AM](#)

SENATOR HUGGINS highlighted the tremendous debt in the public employee retirement fund and said he intends to add broadening provisions in the Finance Committee. Stating that retroactive dates make him particularly nervous when they involve taxes, he said he also intends to bring that provision up for further review.

CHAIR FRENCH said he too had qualms about reaching back but this is fair and he particularly appreciates that all the money coming from retroactivity will go into savings.

SENATOR HUGGINS stated support for the basic concept of budgetary frugality and publicly challenged the administration to come in with some restraint in the operating budget.

[11:42:53 AM](#)

CHAIR FRENCH said he particularly appreciates the reference to the PERS/TRS debt. There are a number of worthy places to save money but in his mind the CBR is the state's savings account so you start there and move forward. "Also, in my heart of hearts I know that finance will work this provision over," he stated.

SENATOR THERRIAULT agreed that everyone might say the money should be saved for a different purpose, but the common thread is that everyone believes the money should be saved. Money that's placed in the CBR could be removed during the next regular session to pay down PERS/TRS or whatever. We're striving to have the money to potentially have the luxury to do that, he said.

CHAIR FRENCH asked Commissioner Galvin to give his thoughts on retroactivity and saving money.

[11:44:11 AM](#)

COMMISSIONER GALVIN stated that the administration supports the amendment in terms of the retroactivity and in particular saving the money. The theme throughout the ACES discussion has been the need to save money that comes in when oil is selling at a premium. He noted that the estimated fiscal impact for current FY08 revenue and retroactive FY07 revenue is in the neighborhood of \$1.2 billion.

CHAIR FRENCH said the figure makes him stutter and then he withdrew his objection to Amendment 9.

SENATOR WIELECHOWSKI clarified that the dates stated in the amendment are conceptual and will be corrected by Mr. Bullock and reviewed in finance.

CHAIR FRENCH found no further objection and announced that Amendment 9 is passed.

[11:46:03 AM](#)

CHAIR FRENCH said the next item is Amendment 10, labeled 25-GS0014\M.2.

SENATOR HUGGINS moved Amendment 10.

25-GS0014\M.2
Kurtz/Bullock

A M E N D M E N T 10

OFFERED IN THE SENATE
TO: CSSB 2001(RES)

Page 1, following line 8:
Insert a new bill section to read:

"* **Section 1.** AS 37.10 is amended by adding a new section to read:

Sec. 37.10.440. Appropriations to the budget reserve fund of production tax revenue. (a) By February 1 of each year, the Department of Revenue shall determine the amount of money received by the state for the general fund during the immediately preceding calendar year from the tax levied under AS 43.55.011, as well as the amount the state would have received that year from the tax levied under AS 43.55.011 under the law in effect immediately

before January 1, 2008. If the amount received is greater than the amount that would have been received under AS 43.55.011 under the law in effect immediately before January 1, 2008, the department shall report the difference between the two amounts to the legislature.

(b) The legislature may appropriate 50 percent of the amount identified by the Department of Revenue under (a) of this section to the budget reserve fund (art. IX, sec. 17, Constitution of the State of Alaska).

(c) Nothing in this section requires that money be appropriated or creates a dedicated fund."

Renumber the following bill sections accordingly.

Page 23, line 3:

Delete "Sections 21, 22, and 25"
Insert "Sections 22, 23, and 26"

Page 23, line 5:

Delete "Sections 19, 20, and 26"
Insert "Sections 20, 21, and 27"

Page 23, line 7:

Delete "Sections 14 and 16"
Insert "Sections 15 and 17"

Page 23, line 8:

Delete "sec. 14"
Insert "sec. 15"

Page 23, line 9:

Delete "sec. 16"
Insert "sec. 17"

Page 23, line 19:

Delete "sec. 9"
Insert "sec. 10"

Page 23, line 22:

Delete "sec. 9"
Insert "sec. 10"

Page 23, line 25:

Delete "sec. 9"
Insert "sec. 10"

Page 24, line 6:

Delete "secs. 21, 22, and 25"

Insert "secs. 22, 23, and 26"

Page 24, line 8:

Delete "secs. 13, 14, 16, 19, 20, and 26"

Insert "secs. 14, 15, 17, 20, 21, and 27"

Page 24, lines 25 - 26:

Delete "Sections 21, 22, 25, and 29"

Insert "Sections 22, 23, 26, and 30"

Page 24, line 27:

Delete "Sections 13, 14, 16, 19, 20, and 26"

Insert "Sections 14, 15, 17, 20, 21, and 27"

Page 24, line 28:

Delete "sec. 32"

Insert "sec. 33"

CHAIR FRENCH objected for discussion purposes. This amendment looks forwards, he said. The intent is to calculate on an annual basis the difference between what will be taken in under ACES and what would have come in under the current PPT. The Department of Revenue is to report that number to the legislature and then 50 percent is to be deposited in the CBR.

[11:48:00 AM](#)

MR. BULLOCK asked if there is a desire to change the dates on lines 9 and 11 to January 1, 2007 in light of the amendment that just passed.

CHAIR FRENCH acknowledged that it would conform to the amendment that just passed.

COMMISSIONER GALVIN opined that it would be confusing because the amendment that just passed drops all the money for that year in the CBR and this amendment says the difference goes in.

MR. BULLOCK said his question relates to which two taxes are being compared and for what period.

CHAIR FRENCH said the comparison is PPT as it passed the 24th Legislature versus ACES should it pass the 25th Legislature. He asked if the intent is clear.

MR. BULLOCK said the law that will be in effect before January 2008 will now be the amendment.

[11:49:06 AM](#)

CHAIR FRENCH said he sees the date issue in the amendment; he wants to know if the intent is clear.

MR. BULLOCK stated, "The law in effect in 2007 will be the law in effect immediately before January 1, 2008. ... Under the amendment that just passed, the law that's effective in 2007 is ACES as modified by the CS."

COMMISSIONER GALVIN suggested the easiest way to address that is on page 1, line 5 following "year" insert "beginning in 2009".

CHAIR FRENCH asked about 2008.

COMMISSIONER GALVIN explained that the calculation starts in 2009 and it looks at the 2008 calendar year.

MR. BULLOCK said two things are going on here. First you're comparing PPT to ACES. PPT was in effect before January 1, 2007 so that's the base comparison. Second you determine when you'll start paying and how much will be paid into the CBR. The first amount that's appreciated by the state will go under the intent of Senator Wielechowski's previous amendment. Starting with the first report in 2009, the amount that's appreciated by the state goes for the purpose expressed in this amendment.

At ease from [11:52:17 AM](#) to [12:09:45 PM](#).

CHAIR FRENCH moved an amendment to the amendment as follows:

Page 1, lines 7-11 of Amendment 10 will read as follows:

"immediately preceding calendar year from the tax levied under AS 43.55[.011], as well as the amount the state would have received that year from the tax levied at the rates under AS 43.55.011(e) and (g) under the law in effect immediately before January 1, 2007 [2008]. If the amount received is greater than the amount that would have been received at the tax rates [UNDER AS 43.55.011] under the law in effect immediately before January 1, 2007 [2008],"

CHAIR FRENCH said the idea is to lessen the burden on the Department of Revenue. They will make a rough calculation of what the old tax would have taken in and compare that to what the new tax takes in. That will be reported to the legislature and half that difference will be placed in a savings account.

[12:11:26 PM](#)

COMMISSIONER GALVIN thanked Chair French for working with him. He said he's had experience with having to keep dual books to track just one calculation. That essentially doubles the accounting so he's sensitive to the unintended consequences of having a law that requires a quick calculation. He understands that the intent here is to say that a calculation will be made under PPT and then under ACES and the difference is the number that falls into this category. The additional administrative burden should be moderate, he said.

[12:13:12 PM](#)

CHAIR FRENCH found no objection and announced that the amendment to the amendment is adopted and Amendment 10 is again before the committee. He asked if there is further objection or comment to Amendment 10.

SENATOR THERRIAULT stated that he would like to be shown as a sponsor of Amendment 10.

CHAIR FRENCH announced that Chair French, Senator Therriault and Senator Wielechowski are sponsors. Finding no further objection he announced that Amendment 10 is adopted.

[12:13:57 PM](#)

SENATOR THERRIAULT relayed that Senator Dyson has said that he will review this in the Finance Committee and more than likely he will be supportive.

[12:14:11 PM](#)

CHAIR FRENCH announced that Amendment 11 by Senator Therriault is next.

SENATOR THERRIAULT moved Amendment 11, labeled 25-GS0014\K.13.

25-GS0014\K.13
Luckhaupt/Bullock

A M E N D M E N T 11

OFFERED IN THE SENATE

BY SENATOR THERRIAULT

TO: CSSB 2001(JUD), Draft Version "K"

Page 27, line 25:

Delete "or is not representative"

Insert "requiring payment [OR IS NOT REPRESENTATIVE]"

Page 27, line 30:

Delete "the conditions"

Insert "a condition [THE CONDITIONS]"

Page 27, line 31:

Delete "are"

Insert "is [ARE]"

Page 28, lines 3 - 4:

Delete "properly on file with"

Insert "that have been adjudicated just and reasonable by [PROPERLY ON FILE WITH]"

CHAIR FRENCH objected for discussion purposes.

SENATOR THERRIAULT explained that this amendment addresses the issue of actual versus reasonable with regard to transportation costs. He referred to an e-mail from Ms. Thompson and said her comments were sent to the drafters. He read the amendment for her benefit and asked her to speak to the concepts.

[12:15:13 PM](#)

NANETTE THOMPSON, Division of Oil & Gas, Department of Natural Resources, Anchorage, AK, said the first provision addresses a concern Senator McGuire expressed last night. The intent is to clarify the exception. Removing the extra "or" does not change the intent, she said.

SENATOR THERRIAULT confirmed that this addresses Senator McGuire's concern.

MS. THOMPSON said last night there was debate about deleting the last sentence in Sec 40. She believes the suggested change addresses the problem, which is that just having a rate on file isn't any representation that it's been reviewed by the regulatory agency. It seems that the committee's intent is to make sure that whatever tariff rates are allowed are reasonable ones, she said.

[12:18:48 PM](#)

SENATOR THERRIAULT added that this addresses his concern that a rate must be adjudicated by the regulatory agency.

CHAIR FRENCH asked if the negotiated rates on file would have any precedential value.

MS. THOMPSON explained that a negotiated rate that's on file wouldn't have been adjudicated just and reasonable by the regulatory agency. Therefore it would not be the basis for calculating this deduction.

CHAIR FRENCH asked the implication of that.

MS. THOMPSON said the concern relates to getting a reasonable rate rather than just an actual rate. Because of the way rates are set and reviewed, it's not uncommon for a rate to be on file and in effect for a period of time before it's reviewed and it might be too high. TAPS, for example, was on file for 6 years before a regulatory agency made the decision that it was not the right rate. The idea here is to create a standard for DOR to use when determining what reasonable rates are. If a rate has been reviewed and the appropriate regulatory agency has determined it is just and reasonable, that should work, she stated.

[12:20:48 PM](#)

SENATOR THERRIAULT asked for clarification that if no rate has been adjudicated just and reasonable, the department would not be precluded from looking at a negotiated rate.

MS. THOMPSON agreed that DOR could look at a negotiated rate and determine it is fair. She added that the previous section says it's the actual rate paid unless one of the exceptions in Sec. 39 applies.

[12:21:45 PM](#)

SENATOR WIELECHOWSKI expressed concern about the change on page 27, line 25. Removing the "or" could create a difficult situation because it could be argued that the market value of the transportation is whatever the market will bear, he stated.

MS. THOMPSON said the intent is to define the circumstances where the rate that's paid might not be reasonable.

[12:24:09 PM](#)

MR. BULLOCK opined that paragraph (2) is really two conditions. You start with the contract of transportation of oil or gas and ask if it's an arms length transaction. If it isn't, that

triggers the use of reasonable rather than actual cost. The second part is the contract of transportation of oil or gas and asking if it is representative of the market value. That's a separate trigger, he said. If the "or" is removed you're only dealing with a contract for transportation of oil and gas that's not an arms length contract. Then only the contracts that are not arms length transaction require payment at market value. He suggested a rewrite to clarify that it is two conditions. First, the contract for the transportation of oil or gas is not an arms length transaction. Then insert a new paragraph that says that the contract for the transportation of oil or gas is not representative of the market value of the transportation.

[12:25:36 PM](#)

COMMISSIONER GALVIN offered the view that changing the "and" to "or" makes it a 4 part test. The problem is that the portion that says, "the contract is not representative of the market value of that transportation" is the definition of why the other three conditions are in the list. It's the test that's used to say it's going to be the actual cost except when there's a reason to look into it. You would look into it if it's affiliated, if it's not arms length, or if it's not reasonable in view of alternative methods, he said.

CHAIR FRENCH asked if his suggestion is to drop the second half of paragraph (2).

COMMISSIONER GALVIN said his suggestion is to blend that as part of the arms length test. The purpose of the second portion is to say if it's not an arms length transaction requiring payment of market value, you'll look at something other than actual costs.

[12:28:04 PM](#)

CHAIR FRENCH asked for clarification that he's now defending the amendment as it was moved.

COMMISSIONER GALVIN said that's correct.

SENATOR WIELECHOWSKI agree with Mr. Bullock . "If we take out that "or" we kind of go back to where we were in the first place," he said . Dropping the "or" changes the entire interpretation of the test.

CHAIR FRENCH asked if he's making an amendment to the amendment.

[12:28:49 PM](#)

SENATOR WIELECHOWSKI said yes and asked Mr. Bullock for help.

MR. BULLOCK suggested the following for the amendment to the amendment:

After "contract for the transportation of oil or gas" insert subparagraph (A) "is not an arms length transaction" or subparagraph (B) "does not require the payment at market value of that transportation".

SENATOR WIELECHOWSKI agreed that would be acceptable.

MR. BULLOCK added, "You look at a contract. If it is not an arms length transaction, then that triggers the use of reasonable rather than actual. If it's a contract for transportation of oil or gas that does not require the payment at market value, then that triggers the reasonable over actual."

SENATOR WIELECHOWSKI stated that that is his intent.

MR. BULLOCK explained that paragraphs (1), (2), and (3) were in the alternative before PPT was enacted. PPT took out the "or" and made it "and" so that all three paragraphs were required for reasonable to be substituted for actual.

[12:30:22 PM](#)

SENATOR HUGGINS stated that he would be a no vote on the amendment and the amendment to the amendment because things are too fluid.

CHAIR FRENCH asked Ms. Thompson to comment on the amendment to the amendment.

MS. THOMPSON said she believes it resolves the issue she was attempting to address in the amendment. She has no objection to the committee taking this approach.

[12:31:24 PM](#)

SENATOR THERRIAULT said as the maker of the original amendment he will support the amendment to the amendment.

A roll call vote was taken. The amendment to the amendment passed 3:1 with Senator Therriault, Senator Wielechowski, and Chair French voting yea and Senator Huggins voting nay.

CHAIR FRENCH announced that Amendment 11 is back before that committee. He asked if there is further discussion.

SENATOR THERRIAULT stated that he believes the language is clear and he has no further comment.

SENATOR WIELECHOWSKI opined that having the "and" rather than the "or" has probably cost the state \$3 billion. This amendment will save \$160 million per year. "I am a strong supporter of the amendment," he stated.

CHAIR FRENCH withdrew his objection to Amendment 11 and asked if there is further objection.

SENATOR HUGGINS maintained his objection to Amendment 11.

A roll call vote was taken. Amendment 11 passed 3:1 with Senator Wielechowski, Senator Therriault, and Chair French voting yea and Senator Huggins voting nay.

At ease from [12:33:20 PM](#) to [12:35:22 PM](#).

CHAIR FRENCH stated that Amendment 12, labeled 25-GS0014\K.10, by Senator Wielechowski is next.

SENATOR WIELECHOWSKI moved Amendment 12.

25-GS0014\K.10
Bullard/Bullock

A M E N D M E N T 1 2

OFFERED IN THE SENATE BY SENATOR WIELECHOWSKI
TO: CSSB(JUD), Draft Version "K"

Page 25, following line 16:

Insert a new subsection to read:

"(c) If an understatement of tax under (a) or (b) of this section is identified as a result of information provided to the department by a person about another person's noncompliance with the provisions of this chapter, there is added an additional penalty, equal to 10 percent of the substantial or gross underpayment, to the penalties established by (a) and (b) of this section."

Reletter the following subsection accordingly.

CHAIR FRENCH objected for discussion purposes.

12:35:55 PM

SENATOR WIELECHOWSKI explained that the amendment relates to the Qui Tam provision that was added. It ensures that when a whistleblower notifies the state about a substantial underpayment of tax, the offender would be required to pay a penalty equal to 10 percent so that the state treasury wouldn't be impacted. "Essentially it makes it revenue neutral," he said.

SENATOR THERRIAULT stated that if the amendment were offered conceptually Mr. Bullock could conform it to the cap. "I wouldn't want to levy a fine back on the taxpayer that's above what was actually given out as a reward," he said.

CHAIR FRENCH asked Mr. Bullock if he understands the idea.

MR. BULLOCK asked if the question relates to the Qui Tam award which is up to 10 percent and the penalty which is 10 percent.

SENATOR THERRIAULT explained the provisions of Amendment 7 that the committee passed earlier and said he doesn't want to charge the taxpayer more than the reward that's paid out.

MR. BULLOCK said this treads closely to dedicating funds. It ought to be treated as a stand alone penalty even though the intention is to use the penalty as the source for revenue that could be appropriated to pay the reward, he stated.

12:38:11 PM

SENATOR THERRIAULT asked about saying that the two amounts will be equal.

MR. BULLOCK said this is a penalty imposed on the taxpayer for not doing something that they were supposed to do. It's not imposed because an informant was involved. To base it on something that's out of the taxpayer's control, particularly with the flexible penalty, doesn't change the nature of the bad act.

SENATOR WIELECHOWSKI asked if he has concerns about the constitutionality of the provision.

MR. BULLOCK said the penalty is stand alone and it's okay as written. It essentially amounts to a penalty against an employer for hiring a whistleblower.

SENATOR WIELECHOWSKI withdrew Amendment 12.

[12:40:55 PM](#)

SENATOR THERRIAULT drew attention to language on page 27, lines 17-18, that says state employees are not eligible for the reward under this section. He asked if the language is broad enough to ensure that contract auditors wouldn't be eligible for the reward.

MR. BULLOCK said it's not broad enough to cover contractors or agents of the state.

At ease from [12:42:05 PM](#) to [12:44:43 PM](#).

SENATOR THERRIAULT moved conceptual Amendment 13 as follows:

AMENDMENT 13

Page 27, line 18, following "employee":
Insert "or an agent of the state"

SENATOR THERRIAULT said this highlights the issue that people who are hired and compensated to do a job shouldn't be rewarded for doing their job.

CHAIR FRENCH announced that without objection Amendment 13 is adopted.

At ease from [12:45:38 PM](#) to [1:12:30 PM](#).

CHAIR FRENCH reconvened the hearing and announced that Amendment 14, labeled 25-GS0014\K.12 is next.

SENATOR WIELECHOWSKI moved Amendment 14.

25-GS0014\K.12
Bullard/Bullock

A M E N D M E N T 14

OFFERED IN THE SENATE BY SENATOR WIELECHOWSKI
TO: CSSB 2001(JUD), Draft Version "K"

Page 25, following line 16:
Insert a new subsection to read:

"(c) In addition to the penalties imposed under (a) or (b) of this section, a person who has made a substantial or gross underpayment of tax is liable to the state for the reasonable costs of the state's

enforcement action, including auditing costs, under this section."

Reletter the following subsection accordingly.

CHAIR FRENCH objected for discussion purposes.

SENATOR WIELECHOWSKI explained that the amendment addresses the situation where there's a substantial or gross underpayment of tax. In that event the liability for the auditing costs is assigned to the offender. He noted that a slight change is necessary.

CHAIR FRENCH asked if he's offering an amendment to the amendment.

[1:13:23 PM](#)

SENATOR WIELECHOWSKI said yes and moved an amendment to the amendment as follows: [Mr. Bullock offered punctuation]

Line 6
Delete "under this section."

Line 5 following "costs":
Delete ","
Insert "."

SENATOR WIELECHOWSKI asked Mr. Bullock if that accurately reflects his understanding.

At ease from [1:14:26 PM](#) to [1:19:19 PM](#) due to microphone problems.

MR. BULLOCK recapped the amendment.

CHAIR FRENCH announced that without objection the amendment to the amendment carries and Amendment 14 is before the committee.

CHAIR FRENCH asked if there are other areas of law where costs are assigned to a wrongdoing party.

SENATOR WIELECHOWSKI replied this isn't out of the ordinary.

MR. BULLOCK recalled that the utility regulation is an example.

MS. THOMPSON confirmed that enforcement costs sometimes show up in rate cases with a proposal to pass them on.

[1:21:16 PM](#)

SENATOR WIELECHOWSKI pointed out that if you don't pay your credit card you'll be subject to penalties, interest and various fees. "It's very standard and very common," he said.

CHAIR FRENCH said that's his understanding as well. He's simply building a record. He withdraw his objection to Amendment 14. Finding no further objection, he announced that Amendment 14 passes.

CHAIR FRENCH said the last amendment embodies the concept of Amendment 5. He understands that it's been thoroughly worked over by the maker, legislative legal, and the commissioner.

At ease from [1:23:02 PM](#) to [4:15:00 PM](#).

CHAIR FRENCH reconvened the hearing and announced that Amendment 15 by Senator Wielechowski is next.

[4:15:14 PM](#)

SENATOR WIELECHOWSKI moved Amendment 15 as follows:

AMENDMENT 15

OFFERED IN THE SENATE

TO: CSSB 2001(JUD) Draft Version "K"

Section 10

Page 9, line 17

Following "Revenue," insert **"and the Department of Natural Resources"**

Section 51

Page 38, line 14:

Following "Revenue," insert **"and no more than two oil and gas revenue audit manager positions to be created in the Department of Natural Resources."**

CHAIR FRENCH objected for discussion purposes.

SENATOR WIELECHOWSKI explained that under version "M", every auditor who was classified was moved into exempt service. The goal of the amendment is to protect the bargaining unit members and give the department the flexibility to hire the super auditors that are needed to protect the state treasury.

[4:17:33 PM](#)

COMMISSIONER GALVIN said the administration appreciates the effort to balance the various concerns. "We believe that with the amendments provided and with the language in the CS that we can meet our requirements and what we're trying to get on the audit side," he stated.

SENATOR WIELECHOWSKI asked the administration to clarify that there is no intent to strip members from the classified service.

COMMISSIONER GALVIN said, "The language in the legislative intent matches our intent, which is that there would be four positions that would be created within the Department of Revenue, two within the Department of Natural Resources."

[4:19:05 PM](#)

CHAIR FRENCH removed his objection. Finding no further objection, he announced that Amendment 15 is adopted.

CHAIR FRENCH said Amendment 16, labeled 25-GS0014\K15, is the last amendment to be offered.

SENATOR WIELECHOWSKI moved Amendment 16.

25-GS0014\K.15
Bullock

A M E N D M E N T 16

OFFERED IN THE SENATE

BY SENATOR WIELECHOWSKI

TO: CSSB 2001(JUD), Draft Version "K"

Page 30, line 28, through page 31, line 30:

Delete all material and insert:

"* Sec. 43. AS 43.55.165(b) is amended to read:

(b) For purposes of (a) of this section,

(1) direct costs include

(A) an expenditure, when incurred, to acquire an item if the acquisition cost is otherwise a direct cost, notwithstanding that the expenditure may be required to be capitalized rather than treated as an expense for financial accounting or federal income tax purposes;

(B) payments of or in lieu of

(i) property taxes for properties on which oil and gas exploration, development, or production is taking place; and

(ii) [,] sales and use taxes, motor fuel taxes, and excise taxes related to transactions or activities involving oil or gas exploration, development, or production;

(C) supplies to be used for oil or gas exploration, development, or production [A REASONABLE ALLOWANCE, AS DETERMINED UNDER REGULATIONS ADOPTED BY THE DEPARTMENT, FOR OVERHEAD EXPENSES DIRECTLY RELATED TO EXPLORING FOR, DEVELOPING, AND PRODUCING OIL OR GAS DEPOSITS LOCATED WITHIN LEASES OR PROPERTIES OR OTHER LAND IN THE STATE];

(D) purchased fuel;

(E) routine maintenance;

(F) the wages and benefits of employees who are directly participating in exploration, development, or production operations; and

(G) other direct costs as may be established in regulations adopted by the department;

(2) in determining whether costs are lease expenditures, the department may consider, among other factors, the

(A) typical industry practices and standards in the state that determine the costs, other than items listed in (e) of this section, that an operator is allowed to bill a producer that is not the operator, under unit operating agreements or similar operating agreements that were in effect before December 2, 2005, and were subject to negotiation with at least one producer with substantial bargaining power, other than the operator; and

(B) standards adopted by the Department of Natural Resources that determine the costs, other than items listed in (e) of this section, that a lessee is allowed to deduct from revenue in calculating net profits under a lease issued under AS 38.05.180(f)(3)(B), (D), or (E) [AN ACTIVITY DOES NOT NEED TO BE PHYSICALLY LOCATED ON, NEAR, OR WITHIN THE PREMISES OF THE LEASE OR PROPERTY WITHIN WHICH AN OIL OR GAS DEPOSIT BEING EXPLORED FOR, DEVELOPED, OR PRODUCED IS LOCATED IN ORDER FOR THE COST OF THE ACTIVITY TO BE A COST UPSTREAM OF THE POINT OF PRODUCTION OF THE OIL OR GAS]."

Page 32, lines 14 - 16:

Delete

"(8) costs of arbitration, litigation, or other dispute resolution activities that involve the state or concern the rights or obligations among owners of interests in, or rights to production from, one or more leases or properties or a unit;"

Insert

"(8) costs of arbitration, litigation, [OR OTHER] dispute resolution activities, lobbying, public relations, advertising, or policy advocacy [THAT INVOLVE THE STATE OR CONCERN THE RIGHTS OR OBLIGATIONS AMONG OWNERS OF INTERESTS IN, OR RIGHTS TO PRODUCTION FROM, ONE OR MORE LEASES OR PROPERTIES OR A UNIT];"

Page 32, lines 23 - 24:

Delete

"(12) for a transaction that is an internal transfer or is otherwise not an arm's length transaction, expenditures incurred that are in excess of fair market value;"

Insert

"(12) an expenditure otherwise deductible under (b) of this section that is a result of [FOR A TRANSACTION THAT IS] an internal transfer, a transaction with an affiliate, or a transaction between related parties, or is otherwise not an arm's length transaction, unless the producer establishes to the satisfaction of the department that the amount of the expenditure does not exceed the [EXPENDITURES INCURRED THAT ARE IN EXCESS OF] fair market value of the expenditure;"

Page 35, line 12, following "processed":

Insert ";

(21) costs relating to office buildings, fixtures and equipment, and real property that are not located in the state;

(22) overhead, office, or administrative expenses, and all other indirect costs of oil or gas exploration, development, or production"

CHAIR FRENCH objected for discussion purposes.

SENATOR WIELECHOWSKI thanked Mr. Bullock for his help in clarifying the intent, which is to tighten the lease expenditure

provision. This gives the taxpayers clear guidance about what can be deducted and it gives the administration flexibility to create regulations regarding direct costs.

CHAIR FRENCH asked Mr. Bullock if he had anything to add.

[4:20:31 PM](#)

MR. BULLOCK explained that the amendment has two parts. Sec. 43, page 1, line 3 of the amendment addresses AS 43.55.165(b). The significant change from what was proposed earlier starts on page 2, he said. Essentially it deletes language in paragraphs (8) and (12) of AS 43.55.165(e) and adds paragraphs (21) and (22).

SENATOR WIELECHOWSKI highlighted page 2, line 7. Version "K" says the department "shall" consider certain factors and this says the department "may" consider the factors, which is less constrictive.

CHAIR FRENCH asked Commissioner Galvin to give his perspective. COMMISSIONER GALVIN said Amendment 16 reflects the direction the administration is trying to go in terms of clarifying what are and are not allowable deductions. The ACES intent is to provide clear rules and Amendment 16 moves in that direction. "We will be looking more closely at the language as it moves into the next committee to ensure that it matches what we would need to be able to implement," he added.

CHAIR FRENCH removed his objection. Finding no further objection, he announced that Amendment 16 is adopted.

[4:22:42 PM](#)

SENATOR THERRIAULT stated that he asked Senator McGuire to move the language in Amendment 8, which relates to in-state use of gas. He said he would like to be shown as a sponsor of Amendment 8 along with Senator McGuire.

CHAIR FRENCH said he has no objection to him being named as a co-sponsor with Senator McGuire on Amendment 8.

CHAIR FRENCH asked Commissioner Galvin if the fiscal note with the component number 2476 was keyed off the bill as it was drafted last night.

COMMISSIONER GALVIN said we anticipated the retroactivity provision so that is reflected.

At ease from [4:24:22 PM](#) to [4:28:22 PM](#).

CHAIR FRENCH said he wanted to make sure that the draft fiscal note reflects the most current thinking of the Department of Revenue with respect to the fiscal impacts of the bill.

COMMISSIONER GALVIN stated:

The draft fiscal note...does reflect the bill as it currently stands with the retroactive effective date of the fiscal terms. The main thing to point out is the change is going to show up on the last page that shows the projected revenues and in particular to key it off the current forecasted price for FY 2008 of \$71 would result in an increase in FY 08 revenue of about \$800 million. Because it's going back into fiscal year 2007, there's a note at the top that...says there's a \$400 million addition to the FY 07 timeframe that is also attributable to the retroactive. And so that's where the...\$1.2 billion comes from—a combination of those two.

[4:29:39 PM](#)

SENATOR WIELECHOWSKI referred to page 1 and read, "the progressivity surcharge is raised to an index of .4%" and asked if that's the ceiling on the progressive rate.

COMMISSIONER GALVIN said that's correct.

SENATOR WIELECHOWSKI asked if Personal Services on page 2 will reflect the changes the committee made today.

COMMISSIONER GALVIN said they will clarify that those are four new positions.

[4:30:13 PM](#)

SENATOR WIELECHOWSKI motioned to pass CSSB 2001, version "K" as amended, from the judiciary committee with attached fiscal notes [and individual recommendations].

CHAIR FRENCH announced that without objection CSSB 2001(JUD) moves to the next committee.

The committee adjourned at [4:30:39 PM](#).