ALASKA STATE LEGISLATURE
HOUSE RESOURCES STANDING COMMITTEE
February 10, 2010
1:05 p.m.

MEMBERS PRESENT

Representative Craig Johnson, Co-Chair
Representative Mark Neuman, Co-Chair
Representative Kurt Olson
Representative Paul Seaton
Representative Peggy Wilson
Representative David Guttenberg
Representative Scott Kawasaki
Representative Chris Tuck

MEMBERS ABSENT

Representative Bryce Edgmon

OTHER LEGISLATORS PRESENT

Representative Mike Chenault

COMMITTEE CALENDAR

HOUSE BILL NO. 217
"An Act relating to the tax applicable to the production of natural gas used in the state as fuel or feedstock in producing a manufactured end product."

- HEARD AND HELD

HOUSE BILL NO. 308
"An Act relating to the tax rate applicable to the production of oil and gas; relating to credits against the oil and gas production tax; and relating to the period in which oil and gas production taxes may be assessed."

- HEARD AND HELD

PREVIOUS COMMITTEE ACTION

BILL: HB 217
SHORT TITLE: TAX ON GAS FOR IN STATE MANUFACTURING
SPONSOR(s): REPRESENTATIVE(s) NEUMAN

04/06/09	(H)	READ THE FIRST TIME - REFERRALS
04/06/09	(H)	RES, FIN
04/13/09	(H)	RES AT 1:00 PM BARNES 124
04/13/09	(H)	Heard & Held
04/13/09	(H)	MINUTE(RES)
01/29/10	(H)	RES AT 1:00 PM BARNES 124
01/29/10	(H)	Heard & Held
01/29/10	(H)	MINUTE(RES)

BILL: HB 308
SHORT TITLE: OIL AND GAS PRODUCTION TAX
SPONSOR(s): REPRESENTATIVE(s) JOHNSON

01/19/10	(H)	READ THE FIRST TIME - REFERRALS
01/19/10	(H)	RES, FIN
02/08/10	(H)	RES AT 1:00 PM BARNES 124
02/08/10	(H)	Heard & Held
02/08/10	(H)	MINUTE(RES)
02/10/10	(H)	RES AT 1:00 PM BARNES 124

WITNESS REGISTER

DONALD BULLOCK JR., Legislative Counsel
Legislative Legal and Research Services
Legislative Affairs Agency
Alaska State Legislature
Juneau, Alaska
POSITION STATEMENT: During the hearing on HB 217, provided information and answered questions.

GARY ROGERS, Oil & Gas Revenue Specialist
Tax Division-Administration
Department of Revenue (DOR)
Anchorage, Alaska
POSITION STATEMENT: During the hearing on HB 217, answered questions.

PAT GALVIN, Commissioner
Department of Revenue (DOR)
Anchorage, Alaska
POSITION STATEMENT: During the hearing on HB 308, provided information, answered questions, and assisted with Ms. Davis's PowerPoint presentation.

MARCIA DAVIS, Deputy Commissioner
Office of the Commissioner

Department of Revenue
Anchorage, Alaska
POSITION STATEMENT: During the hearing on HB 308, answered questions and provided a PowerPoint presentation.

JOHN LARSEN, Audit Master
Tax Division-Production Audit Group
Department of Revenue
Anchorage, Alaska
POSITION STATEMENT: During the hearing on HB 308, answered questions and assisted with Ms. Davis's PowerPoint presentation.

GARY ROGERS, Oil & Gas Revenue Specialist
Tax Division-Administration
Department of Revenue (DOR)
Anchorage, Alaska
POSITION STATEMENT: During the hearing on HB 308, answered questions.

JONATHAN IVERSEN, Director
Tax Division-Administration
Department of Revenue
Anchorage, Alaska
POSITION STATEMENT: During the hearing on HB 308, answered questions.

ACTION NARRATIVE

1:05:54 PM

CO-CHAIR CRAIG JOHNSON called the House Resources Standing Committee meeting to order at 1:05 p.m. Present at the call to order were Representatives P. Wilson, Kawasaki, Tuck, Neuman, and Johnson. Representatives Guttenberg, Olson, and Seaton arrived as the meeting was in progress. Also present was Representative Chenault.

HB 217-TAX ON GAS FOR IN STATE MANUFACTURING

1:06:04 PM

CO-CHAIR JOHNSON announced that the first order of business is HOUSE BILL NO. 217, "An Act relating to the tax applicable to the production of natural gas used in the state as fuel or feedstock in producing a manufactured end product."

1:06:58 PM

REPRESENTATIVE P. WILSON moved to adopt the proposed committee substitute (CS) for HB 217, Version 26-LS0816\R, Bullock, 2/8/10 ("Version R") as the work draft.

REPRESENTATIVE KAWASAKI objected and asked what the differences are between Version R and the bill as introduced.

REPRESENTATIVE NEUMAN, sponsor of HB 217, replied that the differences are related to questions previously raised by committee members about identifying the tax credits. Department of Revenue staff worked with the bill drafter to address these questions. Because of some credits that are available under the Alaska's Clear and Equitable Share (ACES) law, an either/or clause was added to ensure that the 5 percent credit would act to the best benefit. Thus, one sentence became eight pages long because it must be applied to preceding statutes.

REPRESENTATIVE KAWASAKI removed his objection. There being no further objection, Version R was before the committee.

1:08:41 PM

REPRESENTATIVE NEUMAN said HB 217 would reduce the production tax for gas that is manufactured within the state of Alaska in an attempt to induce manufacturing in the state to create jobs. It would not affect Cook Inlet gas. He pointed out that manufacturing is a molecular change in the gas or the methane. An example of manufacturing is the Fischer-Tropsch process, which is a catalyzed chemical reaction for making alternative fuels. However, converting gas to liquefied natural gas (LNG) for export is not manufacturing because it is simply a cooling and compressing process. He reiterated that the purpose of HB 217 is to create jobs.

1:10:52 PM

REPRESENTATIVE SEATON requested further explanation of the differences between Version R and the original bill.

REPRESENTATIVE NEUMAN deferred to Donald Bullock, the bill drafter.

1:11:47 PM

DONALD BULLOCK JR., Legislative Counsel, Legislative Legal and Research Services, Legislative Affairs Agency, Alaska State Legislature, pointed out that Section 9 of Version R, beginning on page 9, line 31, is HB 217 prior to this CS, which was a change in the definition of "used in the state". That "used in the state" definition was relevant to what is currently AS 43.55.011(o), which sets a maximum tax rate on gas that is produced and used in the state. In response to [previous committee] discussion, the sponsor asked for a CS that would allow producers to choose whether to apply the cap to gas that is used in the state or to have it taxed at the regular rate that is applicable to other gas no matter where it is used. He said the reason for this is because, as he understands it, AS 43.55.011(m) requires that gas subject to the cap have the credits applied before the cap is applied; thus, the credits that were applied to gas used in the state could not be available against other production.

MR. BULLOCK explained that Section 4 of Version R therefore adds a new section to AS 43.55 which would provide for an election that a producer could make to either have the gas that is used in the state taxed as any other gas or have the cap applied. If the producer makes the election provided by Section 4, then it is just like AS 43.55.011(o) - the cap on gas used in the state is the same as the cap on gas that is produced in Cook Inlet. Because this is a new section that provides for the cap, most of the bill just corrects cross references to the section and replaces reference to the cap in AS 43.55.011(o) to the new section which is 43.55.014. So, the change in the CS is rather than having the cap applicable to all gas used in the state, producers have the option to go for the cap that is currently in AS 43.55.011(o) through the enactment of this new section or just have gas used in the state taxed as any other gas that is taxed without regard as to where it is used.

1:14:48 PM

REPRESENTATIVE SEATON inquired at what point a company could make this selection. He posed a scenario in which a company that is having a major development takes the tax credits and the tax write-offs against all of its upstream expenses at the high rate and offset that against its oil. Then, once gas starts flowing, the company makes this election and its gas tax is now at a very low rate. In that situation, the state would be spending 60-70 percent of the development cost through tax credits and deferrals and then when production starts the tax

would be at 5 percent and the state would never recover its offsets even if there is great gas production.

CO-CHAIR NEUMAN responded he believes a lot of that is already done and HB 217 is just adding manufacturing to the end of that. He deferred to Mr. Rogers of the Department of Revenue for further explanation.

1:17:25 PM

GARY ROGERS, Oil & Gas Revenue Specialist, Tax Division-Administration, Department of Revenue (DOR), replied that much of the answer to Representative Seaton's question would depend upon each individual producer's circumstances and he therefore does not have an answer at the moment.

REPRESENTATIVE NEUMAN said he believes if that election is made, then all the rules applicable to AS 43.55.011(o) apply to the cap on gas used in state. If the election is not made, the gas is taxed at the other tax rate.

MR. BULLOCK added that HB 217 allows a taxpayer to opt to use what is currently AS 43.55.011(o) or to not have the gas subject to the limitations, and that limitation comes with requirements of how the credits are applied.

1:19:58 PM

CO-CHAIR JOHNSON surmised that Representative Seaton's question is whether a producer has the ability to move back and forth between the tax rates depending on flow - is it an either/or, or is it an and. For example, once an election is made, can the taxpayer go back and pick a better rate based upon its tax credit, or is the taxpayer bound to its original election once gas is flowing.

REPRESENTATIVE SEATON agreed that that sums up his question. He cited Point Thomson as being an example because it is a large gas development and right now the State of Alaska is making a major contribution through the 20 percent tax credit. There is also the upstream tax on oil of 25 percent plus progressivity, so at $70 per barrel the state may be putting in 70 percent of the total investment into that field. After gas starts flowing, his question is whether the 5 percent tax rate could then be elected for gas that is used in in-state manufacturing. He said he does not believe that in such a scenario the state would ever recover its investment. So, yes, the question is timing and

whether a taxpayer could utilize one rate and then at a later date make the other election.

1:22:00 PM

MR. BULLOCK pointed out a disconnect between Sections 4 and 5 in the CS. Under AS 43.55.014(c) in Section 4, the election is made annually at the time the return for the production tax is filed. However, [Section 5] talks about making the estimated payments during the year that would be based on what the projected tax would be if the taxpayer made the election. So, 43.55.014(c) could be amended to say that the taxpayer makes its election at the time the first estimated payment is due for the tax for the year, rather than waiting until the end of the year to claim it.

REPRESENTATIVE SEATON said his problem with this is that most of the investment in the exploration and development of the field takes place before gas ever flows. So, if this is an annual election, it would let an oil company write off at maybe 70 percent; thus, the state would be investing in the field at 70 percent of the total expenses. Then, annually, when the gas starts to flow, the company could elect the 5 percent tax rate. This is something that must be guarded against. Though that may be a provision in the fuel and electrical generation portion, and this is adding manufacturing, the manufacturing could utilize significant amounts of gas, much more than fuel usage for residences. If the state does not have an export market, then all of the gas would be this way and the state would be the major investor and would receive very little in taxes.

1:23:59 PM

CO-CHAIR JOHNSON asked whether that problem would remain if the manufacturing aspect of this is taken out.

MR. BULLOCK answered that the manufacturing expands the definition of gas "used in the state" to manufacturing, which it does not do now. This expands the market for the gas that could be used in the state. That, in turn, expands the amount of gas that would be subject to an election to have the cap applied. However, he pointed out that the credits under the production tax in AS 43.55.023-025 would not be affected by HB 217, and they would still be generated as they always are. So, the effect of the bill is that it expands the volume of gas that could be used in the state by providing more purposes that are

allowed to be subject to what is now a cap and, under the bill, would be subject to the election.

1:25:07 PM

REPRESENTATIVE SEATON said his point is that the purpose of this bill is to expand the amount of gas that would be selling at a very low tax rate and if the state is giving all of the credits that are available through other provisions and allowing upstream deductions of the 25 percent plus progressivity, then the state will have a lot of money invested and get very little back. While the state would receive revenue from manufacturing, manufacturing will not pay the bills.

CO-CHAIR JOHNSON commented that this is a policy call of whether to trade taxes for jobs.

1:26:29 PM

REPRESENTATIVE P. WILSON, in regard to page 3, line 26, "make the election at the time the return is due", requested Mr. Bullock to comment on his previous suggestion to make the election earlier than that.

MR. BULLOCK explained that ACES changed what was a monthly tax to an annual tax, while at the same time providing for monthly installments. So, AS 43.55.020, which is amended by Section 5 of Version R, provides for the calculation of an installment payment that is roughly equal to one-twelfth of the tax liability that will be due for the year. There was already a provision in AS 43.55.020(a) that applied to gas used in the state and how to determine how that cap affects the installment payment. So, his suggestion was that since the taxpayer makes installment payments during the year as the gas is produced, the taxpayer could make the election at the time an installment payment is made rather than after the end of the year. He pointed out that the producer has to know whether the gas is used in the state or not, but in the case of manufacturing there are not yet any manufacturing facilities in the state. The credits that are accruing are going to be applying to other production until this "used in the state" kicks in, which applies to the question that Representative Seaton had.

1:28:40 PM

CO-CHAIR NEUMAN added that HB 217 provides the opportunity for Alaska's gas to be used in different ways for manufacturing.

Right now Alaska's gas is used for home heating and electrical generation. The goal is to also use it for manufacturing and create thousands of jobs in the state. An issue was identified by the Department of Revenue (DOR) and an effort has been made to fix that. The fiscal note is zero. Right now no gas is being produced for manufacturing in-state and 5 percent of nothing is zero to the state. Therefore, to him, this incentive is good. His goal is to have a pipeline to Southcentral Alaska to some manufacturing and everything possible must be done to try to establish that. He agreed that revenue to the state is important, but pointed out that by creating more manufacturing, those manufacturers would be paying corporate taxes. Alaska needs to find ways to diversify its economy, he opined.

CO-CHAIR JOHNSON interjected that manufacturing could take place anywhere in the state.

CO-CHAIR NEUMAN agreed and reiterated that manufacturing means a molecular change and would not include LNG export.

1:31:35 PM

REPRESENTATIVE SEATON agreed that the state has been counting on gas as the replacement when oil goes down. However, should HB 217 pass, and the "large" pipeline stays inside the state, and all of the gas is used in-state, then the state would get no revenue off of that gas. He said he is using the term "no revenue" because the tax credits and the upstream amounts would probably fully offset any amount of tax the state receives. When he looks at jobs he is also looking at saying there will not be forward funding of education and there will not be a number of other things because the state's tax base has gone down as a result of the decline in oil and almost no tax on the gas used for manufacturing. The state would then need to substitute another tax regime, such as an income tax, tax on mining, or tax on manufacturing.

CO-CHAIR JOHNSON commented that if those other funding sources were out there, such as the manufacturing, that would be a pleasant decision to make. It is a policy call, he reiterated.

1:33:49 PM

REPRESENTATIVE SEATON said his problem with HB 217 is whether the incentive is being given to the right people - it is a production tax; it does not go to the manufacturer. If the state wants to have use of gas for manufacturing, a credit would

be given to manufacturers that use gas as a feedstock. Then it would be the manufacturer that is being encouraged instead of giving a low tax rate to the producers and hoping that they pass their lower costs on to the manufacturer using that gas.

CO-CHAIR JOHNSON offered his understanding of that concern.

MR. BULLOCK pointed out that AS 43.55.014 would sunset in 2022, so there would be an end period for the election to apply. As it went forward it could be seen how it works and the statute could be adjusted by the legislature.

CO-CHAIR NEUMAN allowed that this is his concern too, but there is also revenue from corporate taxes, royalties, local property taxes, and the purchase of permits and leases from the state. He noted that HB 217 says "used as ... feedstock" for the manufacturing process and this is what the bill started with.

1:35:50 PM

REPRESENTATIVE GUTTENBERG commented that at times the state's tax breaks and incentives do not produce what is expected. For example, in the Interior the requirement that logs could be exported until they were milled resulted in the logs being run through the mill to cut off two sides to create slab wood and then the rest of the log was exported to Japan. He offered his concern that a minor part of the gas molecules could be taken off and the rest exported, rather than using most of the gas for in-state feedstock for lots of different products. He inquired whether such an unintended consequence has been looked at.

CO-CHAIR NEUMAN responded that he hopes lots of products will be made from the gas. He noted that the Fischer-Tropsch process creates synthetic transportation fuels and a by-product of that process is feedstock for plastics. The goal is to have ethanes for raw plastics, as well as butanes and synthetic propanes. He urged members to talk to him and Mr. Bullock to get their questions answered.

CO-CHAIR JOHNSON urged members to speak individually with the sponsor so their questions can then be put on the record in a clear and concise manner at the next hearing of HB 217 and action can be taken on the bill.

1:41:04 PM

MR. BULLOCK pointed out that the reason HB 217 has gone from one paragraph to ten pages is because of all of the cross references that have to be changed. He advised that when reading the bill, anything related to such cross references will be seen as (o) in brackets, because this is the subsection of AS 43.55.011 that is being deleted, and before that bracketing will be insertion of the new election section which is bolded and underlined.

1:42:06 PM

REPRESENTATIVE P. WILSON asked why the sponsor chose to provide the benefit to the producer rather than the manufacturer.

CO-CHAIR NEUMAN replied that the cost of feedstock will be a primary consideration for potential manufacturers because that will eventually be the cost of the finished product. This would get that cost of the feedstock to a rate that is acceptable. He related that the cross references are the result of the Department of Revenue's determination that maybe - in a few circumstances - there could be a disincentive to the cost of gas for electrical generation and home heating use. If that happened, it could cause Alaskans to have to pay more for home heating and electrical generation. Therefore, he agreed to this suggestion in an attempt to reduce the cost for those customers, which was the intent of expanding the Cook Inlet rate of 17.5 cents to the rest of the state.

CO-CHAIR JOHNSON held over HB 217.

HB 308-OIL AND GAS PRODUCTION TAX

[Contains discussion of HB 337]

1:45:14 PM

CO-CHAIR JOHNSON announced that the next order of business is HOUSE BILL NO. 308, "An Act relating to the tax rate applicable to the production of oil and gas; relating to credits against the oil and gas production tax; and relating to the period in which oil and gas production taxes may be assessed." [Before the committee was the proposed committee substitute for HB 308, labeled 26-LS1328\E, Bullock, 2/5/10 ("Version E").]

1:46:42 PM

REPRESENTATIVE GUTTENBERG inquired whether another committee substitute (CS) will be coming before the committee.

CO-CHAIR JOHNSON responded that he is not married to Version E and it probably needs some minor technical changes that are cleanup, but not anything major.

REPRESENTATIVE GUTTENBERG requested that members be given some leeway with amendments that they may have for the sections that are to be changed.

CO-CHAIR JOHNSON agreed.

CO-CHAIR NEUMAN encouraged members to talk to the sponsor and the Department of Revenue about the bill.

CO-CHAIR JOHNSON added that he wants everything on the record, but that Co-Chair Neuman's suggestion would provide for a smooth process in committee.

1:48:32 PM

PAT GALVIN, Commissioner, Department of Revenue (DOR), noted that Governor Parnell's oil tax amendment bill [HB 337/SB 271] was read across both floors today. Therefore, while presenting the department's perspective on HB 308, Version E, he and Deputy Commissioner Davis will also tie in the governor's bill with the committee's proposed CS.

CO-CHAIR JOHNSON urged that it be the similarities between the bills that are discussed and not the differences, because the committee has yet to notice the governor's bill.

COMMISSIONER GALVIN agreed.

1:50:13 PM

COMMISSIONER GALVIN commended the sponsor for his intent to find ways to increase jobs for Alaskans and production in Alaska. He said the governor and the administration share this goal and want to work with the sponsor in finding the most effective and efficient way to reach that goal. Today's presentation will look at how Version E would function from the Department of Revenue's perspective, how the provisions would be implemented by the department, and the issues that need to be addressed in order to properly implement those provisions. He and Ms. Davis will also talk about some of the trade-offs associated with different ways of trying to accomplish the goal of increasing production and increasing jobs.

COMMISSIONER GALVIN noted that both HB 308 and the governor's bill would provide increased credits and an increased definition for new drilling activities within existing fields, and the department views this as very valuable and favorable. He said the department supports the purpose of [Section 15 in Version E] to maximize Alaska hire in the oil patch, which would be done by providing a tax rebate. The state has always struggled with finding ways to do this within the constraints of the U.S. Constitution and elsewhere; therefore, he will talk about this issue in terms of the mechanism that is provided and not the legal side.

1:52:43 PM

COMMISSIONER GALVIN recognized that Version E's proposed progressivity change is intended to bring the progressivity rate to a level similar to that in the original Alaska's Clear and Equitable Share (ACES) measure. He noted, however, that there are two differences. The more significant of the two differences is the package of the tax that is provided by Version E. Reducing the progressivity does not put in place what was seen as the tradeoff for that reduced progressivity, which was a gross-based floor on the two major fields to ensure the state had revenue at low price; this was the tradeoff for the lower take at high prices. When that low price security - the guaranteed revenue to the state - was removed, the progressivity was supported to go up to provide a risk balance that the administration felt was appropriate given the amount of state credits and participation at the front end of all the new investment. That was a package when that part of the bill was included in the original proposal. The second difference is technical. In the original ACES proposal there was not a 0.1 percent escalation beyond the 50 percent total rate. He said the department's presentation will provide from an empirical standpoint what that change means in terms of potential revenue.

1:54:38 PM

CO-CHAIR NEUMAN maintained that there is a tradeoff between creating jobs and generating revenue, and that those benefits outweigh the revenue to the state because of other revenues generated beyond that.

COMMISSIONER GALVIN responded that the intent is to create jobs through the investment in oil and gas exploration and development. The issue for the tax system is to find not just a

balance, but also a structure that maximizes benefit to the state in terms of revenue and ensures a structure that incentivizes investment in new exploration and development. That is where the question of changing the progressivity comes in. Changing the progressivity will result in less money coming to the state and more money staying with the taxpayer, but does it result in new investment? There will be a lot of debate on that. From the administration's perspective at this time, given the information the department has received from companies in the industry, there is no commitment to take any tax savings that would result from a lower tax rate and turn it into jobs and investment. However, a structure that emphasizes the credits will ensure that the state benefits because the reduction in the tax only goes to those who actually are investing and creating jobs in the state.

1:57:13 PM

COMMISSIONER GALVIN agreed that the policy issue of choosing between increasing revenue to the state or increasing jobs in the state is a valid question. The analysis comes down to the relative tradeoff - will the state forego a significant amount of revenue to create a handful of jobs, or is the state going to forego a smaller amount of revenue to create a lot more jobs. That is the crux and is something members will have to get from the analytical information the department will provide and perhaps from testimony from people that will actually make those decisions. He explained that from a purely analytical standpoint, a direct relationship can be seen between providing credits for actual work resulting in actual jobs and being able to quantify what that cost the state. This gives the state the ability to provide a rational explanation for why it is doing that. It is difficult to provide the same linkage between a drop in a tax that just goes back to a company and the company gets to decide what to do with that investment because the linkage is not in actual numbers. In such a case, the state is merely hoping the company will bring it back into the state.

1:58:59 PM

COMMISSIONER GALVIN pointed out that there are two parts to the interest rate provision in HB 308, Version E. One part is a waiver of the interest that would be due on underpayments of taxes that are due to regulations that are retroactive. Because of the complexity of the changes made in the law by ACES, a series of regulations have had to be developed in order to refine for the taxpayer the implementation method and the

interpretation method. By statute those regulations are being made retroactive to when ACES became effective and, in some cases, actually retroactive all the way back to when the production profits tax (PPT) became effective. Thus, they may result in underpayments because in good faith the taxpayer made payments that it thought would be correct. The Department of Revenue shares the sponsor's view that it is fair to waive that interest to address that particular issue.

2:00:38 PM

REPRESENTATIVE OLSON asked whether the department is expecting any lawsuits in regard to going back that far.

COMMISSIONER GALVIN replied that the department is unaware of any pending lawsuits. In further response, he said most of the regulations are now out and he believes the department has significantly mitigated the risk of such a lawsuit through the method used to develop the regulations. He explained that in the typical regulation development process, a draft is sent out, comments are taken, decisions are made behind closed doors, and then a final regulation is sent out. In this case, the department has had a much more interactive process that has engaged the industry so that industry has seen the development over the course of the past couple of years and has been involved in the department's analysis of how it will work and what the implications will be. Therefore, he sees less risk of industry feeling it was unfair or a surprise or an inappropriate lag time because industry participated in creating that lag time. He said he is not expecting the department to be putting out any modified records of decision (MROD).

2:02:24 PM

CO-CHAIR JOHNSON understood that current law allows the department to forgive the penalty on the tax debt, but not the interest.

COMMISSIONER GALVIN answered correct. The department has the authority and the discretion to waive the penalty for underpayment, but not the discretion to waive the application of interest for underpayment.

COMMISSIONER GALVIN stated that the department's presentation will also address the restoration of the 3-year statute of limitations that is proposed by HB 308, Version E.

2:04:01 PM

REPRESENTATIVE SEATON inquired whether application of lease expenditure regulations is somewhat mitigated due to the sunset of the standard deduction.

COMMISSIONER GALVIN responded that in general, yes. The definition of lease expenditures applies to both operating and capital expenditures, the two components of lease expenditures. The so-called standard deduction, which expired December 31, 2009, basically froze the allowable lease expenditures on the operating side for Prudhoe Bay and Kuparuk. Since those are larger fields and a larger taxpayer, that would be a substantial portion of any potential change that might come about because of the operation of the lease expenditures. The supposition that it reduced the potential effect of the retroactive application of the regulations is thus correct. Over the last couple years, lease expenditures have been fairly evenly split between operating and capital expenses. Therefore, from a taxpayer standpoint, a substantial portion of half of what the lease expenditure is defined will be unaffected by the change in definition.

2:06:37 PM

REPRESENTATIVE SEATON, in regard to the retroactive application, surmised that what is really being looked at are problems with underpayment or those things that would relate to capital expenditures because operating expenses were fixed until December 2009.

CO-CHAIR JOHNSON interjected that he thinks the number was also based on 2006.

COMMISSIONER GALVIN, in response to Co-Chair Johnson, replied right. It was the 2006 grossed up to be annualized because it started in April, and then moved forward with the escalation factor. In response to Representative Seaton, he said there are some operating expenditures associated with other fields that would be affected by the lease expenditure definition, but it is correct that for the most part it is going to be the capital expenditure portion that is affected.

2:07:57 PM

REPRESENTATIVE GUTTENBERG, in regard to the standard deduction, asked whether additional perspective on the industry was learned

that allowed the Department of Revenue to understand tax structure and how it affected those companies.

MARCIA DAVIS, Deputy Commissioner, Office of the Commissioner, Department of Revenue, answered that after passage of ACES the department immediately undertook an audit of the 2006 operating expenditures for both Prudhoe Bay and Kuparuk. This audit established the baseline from which an indexed value could be applied for what would be allowable lease expenditures - from an operating expense point of view for those two fields - for the rest of 2006 and all of 2007, 2008, and 2009. So, yes, the department was able to better understand and learn how operating expenses were charged across the field, how they were grouped, and where the data was. The department engaged with the two operators and obtained the charge systems for both sides. In turn, the operators received immediate feedback from the department as to what was in and what was out of the bucket for lease expenditures and that served as guidance for them even though a formal regulation was not yet in place.

2:10:02 PM

REPRESENTATIVE GUTTENBERG, in regard to taxpayers understanding what constituted an allowable expense under the standard deduction, inquired whether industry had an issue when operating costs went above the standard deduction.

MS. DAVIS stated that the 2006 level was the level that the department accepted as the beginning of the indexed year. She advised that she can speak with reference to Prudhoe Bay and Kuparuk because they each contain more than three taxpayers. In each of those instances, each taxpayer reports its own view of its operating expenses on a year-to-year basis, and these reports do not necessarily match one another because each taxpayer has its own accounting and allocation systems. Looking at them as a group, the reported operating expenditures exceed by a small amount the standard deduction on the Kuparuk side and on the Prudhoe Bay side it was a little larger than for Kuparuk. In both instances the actual expenditures exceeded the limitation imposed by the standard deduction for operating expenses for the following years.

2:11:52 PM

CO-CHAIR JOHNSON asked whether the amount above the standard deduction is in the tens or hundreds of millions of dollars.

MS. DAVIS answered that it depends upon the year. Some years it might be less than $100 million and some years more. She said she does not have the actual numbers before her and it covers about three years.

CO-CHAIR JOHNSON inquired whether the actual numbers would be confidential.

MS. DAVIS responded that she would have to be reporting an averaged number. In further response, she agreed that generally the number is in the hundreds of millions of dollars.

2:12:45 PM

COMMISSIONER GALVIN clarified that while the amount of additional lease expenditure that the taxpayers experience is greater than the standard deduction in the three years, the impact on their tax liability was different in each year. In 2008, for example, their price was significantly higher and progressivity was higher. Therefore, the impact of the standard deduction was significantly greater on their tax liability in 2008 than it was in 2009, even though the difference in the actual spending level was fairly similar.

CO-CHAIR JOHNSON presumed that this was a function of progressivity and price.

COMMISSIONER GALVIN replied yes. In further response, he agreed that the amount of money being talked about is in the hundreds of millions of dollars.

2:13:37 PM

REPRESENTATIVE GUTTENBERG surmised that the other side of that equation is that the taxpayers' profits had escalated quite a bit, so the taxpayers were making more money while paying more taxes.

COMMISSIONER GALVIN answered right.

2:13:59 PM

MS. DAVIS began her PowerPoint presentation providing the administration's comments on HB 308, Version E. She noted that the Department of Revenue has reviewed the bill in terms of how it would implement the provisions. In regard to the proposed resident worker tax rebate [in Section 15], she said that

Version E is unclear as to whether the rebate would affect only the taxpayer's/producer's own discreet workforce, or would also include the workforce of the contractors that a producer engages for the various North Slope operations [slide 3]. This is a significant distinction for the department when reviewing the numbers, she pointed out, because the vast majority of the workforce is employed at the contractor level, not the producer level. She asked for clarification in this regard.

2:15:57 PM

CO-CHAIR JOHNSON responded that the intention is for the rebate to apply to both the producer and the contractor. He said he will work with the Department of Revenue (DOR) and the Department of Labor & Workforce Development (DLWD) to come up with a CS that clarifies this.

REPRESENTATIVE GUTTENBERG said this was his concern also. He directed attention to page 29 of Mr. Dan Dickinson's 2/8/2010 PowerPoint presentation [which lists the top employers in the oil and gas industry] and pointed out that the slide states the list does not include catering/security, engineering, transportation, communications, and construction.

CO-CHAIR JOHNSON reiterated that there will be a CS.

2:16:44 PM

MS. DAVIS continued her presentation, noting that Section 2 of Version E requires the individual charged with maintaining the labor workforce data to keep that data for 3 years. Regardless of whether this bill is passed and the tax assessment period is changed from six to three years, the Department of Revenue will look for a continuity of records being retained for as long as the tax question remains open. Therefore, it would be helpful to the department to have this language modified to state, "three years, or the close of the relevant tax year." Further, if the bill is clarified to include contractors, it would help the department if in Section 15 [page 6, lines 7-11] it is clarified that the word "incurs" includes direct labor costs as well as labor costs incurred through a contractor.

2:17:55 PM

MS. DAVIS observed that the rebate use and payment mechanism for the local hire provision is unclear in terms of how the department would implement it [slide 3]. Version E couches the

incentive in the form of a rebate and has the rebate arise after the filing of the annual report that is due on March 31. What actually happens in the state's tax world is that a taxpayer looks through the year and files monthly payments that are based on estimates of what the taxpayer thinks its tax bill is going to be. Each month the taxpayer will true up its payment as it learns more and more what it thinks will be its tax bill.

MS. DAVIS said the department is therefore looking for some clarity from this committee as to whether a taxpayer is authorized to anticipate that it will ultimately receive a rebate and can factor that into the monthly payments. Or, is the intent that the taxpayer pay its tax bill without consideration of the rebate such that at the end of the tax year the Department of Labor & Workforce Development obtains the records and verifies for the Department of Revenue whether the appropriate hiring rate has been met to qualify for rebate? In that case it would truly act as a rebate and would be similar to how the department does credits. For example, a taxpayer applies for credits, the department gives it a value, and by then the department knows what the tax bill is and can apply the credit or rebate, which would be similar to a certificate. If that is the mechanism, there needs to be clarification as to where the money will come from to pay the rebate; for example, whether it would come out of the credit fund that is set aside and renewed through general funds.

2:19:55 PM

MS. DAVIS referred to the definition of "resident worker" which is provided by Section 15 [page 8, line 12] as being the meaning given in another section of the tax code [AS 43.40.092]. Under [AS 43.40.092] a resident worker may be required to swear under oath that he or she is in fact domiciled in the state. She said it would be helpful to know whether authority is being given to the Department of Revenue or the Department of Labor & Workforce Development for administering that definition. Someone will need to create a form that would be given to the producers and their contractors should it become necessary for an employee to make that affirmation of residency.

CO-CHAIR JOHNSON related that he is working with the Department of Labor & Workforce Development in this regard. He inquired whether this is something that is wanted in the statute or would be handled through regulation.

MS. DAVIS said it could be handled through regulation as long as something is in this statute that gives one of the departments the authority to implement that section of the definition.

2:21:15 PM

REPRESENTATIVE GUTTENBERG pointed out that often a contract with a contractor is seasonal or for just a few weeks or months. He posed a scenario in which an Arkansas contractor composed of three Arkansas employees is hired for a short period of time and that contractor then hires twenty Alaskans. He asked whether it is only the percentage of time that the contractor is in Alaska actually doing the job or also count the time for paperwork that is completed after the contractor is back in Arkansas.

MS. DAVIS replied that she would defer to the Department of Labor & Workforce Development in this regard because deciding who is a resident or nonresident is DLWD's jurisdiction. She said the statutory definition seems like a solid definition as to what constitutes an Alaskan year around. Therefore, she would say that the seasonal workers in the aforementioned scenario would not qualify as Alaska residents.

REPRESENTATIVE GUTTENBERG stated that that was not what he was asking and he will ask the question of the Department of Labor & Workforce Development.

2:23:49 PM

MS. DAVIS continued her presentation and advised that Version E does not address or make it clear that the Department of Revenue has the legal authority to adjust the tax post-audit [slide 3]. Currently, the department has the right to review the information that the Department of Labor & Workforce Development acquires from its audits, but there is no authority for the Department of Revenue to adjust the tax bill when subsequent review finds that a rebate was qualified or disqualified. She explained that the department has the authority to adjust a tax bill if an audit finds that a credit was inappropriately granted, and this just needs to be expanded to ensure that the department can also adjust the tax bill if it finds that a rebate was inappropriately granted.

CO-CHAIR JOHNSON inquired how the Department of Revenue handles the film industry's 10 percent rebate for local hire.

MS. DAVIS answered that the department has not yet audited one of those, although the regulations are out. She said she believes the authority resides in the corporate income tax to adjust the tax on audit. She offered to look at the film industry language and see how it has been addressed.

2:25:29 PM

MS. DAVIS pointed out that the [portion of Section 15], which deals with the Department of Labor & Workforce Development's right to require the data be made available for verification and audit of the certificates of residency, is written such that it only covers agents or employees of such person, and a contractor might not fit that criteria. Therefore, the language needs to be corrected to ensure that the Department of Labor & Workforce Development has the right to review the contractor's data. In all likelihood, a producer will simply ask a contractor to provide a document that verifies the producer's compliance, but the underlying data will reside with the contractor.

MS. DAVIS explained that the Department of Revenue conducted a numerical analysis to understand how the resident hire rebate would work. She drew attention to slide 4 which depicts the bill's structure in terms of the rebate amount for various percentages of resident hire. The rebate amount depicted is the percent reduction of the total tax bill when these hiring criteria are met.

2:26:58 PM

CO-CHAIR JOHNSON stated the rebate applies only to the base tax rate and does not include the progressivity tax or royalties.

MS. DAVIS responded that the department did not understand this and will have to rerun the numbers.

CO-CHAIR JOHNSON offered to clarify this in the bill if it is not clear.

MS. DAVIS said she will skip [slide 5] until the department is able to rerun the numbers. She explained that the slide takes three different companies of three different sizes with roughly three different tax bills that are aspiring to receive the tax rebate by hiring more Alaskans. The analysis was an effort to discern the number of employees that it would take for each company to move to the next rebate bracket and what the cost to

the state would be per employee. [Commissioner Galvin and Ms. Davis returned to slide 5 later in the meeting at 4:05:42 p.m.]

2:28:24 PM

MS. DAVIS added that while conducting this analysis the department learned that there are two ways to approach this [slide 8]. The analysis was done with the assumption that an employer would simply keep its status quo and seek to hire Alaskans to raise its percentage of local hire. However, she cautioned, there is the possibility that an employer could fire nonresidents without hiring any new Alaskans and thereby alter its overall percent of Alaska hire.

CO-CHAIR JOHNSON replied he appreciates that, but he is going to operate under the assumption that these are for-profit companies and they are going to want to have employees to generate revenue to generate profits. Thus, he cannot think that they will fire all of their non-Alaskan employees to get to 100 percent.

MS. DAVIS pointed out that while it might not make sense for big moves, it would make sense for a company on the bubble to fire one or two people to fall into a bracket that gets the company $10 million or $20 million.

CO-CHAIR JOHNSON commented that when the company hires those people back they will be Alaskans.

REPRESENTATIVE TUCK referenced the committee's discussions [of 2/8/10] regarding the legality of disparity between residents versus nonresidents. He pointed out that this could end up being a case that nonresidents can fight to show disparity and he would hate to see something like that actually take place.

CO-CHAIR JOHNSON stated his belief that that would be recourse against the company and not the state.

2:30:34 PM

COMMISSIONER GALVIN reported that when conducting the analysis, the department discovered that Version E's proposed structure of tiers based upon a percent of resident hire will result in behavioral issues that are unique to each taxpayer and that will create inefficient behavior. Under this proposed structure of tiers, the addition of one or two employees could mean tens of millions of dollars of additional rebate. Therefore, because the methodology is hours worked, a for-profit company is

incentivized to bring in three or four people to just stand around for minimum wage and the company would then get an extra $10 million. He said he is simply bringing this outcome of the proposed tiered structure to the sponsor's attention.

CO-CHAIR JOHNSON responded that his reason for the small increments is that once a company gets from 80 percent resident hire to 85 percent, he does not want there to be such a big jump to the next hurdle that the company decides to stop hiring Alaskans. There needs to be a balance somewhere. He offered to work with the department to correct the problems, but said he does not want to take away the incentive for a company to keep hiring more Alaskans. He would like companies to strive for 95 or 100 percent and he wants to incentivize them with steps.

2:32:23 PM

COMMISSIONER GALVIN suggested that from a structural standpoint, it may make more sense to have a straight line as opposed to tiers. A mechanism could be established where for each additional Alaskan a company gets an incremental change in tax.

CO-CHAIR JOHNSON replied he thought about this, but the bill drafter said it would be very difficult to write such a bill.

2:33:19 PM

MS. DAVIS noted the department has completed its regulations defining what labor costs qualify as lease expenditures. She said Mr. John Larsen will share with members what the department understands to be the labor costs that would fall within this category of lease expenditures [slides 9-13].

JOHN LARSEN, Audit Master, Tax Division-Production Audit Group, Department of Revenue, explained that there are two classes of allowable employee expenses for the operator [slide 10]. The first class of expenses is employees that are located on the site of the oil or gas exploration, development, or production operations, including the infrastructure for those operations. The second class of expenses is employees having special and specific engineering, geological, or other technical skills. These employees do not need to be located onsite, but the costs of their labor are limited to the handling of specific problems or operating conditions involving the operations there, and only the time actually incurred working on those problems. Outside of the operator's labor would be the contractor's labor, which is 100 percent deductible.

2:35:07 PM

REPRESENTATIVE SEATON surmised that the second class of employees could be located anywhere, including other countries.

MR. LARSEN responded right. The essential criteria is that historically, prior to electronic telecommunications, it was a clear cut distinction that if an employee was on a lease or property the employee was chargeable. However, the new technologies have expanded the lease boundary. The department realizes that there are people who are employed directly in the operations but who may not necessarily be directly on the lease site itself. There is a benefit for both the operator and the state to recognize that there is a cost savings in not having technical labor onsite of the lease, such as savings in travel, housing, and safety costs.

REPRESENTATIVE SEATON presumed that this includes accountants and others if they are working on maintaining records for leases in Alaska.

MR. LARSEN replied correct.

2:37:04 PM

REPRESENTATIVE P. WILSON, in regard to contract labor being 100 percent deductible, inquired as to what is normally contracted out because a producer could contract every single thing that there is.

MR. LARSEN answered that it goes back to the assumption that these are for-profit companies. They are also working in conjunction with their joint operating partners, and the presumption is that they will not make a decision that is contrary to all of their best financial interests there.

COMMISSIONER GALVIN added the idea is that the contract labor is going to be for services that the company needs someone else to do. It is presumed that this takes the place of the company hiring someone itself and having that person do the same service. For the department, it really is either/or because hopefully the company is finding a more efficient contractor than what it would cost for the company to pay this person itself. Thus, the state benefits from the company's motivation to bring in contractors where it is more efficient to do so, and the state gives them 100 percent of that cost. He pointed out

that the state also pays 100 percent of the class one and class two employee expenses, and contract labor substitutes for one of those two.

CO-CHAIR JOHNSON surmised there is nothing at this point that says contract labor is Alaskans.

MS. DAVIS responded correct.

MR. LARSEN also replied correct.

2:39:21 PM

REPRESENTATIVE TUCK posed a scenario of an Alaskan employee who is in the state of Washington to oversee the building of a module. He asked whether the employer would receive a deduction for that employee.

MS. DAVIS answered that as long as Alaska remains that employee's state of domicile and it is a temporary location on a project basis, the department would assume that that employee would still meet the criteria for defining Alaska resident.

REPRESENTATIVE GUTTENBERG understood Ms. Davis to be saying that the construction of modules outside of Alaska would be included in the definition.

MS. DAVIS responded that the department would actually be looking at each individual laborer, and in the scenario presented by Representative Tuck the employee was the project manager who had flown down to Washington to oversee construction of that particular project.

COMMISSIONER GALVIN interpreted Representative Guttenberg's question to be whether the construction of a module is a deductible lease expenditure under the department's definition of lease expenditures.

MS. DAVIS deferred to Mr. Larsen.

MR. LARSEN said he believes construction of a module in the state of Washington would be considered a lease expenditure - as long as it is placed in service [in Alaska]. If the module is not placed in service, then he does not think it would count as a lease expenditure.

2:41:27 PM

MR. LARSEN reviewed examples of type one allowable labor [slide 11]. Any employee working onsite of the oil or gas exploration, development, or production operation will be chargeable. Such employees include: drillers, roughnecks, roustabouts, electricians, plumbers, pipefitters, welders, mechanics, and others onsite. These examples pertain to the exploration, development, or production operations themselves. Other type one allowable labor is employees working in infrastructure or support operations [slide 12]. This would include: people in the camps doing housekeeping, janitorial, and food service; operations centers and the technicians within the centers; staging pads, road bridges, landing areas, and similar transportation structures and therefore all employees operating graders and doing road maintenance; employees working on communications systems out in the field in the support area, but not employees working on communications who go back to an office outside of Alaska; medical facilities; emergency personnel; security personnel; and security, repair, and maintenance shops.

MR. LARSEN, in response to Co-Chair Johnson, clarified that a person flying up to Alaska to work onsite on a telecommunications system would be an allowable charge.

2:44:32 PM

MR. LARSEN highlighted examples of type two allowable labor, which is employees with special and specific engineering, geological, or other technical skills. He said these employees would be chargeable whether or not they are on site of the operation. Only that portion of time the employee actually devotes to the exploration, development, or production operations is chargeable. These employees include: engineers, such as reservoir and petroleum engineers; geologists; environmental specialists because they may have to do permitting or archeological work in order to be in compliance with permits; employees engaged in field automation systems, such that the field could be remotely operated from a distant location; and employees engaged in computer applications that are specific to the oil or gas exploration, development, or production operations.

2:45:40 PM

REPRESENTATIVE SEATON asked whether an accountant could determine not to include a geologist or other type one or type

two employee as a lease expenditure and instead apply those employees to the local hire tax rebate.

MR. LARSEN replied that the lease expenditure regulations are ambivalent to who the person is and where the person lives. A person's place of residency has no bearing on whether or not it is a lease expenditure and is a separate issue with the bills pending before the committee.

COMMISSIONER GALVIN added that deducting a particular employee because the employee would qualify as a lease expenditure is not mandatory. Under Representative Seaton's scenario, employees outside of Alaska would, under the definition of lease expenditures, actually qualify as a lease expenditure. If Version E were to pass in a similar form, and adding an employee to the calculation [for lease expenditures] would result in the company not hitting a particular threshold and enjoying a particular rebate, then the company could choose not to claim the employee as a lease expenditure.

2:48:16 PM

COMMISSIONER GALVIN, in response to Co-Chair Johnson, said local hire does have to do with lease expenditure because HB 308, Version E, defines it is the total labor that falls as a lease expenditure. He explained that the department is going through this exercise to show members what is in the universe of lease expenditures. If the legislation were to break that and instead say it is all labor costs under some other definition of connected to Alaska, a whole different problem would be created because a different definition of what is connected to Alaska would have to made in order to define that whole - the whole being the denominator of the percentage calculation. The department recognizes the need for defining the whole of the labor costs around lease expenditures that works, but the department wanted to make sure the committee understands where the edges are for that. Regardless of how it is defined, some aspect of voluntary reporting will always be faced, and the Department of Revenue will work with the Department of Labor & Workforce Development to confirm whether all the parts that have been included are proper. Realistically, if something is not reported, DOR will never know. So, in regard to Representative Seaton's question, that is a possibility, but it goes to the question of what is the behavioral reaction to this and making sure that that is tightened down.

2:50:35 PM

REPRESENTATIVE SEATON drew attention to page 6, [lines 7-11], Version E, regarding the labor costs that are allowable lease expenditures, and the entitlement to a rebate if 80 percent or more of that labor is done by resident workers. The state's normal consideration is that the taxpayer will get credited for a laborer and get to deduct the laborer's wage expenditures from its taxes as long as that laborer is classified as part of the allowable lease expenditures. He is concerned that by not declaring non-Alaskans as lease expenditures or by paying them under the table, a taxpayer could save 5 percent on its gross taxes by saying it had a 100 percent Alaska resident workforce.

CO-CHAIR JOHNSON allowed that that is a possibility.

2:51:57 PM

MS. DAVIS offered to run some numbers in this regard. As long as this credit does not dominate the value to an operator of having that underlying lease expenditure, then the drive to get the lease expenditure should still dominate and this tax credit will hopefully be subordinated to that.

CO-CHAIR JOHNSON said he is hoping the math works out that it is better for the operator to hire the Alaskan than to cheat.

COMMISSIONER GALVIN quipped that the department prefers to call it tax avoidance as opposed to tax evasion. He noted that it is a company's right to avoid taxes where legally possible.

2:52:54 PM

REPRESENTATIVE P. WILSON commented that if she were a laborer she would not want to be paid under the table because there would be no protection supplied by unemployment insurance and other benefits.

CO-CHAIR JOHNSON answered that he does not think it is under the table that is being talked about but rather being off the records that relate to the tax structure of Alaska. In other words, tax avoidance, not tax evasion.

The committee took an at-ease from 2:54 p.m. to 3:02 p.m.

3:02:38 PM

MR. LARSEN related that prior to ACES, overhead was considered a direct cost. However, ACES made a distinction between direct cost and overhead, and overhead was changed to being a lease expenditure separate from direct cost. This is not a minor distinction out in the oil field, he advised. He explained that the previous portion of his presentation regarding type one and two labor referred to the direct charges that operators will make pursuant to operations. The purpose of the overhead is to allow an operator to recover costs that it incurs as operator of the property that are not recovered through the direct charges. The mechanism used to do that is overhead. One of the tenants of overhead in a joint operating agreement is that an operator shall neither profit nor incur cost due to its position as the operator, so all the working interest owners and parties to the agreement have resolved to make the operator whole for these types of costs.

MR. LARSEN explained that typically, the joint operating agreement allows the operator to recover certain indirect and overhead costs incurred offsite of the exploration, development, or production operations [slide 14]. This is because if it was an onsite cost it would be recovered as a direct cost. The overhead costs are not directly billed but recovered through the overhead allowance.

3:04:50 PM

REPRESENTATIVE SEATON understood that people on the job would be included in the overhead allowance and would therefore not be individually reported as a lease expense because they would be covered in the overhead.

MR. LARSEN replied correct, their costs are not billed direct, but are recovered through the overhead mechanism.

3:05:21 PM

MS. DAVIS explained that the department is discussing this to make it clear that overhead does contain labor costs. It is allowed as a lease expenditure and therefore the department would read Version E to include the labor costs incurred by an operator that are corporeal to the operator's overhead charge, even though it is an indirect charge and does not look as dominant or as obvious as the direct charges for labor. Typical overhead labor includes technical supervisors, drafting and engineering aides, accounting, clerical, certain legal activities but not attorneys, and offsite computer and

communications activities [slide 15]. These are things that support the operator in doing its job and the operator is allowed to charge the costs for it. As currently written, Version E would cover all of those labor costs and this is being flagged in case that is not the intent of the committee.

CO-CHAIR JOHNSON responded that he wants to look at the advantages and disadvantages of doing this. He wants to include as many people as possible in the formula that pushes Alaskan jobs, although there may be some point at which that needs to be cut off because it does not make sense.

3:07:11 PM

MS. DAVIS asked Mr. Larsen whether overhead labor is generally the people who are working out of the headquarters office and would that office be located in Alaska.

MR. LARSEN replied that care must be taken when talking about overhead because in general it is not specific jobs or functions that are being talked about; rather, it is a kind of general allowance meant to cover a category of costs that are incurred by the operator. Specifically identifying those individuals is therefore an area where he would want to tread pretty lightly.

REPRESENTATIVE GUTTENBERG inquired whether Ms. Davis's question was about including in the bill the accountant who spends a portion of his or her time doing the calculations for the North Slope.

MS. DAVIS answered yes.

3:09:15 PM

REPRESENTATIVE SEATON presumed the rebate would be by taxpayer.

MS. DAVIS agreed.

REPRESENTATIVE SEATON asked whether there are any large taxpayers that do not operate any fields and that would therefore have few employees and a high resident hire percentage, or does Version E look at the field and divvy up the number of employees on the field based upon the percentage of ownership of that field?

MS. DAVIS responded that DOR would look at the cost reported on each taxpayer's tax return. Each taxpayer gets allocated a

share of the lease expenditure for each field in which it has an ownership interest. For example, a taxpayer owning 20 percent of Prudhoe Bay would be charged 20 percent of those lease expenditure costs and that would be reflected in the tax return. Those costs are offset against the taxpayer's revenue to arrive at the tax value from which the tax is calculated. The department would consider that taxpayer, as it does the operator, an employer of those people. So, every working interest owner on the North Slope would be considered to have a share of these labor costs and therefore have a share of the rebate. The taxpayer is driven by the operator because the operator controls who gets hired and who is doing what.

3:11:19 PM

COMMISSIONER GALVIN added that all of this revolves around the word "incur" and whether the taxpayer "incurs labor costs" [page 6, line 9, Version E]. The department is interpreting this to mean that if a taxpayer is charged for labor costs it has incurred those costs, regardless of whether the charge is from the operator of the field in which the taxpayer is a working interest owner or from a contractor hired directly by the taxpayer. Initially, it is the operator that incurs 100 percent of the labor cost. That operator will have a certain percentage of Alaskans that it hires. The operator will then divvy up that cost among the working interest owners according to percentage of ownership. Each working interest owner will then ultimately incur its portion of that labor cost with that percentage of Alaska hire. A taxpayer that is the operator of one field and the working interest owner of another field has more direct control over the percentage of resident hire allocated in the field it is operating, but will be a "rider in the car" for the other field. A blend of the two will ultimately determine that taxpayer's qualification for this rebate.

3:13:22 PM

COMMISSIONER GALVIN, in further response to Representative Seaton, pointed out that the unit of measure under Version E is hours. Therefore, the percentage for each working interest owner would be based upon the total number of hours worked for the whole field for the year. A 20 percent owner would get 20 percent of the total hours worked - both the total hours worked and the total Alaska hours. If that field dominates that taxpayer's Alaska portfolio, it may not matter too much what the taxpayer's other ownerships are because the taxpayer will get that 80 percent as a significant portion of its overall

calculation. He posed another scenario in which a taxpayer is a working interest owner of a field with 80 percent Alaska hire and the operator of another field with 70 percent Alaska hire. In this case, the taxpayer would be knocked from qualification for the first tier because the blend of the two fields brings the taxpayer below 80 percent. However, if the working interest partner of that field has no other operations in the state, it would get the rebate. The rebate is taxpayer specific and depends upon each taxpayer's portfolio and the number of hours being worked for the various fields and the individual taxpayer's share of those hours.

3:15:48 PM

REPRESENTATIVE SEATON inquired whether the department would use a formula of some kind for salaried workers.

MS. DAVIS deferred the question to the Department of Labor & Workforce Development. However, she guessed that DLWD could use a little more guidance. The problem with people who are salaried is that they could in actuality work 20 hours a day, rather than 8 hours, and therefore guidance from the legislature would be helpful in what to do in that kind of instance.

3:17:00 PM

MR. LARSEN resumed his presentation and began discussion about non-deductible lease expenditures for labor [slide 16]. He acknowledged that some types of labor are included under both overhead and non-deductible and that he may have been remiss to have identified specific jobs or people associated with the overhead, specifically the legal and accounting people. In regard to labor that is not an allowable lease expenditure, he provided the following examples: tax; legal; accounting; labor expenses that are for the benefit of an individual lessee or producer only, and not necessarily for the benefit of the joint operations or production; and community, public, and government relations.

MR. LARSEN explained that no two joint operating agreements are alike, and some may have an election where a partner indicates that certain classes of cost shall constitute a direct expense or shall be included in the overhead rate. Depending upon the election, the overhead rate is adjusted accordingly. Examples of those classes of costs would include certain types of technical labor, such as the computer and the lease operations application for remote technologies, and legal costs

specifically for perfecting the lease or protecting an owner's interest in the lease. The accounting necessary for paying the people that are up there would be covered as a part of the overhead rate, but the rest of the day-to-day operations of the accounting function for the operator's or producer's other employees would not be covered by the overhead rate.

3:19:53 PM

MR. LARSEN elaborated further in regard to the labor expenses that are for the benefit of the joint operations. He said the lease expenditures are allowed for the operator, which is the company that actually runs the lease. It is the operator, not the working interest owners, that is involved in the day-to-day operations and in determining who is employed on the lease. The working interest owners then pay their share of the operator's costs for those employees. The individual geologists or engineers who are looking out specifically for the interest of a company are not chargeable as a lease expenditure because they are not involved in the day-to-day production operations and this is a production tax that is being talked about.

3:21:08 PM

MR. LARSEN, in response to Representative Guttenberg, confirmed that the sole owner of a lease is the operator of the lease and would therefore qualify for those expenditures. In further response, he said the department's regulations apply whether it is an operator that has other parties as working interest owners or an operator that is the sole party of interest in the field.

3:22:06 PM

MS. DAVIS, in response to Representative Seaton, explained that an operator will nearly always represent all of the owners in the relationship to contractors and others, so the operator will incur the legal obligation and be responsible for paying the entire bill. The operator then bills out the costs to the other parties to be reimbursed. There may be a rare instance where a very small operator cannot afford to take the hit so the operator allocates the bill; however, that is very unusual. In further response, she clarified that once a working interest owner pays its share of the billed costs to the operator, the owner incurs that cost and that cost becomes the owner's legal lease expenditure that can be reported against the owner's tax return.

3:24:24 PM

REPRESENTATIVE OLSON, in regard to when a CS for Version E is done, asked whether it would be easier to take the original version of ACES and put the local hire provision into that.

COMMISSIONER GALVIN responded no, because then there would be two different universes of lease expenditure and both the taxpayer and the state would have to simultaneously have two different definitions and that would create a significant burden for both. In further response, he said the base tax in the original version of ACES was 25 percent, the progressivity was 0.2 percent, and there was a gross tax floor.

3:25:53 PM

REPRESENTATIVE SEATON inquired whether it would be a lot cleaner to have the state give a rebate of $20,000 for every employee above a specified percent that is hired into the company. Then it would be a known amount and it would be a significant incentive for actual hiring of Alaskans without going through complex calculations and regulatory procedures.

CO-CHAIR JOHNSON replied that Representative Seaton's suggestion would not be optional and would make Alaskans on a different par than nonresidents and would not stand muster. Version E makes it optional. However, he said he will take a look at it.

REPRESENTATIVE SEATON added that his suggestion could be made an optional credit that a taxpayer could choose to apply for.

CO-CHAIR JOHNSON answered that the local hire provision in Version E was modeled a little bit after the film credit because that credit has withstood some time, although there has not been a legal challenge to it.

3:27:58 PM

MS. DAVIS returned to the Department of Revenue's presentation to discuss the progressivity rate change proposed by HB 308, Version E. She called attention to slide 18 depicting the nominal tax rates currently in effect under ACES, and which include the [25 percent] base tax and the 0.4 percent [progressivity] that goes up to 0.1 percent [after a 50 percent production tax rate is reached]. Under the nominal tax rates proposed by Version E, the progressivity kickoff point would be similar but the progressivity would be 0.2 percent up to $155

per barrel production tax value [slide 19]. For comparison, slide 20 is an overlay of the two aforementioned charts.

MS. DAVIS specified that the change in state revenue from the [proposed change in progressivity] is what is relevant to the Department of Revenue. The department asked the question, If the state does not have the revenue, who does? Slide 21 depicts the answer under three different scenarios of oil prices. The key point is that when the state gives up revenue, it is not a purely efficient transfer to the contractors because the federal government captures a chunk. Once the annual average oil price reaches $76 per barrel and progressivity starts to take effect, money would begin shifting to the federal government. At $100 per barrel a sizeable amount of money would shift to the federal government. Thus, as progressivity starts to play a bigger role, money would shift to the federal government. The direct money transfer that Representative Seaton was describing might have some linkage to the federal tax as well.

3:29:54 PM

MS. DAVIS, in regard to the retroactive interest waiver proposed by Version E, explained that DOR can waive the penalty associated with an amended or revised tax bill that is caused by a change or by retroactive application of a regulation. However, the department does not have the statutory authority to waive the interest that would accrue. So, when asked by the governor what the department would see as an important improvement to ACES, the department recommended that the interest not begin until a reasonable period after the regulation is put in place. Under the proposed provisions of Version E, underpayment would not be considered delinquent until after 30 days from the effective date of the regulation. Under the proposed provisions of Governor Parnell's bill [HB 337], interest for underpayment would be waived before the first day of the second month following the month in which the regulation became effective; thus it could be as low as 31 days, but as high as 60 days. It is a matter of making sure that both the department and the taxpayer have enough time to react.

3:30:59 PM

MS. DAVIS addressed the proposed change in interest rate for interest the state would owe the taxpayer when taxes are overpaid [slide 24]. She asked members to disregard the typographical error at the bottom of the page which states that Version E changes the long-standing rule that interest is not

allowed if an overpayment is refunded within 90 days; Version E would not change this rule. The place where Version E adds a unique factor is the change in the interest rate itself. The department looked into this and learned that the interest rate was raised [in 1991] because interest rates were much higher at that time. Additionally, there was a view at that time that taxpayers were essentially using the state as the bank so to speak. So, there needed to be a high enough interest rate that taxpayers would be incentivized to go ahead and pay disputed amounts. For example, the state might earn 5 percent on the difference, but a company might be able to make 10-15 percent on the money that it kept in its pocket. From a revenue forecast and flow point of view, DOR believes it is easier to not make the state the bank and that is why Governor Parnell's bill does not propose to change the interest rate.

CO-CHAIR JOHNSON stated that Version E is modeled after what the Internal Revenue Service does.

3:32:34 PM

MS. DAVIS spoke to the proposed provision for a 30 percent credit for well-related expenditures [slide 26]. [HB 308, Version E, would provide this credit by amending AS 43.55.023; the governor's bill would amend AS 43.55.025.] She noted that that there is a gap in the statutes for well credits. Wells that are less than three miles out do not qualify for credits under AS 43.55.025, and AS 43.55.023 provides a 20 percent credit only for qualified capital expenditures. When working on the governor's bill, the department's goal was to find a place for a 30 percent credit on well work that would yield immediate production benefits. Capital expenses needed to go from 20 percent to 30 percent and operating expenses needed to go from 0 percent to 30 percent. Therefore, the governor's bill puts the proposed 30 percent well credit under AS 43.55.025 because that statute covers both capital and operating expenses. Also, it is important to share information with the Department of Natural Resources (DNR) and an information-sharing requirement is already provided by AS 43.55.025. Additionally, to correct the inequity when an explorer is less than three miles out, the governor's bill proposes to collapse and meld the three-mile and in-field expenses in a rewrite of AS 43.55.025. Thus, the department approached the same problem as did the sponsor of HB 308 and got much the same result. However, the department believes that administratively the proposed credit for well work might be cleaner in AS 43.55.025 and therefore recommends the committee look at that statute for HB 308.

3:34:42 PM

CO-CHAIR JOHNSON said AS 43.55.023 only deals with capital expenditures. He surmised that if both capital and operating expenditures are credited it will be more money that can be deducted.

MS. DAVIS responded that when DOR read HB 308, it was unclear that the credit was being limited to capital costs, and the department thought the sponsor's intent was to pick up the capital and operating expenses.

CO-CHAIR JOHNSON stated that it was, by the nature of it being in AS 43.55.023. He presumed the effect would be the same; it is just where it is placed in the statute.

MS. DAVIS agreed that it is.

COMMISSIONER GALVIN pointed out that AS 43.55.023 defines capital credits. To get the well work that is currently considered to be an operating credit, not a capital credit, a portion of AS 43.55.023 would have to be carved out that says that for this category AS 43.55.023 is broader. It is this amalgam within the AS 43.55.023 credit that becomes a bit problematic because this extra concept is attached to the side of it. When dealing with this same problem, the department found that AS 43.55.025 provided a cleaner way of expanding that definition.

3:36:22 PM

REPRESENTATIVE SEATON pointed out that with in-field work there is no risk because it is known that the pool is there. The trade-off was that the further the step-out, the more risk, thus the more credits that are needed. Now, it is being proposed that there be 30 percent capital and 30 percent operating credits. In addition, the 25 percent base rate and the progressivity will be deductible since these are lease expenditures. He expressed his concern that the state could end up paying more than 100 percent of these non-risky investments.

3:38:19 PM

COMMISSIONER GALVIN replied that AS 43.55.025 credits cannot be added to AS 43.55.023 credits; they are mutually exclusive of each other and a company cannot receive both. Under

Representative Seaton's scenario, the state would provide a 30 percent credit for well work and the company would get to deduct that cost and the 25 percent plus progressivity. But that is where it would stop because it is one system or the other.

COMMISSIONER GALVIN, in regard to incentivizing risky and economically challenged projects versus less risky in-fill drilling, said he is not suggesting that this now be seen differently. Rather, he is recognizing is that there is within a field a spectrum of potential projects that could be pursued and those projects are going to have different economics depending upon what the expected cost is to reward. He allowed that there will likely be projects that will qualify for this credit that would have proceeded without the credit. However, the intent of the governor's proposal, which he thinks is shared by Co-Chair Johnson's proposal in HB 308, is that there are also likely to be a suite of projects that this credit will kick over the threshold from no-go to go, and those are the ones DOR is trying to target. The department feels this tradeoff is appropriate given that at the end of the day a company is going to have to actually spend money to earn these credits.

CO-CHAIR JOHNSON said he remembers the step-out differently. Yes, the step-out was more risky, but it was also new oil for the Trans-Alaska Pipeline System. However, it is his view that anything that accomplishes that goal, whether it is three miles out or in the existing field, is eligible for those credits. If it puts oil down the pipeline, that is what the state is after. It is not necessarily the risk, but the oil that is put down the pipeline.

3:42:05 PM

REPRESENTATIVE SEATON requested that the department provide an analysis of what the state's participation would be at these higher credit lines for in-field, no-risk projects under various oil price scenarios.

COMMISSIONER GALVIN agreed to do so.

CO-CHAIR JOHNSON cautioned against using the term no risk. Any time a drill rig is set up there is a risk, it just might be less risk.

3:43:14 PM

REPRESENTATIVE GUTTENBERG commented that some of the re-work activities only require a small crew, not setting up a full drilling rig. He agreed that some of these things would get done anyway because it is in the company's economic interest to so, regardless of tax credits or other incentives. He inquired whether there is a way to separate these out and make this only for those that need an incentive.

CO-CHAIR JOHNSON responded that this is not what is being talked about here, but Representative Guttenberg would be welcome to introduce such a bill. If it were the case that companies would do it anyway, then the companies would be doing it, but the companies are not despite an oil price of $70 per barrel. The question is why not.

REPRESENTATIVE GUTTENBERG said he is not sure that is true. Companies have a lot of these things on schedule and that is what he is talking about. Things that are on a company's normal maintenance schedule, such as re-logging, re-cracking, re-casing, are being done anyway.

CO-CHAIR JOHNSON replied that the committee will be hearing from the producers in this regard.

3:45:36 PM

MS. DAVIS drew attention to a section of the proposed well credit in HB 308, Version E, that defines what is a well-related expenditure: up to the flange and connecting the well head to the well line [slide 26]. She said the department is unclear whether this modifier references only the intangible drilling and development costs or also reaches up and is a qualifier on the other listed well-related activities.

CO-CHAIR JOHNSON answered that the intention is the well activity and not beyond the well, so it is setting the rig up and not the pipeline or other things that might need to be redone. It is strictly the well workover expenditure.

MS. DAVIS added that the department was thrown off by the well-related seismic work that is included in the provision. She suggested that some drafting finesse be done to clarify that.

3:46:38 PM

MS. DAVIS reviewed the last change proposed by HB 308, Version E, which is the change in the statute of limitations for

production tax assessments. She began this discussion by reviewing the department's current production tax audit status [slide 28]: eight production profits tax (PPT)/ACES audits are in progress for the time period of April-December 2006, with completion of these audits estimated to be 3/31/2010; two PPT/ACES audits pending from the year 2006 which will be completed after 3/31/2010; one economic limit factor (ELF) audit in process from the 2003, 2004, 2005 time period [which will be completed after 6/30/2010]; and three credit audits for 2006 [with estimated completion by 3/31/2010]. She noted that as a result of ACES, the department must also now do credit audits, and out of the department's eleven auditors, four are dedicated full-time to just auditing credits. Six auditors, and soon seven, are focused on production tax returns. There are two empty auditor positions.

3:47:59 PM

CO-CHAIR NEUMAN inquired whether audits generally result in more money coming in to the state or the state owing money.

MS. DAVIS responded that generally most audits result in some increase in tax payments to the state.

CO-CHAIR NEUMAN asked where that money would be seen.

MS. DAVIS said she believes money received from audit and resolution settlements goes into the Constitutional Budget Reserve (CBR).

CO-CHAIR NEUMAN presumed the funds would come out of the CBR if the state owed a taxpayer money after an audit.

COMMISSIONER GALVIN answered that he is not aware of many times when an audit resulted in a repayment; usually a taxpayer pushes the definition to its advantage. If there is a necessity to repay a taxpayer, it would have to be appropriated by the legislature as that is not something the department would do on its own.

3:50:02 PM

REPRESENTATIVE GUTTENBERG noted that the legislature previously authorized the Department of Revenue to hire more auditors at a premium salary range. He inquired whether more auditors would allow the department to decrease the audit time [from six years] to three years.

MS. DAVIS responded that the authorization was for master auditors and that by statute those individuals supervise audits as opposed to doing audits. The department has what it needs for master auditors, but needs "worker bees." The challenge is being able to attract qualified auditors with oil and gas experience that can step in and immediately do these high level, complicated audits. Generally, what the department can attract is beginning level individuals who must be trained; so the department is using the credit audits as the training ground.

3:51:33 PM

REPRESENTATIVE GUTTENBERG noted that slide 28 shows that the audits for all taxpayers for the years 2007 and 2008 have not yet been started. He surmised that a taxpayer submits its taxes for the previous year and something triggers an audit or an audit is just done automatically. He inquired whether it is the department's time that is delaying this or the department waiting for industry responses.

MS. DAVIS replied that it is a combination of both. The department gets after the immediate ones, such as the older ones where the time limit is coming up. But, by and large, the department is driven by information gathering. The information that is required to do an audit under ACES is substantially more expansive than it is for the tax type under ELF [slide 29]. For example, additional information required by ACES includes all of the lease expenditures, joint operating agreements, tracking overhead charges, and all of the various credits that must be rolled up to apply against the tax bill. Audits are now much more work than they were under ELF, and that is the reason why ACES extended the statute of limitation from three years to six. If the statute of limitation is returned to three years, as proposed by HB 308, Version E, the department would definitely require additional oil and gas tax auditors to be able to complete the work in that timeframe.

MS. DAVIS returned to Representative Guttenberg's question, saying that it is an almost equal combination of department staff and the taxpayers needing to pull together all of the aforementioned information for the audit. The department is very driven to stay within that two- to three-year timeframe of staleness because the department recognizes it costs the taxpayers money to keep the records around. However, once the department has the information, it takes awhile to digest and analyze it and have discussions with the taxpayer, and this

takes the department from the three years to the four and five year timeframe to conclude a tax audit.

3:54:28 PM

MS. DAVIS, in further response to Representative Guttenberg, explained that the proposed change in the statute of limitations requires the department to conclude an audit within the three-year timeframe, not begin the audit, because at the conclusion of the audit is when the assessment is made as to what the department believes the tax bill truly should be. The department would be forced to scramble because it could not risk loss of value to the state and would essentially shift what is now a mostly cooperative environment with the taxpayers to a confrontational one. More hearing officers would likely be needed and there would likely be more litigation accompanied by litigation costs.

3:55:48 PM

REPRESENTATIVE GUTTENBERG asked what the average audit time is right now.

GARY ROGERS, Oil & Gas Revenue Specialist, Tax Division-Administration, Department of Revenue (DOR), answered that once an auditor has all of the information it can take a year or more to do. It takes a long time to get the information, digest it, process it, re-run calculations, discuss those with the taxpayer, and go back and forth to get more information. This is why it takes years to do these audits.

JONATHAN IVERSEN, Director, Tax Division-Administration, Department of Revenue, agreed with Mr. Rogers. He pointed out that on slide 29 it can be seen that the number of bullets for information required under ACES is double that of ELF. However, those bullets represent three to five times more information that is required under ACES than under ELF. The ELF audits took roughly 3 years to do and were being done by people with 15-20 years of experience. Today, by and large, the department has a very inexperienced staff due to retirement.

3:58:30 PM

REPRESENTATIVE P. WILSON presumed that DOR is not getting the information back from the taxpayers soon enough.

MS. DAVIS allowed that this is one of her concerns. Right now the department's entire tax system is manual. The department has endeavored to have on-line filing and a 56-page tax form has gone out to the taxpayers to use next year. The oil companies are struggling to interface with the state's antiquated system. The tax form is a Microsoft Excel spreadsheet and when it comes back the auditors will have to search through it to find things. There is nothing automated that will kick out capital or operating expenditures or credits. It does not flow easily. Having an automated system would help with the information sharing and would be a key part. The department must launch an audit within two years so it can begin to get data while it is fresh and have ample time to exchange it with the taxpayer. Some of the information is lying outside of Alaska in locations where the companies have centralized their accounting and tax systems.

4:00:15 PM

REPRESENTATIVE P. WILSON inquired how much an automated system would cost.

MS. DAVIS responded that it was in a prior year appropriation and at that time it was about $30-$35 million to automate all of the tax types so that fisheries and all the other folk would be able to have on-line filing and interface with the systems. The governor's budget this year has $300,000 to study how the department would go about getting an automated system. She pointed out that DNR has six years to do audits on the royalty side, and the set of information that DNR must review is substantially less than that for the Department of Revenue. Therefore, DOR is happy to have a six-year statute of limitation.

4:01:37 PM

CO-CHAIR JOHNSON said a reliable computer system is reasonable for the department that is responsible for 85 percent of the state's budget. He asked whether DOR audits everyone.

MS. DAVIS replied no.

CO-CHAIR JOHNSON surmised it is like the Internal Revenue Service and there is a formula that Ms. Davis cannot share.

MS. DAVIS answered that that is probably accurate.

CO-CHAIR JOHNSON inquired whether Ms. Davis can state the percentage that is audited.

MS. DAVIS responded that it depends upon the tax type because the department is trying to ensure that the lion's share of the revenue coming in is accurate.

4:02:34 PM

CO-CHAIR JOHNSON asked why everyone is not audited given that audits result in more money.

MS. DAVIS replied that DOR does not have the staff to do that.

CO-CHAIR JOHNSON inquired whether it would make sense to have staff to do that, and how much money would that cost.

COMMISSIONER GALVIN answered that it is like the "80-20 rule," where with 20 percent of the effort, one gets 80 percent of the results. In terms of responding to the question, the department must make sure that it is requesting and providing a picture of where it believes it can get the best return for the additional expenditure. Similar to how a tax system relates to investment, there are a number of different factors that would go into the ability of just giving the department more staff and more appropriation and having more audits and more effective audits.

CO-CHAIR JOHNSON interjected that he is not interested in auditing everyone. In regard to the six years, he requested that the department think about whether there are ways to streamline things and make them more efficient.

4:05:42 PM

COMMISSIONER GALVIN returned to the resident hire provision proposed by Version E and noted that in retrospect the numbers shown on slide 5 are still valid.

MS. DAVIS directed attention to the far right column of the top table on slide 5 labeled, "Current Tax Liability before Rebate," and instructed members to assume the figures are calculated appropriately with the rebate going against the base tax only. The slide depicts three companies: Company A is small, Company B is medium sized, and Company C is large. She then directed attention to the bottom table on slide 5 and explained that Company A currently has a workforce of 87 percent Alaska residents and wants to get to 87.5 percent. Company A is

currently enjoying a 6 percent rebate so the current tax rebate is $6 million. If Company A gets to the 87.5 percent [by adding 20 Alaskan employees], it will receive $8 million in rebate, an increase of $2 million. Company B is currently at 82 percent Alaska workforce and if it goes to 82.5 percent by adding 29 Alaskan employees it will receive an additional $10 million. Company C is at 79.5 percent and has no rebate, but if it goes to 80 percent by adding 50 Alaskan employees it would receive a $30 million rebate.

4:08:06 PM

COMMISSIONER GALVIN added that the number of employees means the hiring of Alaskans who are currently not part of a company's labor pool; the Alaska hires would be an addition to the company's existing labor pool. It is not being said that the Alaskan employees would substitute for out-of-state workers, which would be a potentially lower number to make that change.

MS. DAVIS interjected that the chart is not assuming any firing.

4:08:35 PM

MS. DAVIS moved to slide 6, which depicts the least amount that the rebate would be. If Company A moved from an 87.5 percent Alaska workforce to 90 percent, then that would be an addition of 20 employees and it would cost about $19,000 per employee. It could be anywhere from $2 million to that number depending upon how close Company A is to the line in the tier. This gets to the discussion of whether it would be better to do it in a linear fashion if there is a way to draft it because that would avoid the inequities on either end of the line.

CO-CHAIR JOHNSON responded that he is not locked in if there is a way to draft it as he does not want to deter someone from going from 82 percent to 85 percent. He said he would like to see that every employee hired is a benefit and allowed that maybe Representative Seaton's way is the right way to go. He added that he would like to work with the department on some of the finer points. The committee should move with the things on which there is agreement and where there is disagreement there should be an attempt to make them as palatable to the administration as possible.

[HB 308 was held over.]

4:10:54 PM

ADJOURNMENT

There being no further business before the committee, the House Resources Standing Committee meeting was adjourned at 4:11 p.m.