

**ALASKA STATE LEGISLATURE
HOUSE RESOURCES STANDING COMMITTEE**

February 24, 2010

1:19 p.m.

MEMBERS PRESENT

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

MEMBERS ABSENT

All members present

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."

- MOVED CSHB 217(RES) OUT OF COMMITTEE

HOUSE JOINT RESOLUTION NO. 40

Opposing the proposed designation by the National Marine Fisheries Service of 3,000 square miles of upper Cook Inlet, the mid-inlet, all of the inlet's western shores, and Kachemak Bay as critical habitat for beluga whales.

- MOVED CSHJR 40(RES) OUT OF COMMITTEE

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)
02/10/10 (H) RES AT 1:00 PM BARNES 124
02/10/10 (H) Heard & Held
02/10/10 (H) MINUTE(RES)
02/15/10 (H) RES AT 1:00 PM BARNES 124
02/15/10 (H) Scheduled But Not Heard
02/17/10 (H) RES AT 1:00 PM BARNES 124
02/17/10 (H) -- MEETING CANCELED --
02/22/10 (H) RES AT 1:00 PM BARNES 124
02/22/10 (H) -- MEETING CANCELED --
02/24/10 (H) RES AT 1:15 PM BARNES 124

BILL: HJR 40

SHORT TITLE: COOK INLET/KACHEMAK BELUGA POPULATION
SPONSOR(S): REPRESENTATIVE(S) MILLETT

01/27/10 (H) READ THE FIRST TIME - REFERRALS
01/27/10 (H) RES
02/24/10 (H) RES AT 1:15 PM BARNES 124

WITNESS REGISTER

DAN STICKEL, Petroleum Economist
Tax Division-Economic Research Group
Department of Revenue (DOR)
Juneau, Alaska

POSITION STATEMENT: During the hearing on HB 217, provided information, answered questions, and suggested amendments.

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.

REPRESENTATIVE CHARISSE MILLETT
Alaska State Legislature
Juneau, Alaska

POSITION STATEMENT: Testified as the sponsor of HJR 40.

JEFF TURNER, Staff,
Representative Charisse Millett

Alaska State Legislature
Juneau, Alaska

POSITION STATEMENT: During the hearing on HJR 40, explained the differences between the original resolution and the proposed committee substitute, Version E, on behalf of Representative Millett, sponsor.

ARNE FUGLVOG, Legislative Assistant
to U.S. Senator Lisa Murkowski
Washington, D.C.

POSITION STATEMENT: During the hearing on HJR 40, provided information and answered questions.

RICHARD BERKOWITZ, Pacific Coast Director
Transportation Institute
Seattle, Washington

POSITION STATEMENT: Supported HJR 40.

JOHN MCCLELLAN, P.E.
Tyonek Native Association
Anchorage, Alaska

POSITION STATEMENT: Supported HJR 40.

JASON BRUNE, Executive Director
Resource Development Council
Anchorage, Alaska

POSITION STATEMENT: Supported HJR 40.

BRUCE WEBB
Anchorage, Alaska

POSITION STATEMENT: Supported HJR 40.

STACY SCHUBERT, Intergovernmental Affairs Director
Mayor's Office
Municipality of Anchorage
Anchorage, Alaska

POSITION STATEMENT: Supported the proposed committee substitute for HJR 40, Version E, on behalf of Mayor Dan Sullivan.

GRAHAM SMITH, Communications and Membership Director
Alaska Support Industry Alliance
Anchorage, Alaska

POSITION STATEMENT: Supported HJR 40.

ACTION NARRATIVE

[1:19:38 PM](#)

CO-CHAIR CRAIG JOHNSON called the House Resources Standing Committee meeting to order at 1:19 p.m. Present at the call to order were Representatives P. Wilson, Olson, Kawasaki, Seaton, Tuck, Neuman, and Johnson. Representatives Guttenberg and Edgmon arrived as the meeting was in progress.

HB 217-TAX ON GAS FOR IN STATE MANUFACTURING

[1:20:01 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." [Before the committee was the proposed committee substitute for HB 217, labeled 26-LS0816\R, Bullock, 2/1/10 ("Version R").]

[1:20:23 PM](#)

REPRESENTATIVE NEUMAN reminded members that his intent as sponsor of HB 217 is to expand manufacturing in the state, and this provision can be found on page 10 of Version R. He stressed that HB 217 is also a jobs creation bill. Three [oil] companies pay 90 percent of the state's expenses, he pointed out, and this bill is one of several in committee that seek to create an environment in the state in which industry and hundreds of companies can thrive. The bill would go a long way in helping to provide for an anchor tenant for an in-state gas pipeline, a project that might not happen otherwise. An in-state gas pipeline would benefit the entire state because it would support development, such as the Donlin Creek Gold Mine that would provide 2,000 family-sustaining jobs. Alaska does not have the time to continue delaying this project, he opined, given the state's current dependence on only three companies.

[1:22:31 PM](#)

REPRESENTATIVE NEUMAN noted that today he is providing several amendments as requested previously by committee members. One of those amendments expands on the meaning of manufacturing.

REPRESENTATIVE P. WILSON moved the adoption of Amendment [2], labeled 26-LS0816\R.4, Bullock, 2/23/10, written as follows [original punctuation provided]:

Page 10, line 4, following "product":

Insert "; in this paragraph, "manufacturing process" does not include cooling gas for the purpose of storing or shipping the gas as a liquid"

CO-CHAIR JOHNSON objected for discussion purposes.

[1:23:13 PM](#)

REPRESENTATIVE NEUMAN explained that the language added by Amendment 2 would ensure that the export of liquid natural gas (LNG) is not included as a manufacturing process, given that the cooling and compressing of gas is the method used for moving gas. The bill is meant to deal with manufacturing which is a molecular change. However, the Department of Law does not want to define manufacturing in statute and has some conceptual amendments to Amendment 2 that it would like to offer.

[1:24:24 PM](#)

REPRESENTATIVE TUCK asked whether another definition of manufacturing had previously been moved forward. In response to Co-Chair Johnson, he said he remembers a different amendment that did the same thing.

REPRESENTATIVE NEUMAN replied that perhaps Representative Tuck is referring to one of the Department of Revenue's suggested amendments to Amendment 2.

CO-CHAIR JOHNSON pointed out that HB 217 was amended once before. [Amendment 1 to the original version of HB 217, labeled 26-LS0816\A.1, Bullock, 4/13/09, adopted on 4/13/09.]

[1:26:27 PM](#)

DAN STICKEL, Petroleum Economist, Tax Division-Economic Research Group, Department of Revenue (DOR), stated that the department had informed the sponsor that a clear definition of manufacturing was needed before the bill could be supported by the administration. Work was done within the Department of Revenue, along with the Department of Law and the Department of Natural Resources, to come up with a suggested definition for manufacturing under HB 217, and perhaps this is what Representative Tuck is speaking to. To protect against certain unintended consequences, the Department of Revenue recommends that the list of exclusions from the manufacturing definition in Amendment 2 be expanded to include gas processing, gas

treatment, dehydration, fractionation, compression, or liquefaction.

REPRESENTATIVE NEUMAN responded that he is working toward a gas-to-liquids, or Fisher-Tropsch process, which takes methane apart at the molecular level and reconnects the chains of waxes to create different transportation fuel components. He said he is concerned as to whether that would be considered gas processing or fractionation of molecules; therefore, he would like to know if that would be the case.

[1:28:31 PM](#)

REPRESENTATIVE SEATON surmised the department's fear is that if certain things like compression and conditioning are not excluded, an unintended consequence could be that a gas conditioning plant is suddenly considered manufacturing and all the gas transmitted down a pipeline, whether for import or export, could then qualify for this proposed lower tax rate.

MR. STICKEL answered that this is exactly the situation the department is trying to protect against by having this longer list of exclusions from manufacturing. In response to Co-Chair Johnson, he stated that Amendment 2 does not currently include the Department of Revenue's suggestions.

[1:31:23 PM](#)

REPRESENTATIVE P. WILSON pointed out that Amendment 2 does not define manufacturing; rather, it states what is excluded from consideration as manufacturing. She said she understands what is being accomplished by Amendment 2 should more exclusions need to be added to it.

REPRESENTATIVE NEUMAN related his understanding that the administration's suggested amendment to Amendment 2 would not interfere with a gas-to-liquids processing plant. He further understood that the administration supports the gas-to-liquids concept to create more jobs. He said he therefore does not have a problem with the proposed amendment to Amendment 2.

The committee took an at-ease from 1:32 p.m. to 1:37 p.m.

[1:37:55 PM](#)

CO-CHAIR JOHNSON removed his objection to Amendment 2.

REPRESENTATIVE P. WILSON withdrew Amendment 2. There being no objection, Amendment 2 was no longer before the committee.

REPRESENTATIVE P. WILSON moved the adoption of Conceptual Amendment 3, dated 2/23/10, written as follows [original punctuation provided]:

"manufacturing" means chemically converting gas or components of gas, or chemically combining gas or components of gas with other substances, to form valuable compounds; "manufacturing" does not include gas processing, gas treatment, dehydration, fractionation, compression, or liquefaction.

CO-CHAIR JOHNSON objected for discussion purposes.

[1:38:46 PM](#)

REPRESENTATIVE NEUMAN read Conceptual Amendment 3 to members and offered his belief that the intent of the amendment is to ensure that LNG export is not considered manufacturing, but a gas-to-liquids process like Fisher-Tropsch is considered manufacturing.

CO-CHAIR JOHNSON inquired whether Conceptual Amendment 3 addresses the administration's concerns and whether the administration is comfortable with this language.

MR. STICKEL offered his understanding that this definition was necessary before the administration could support the bill. Since this particular definition was developed within the Department of Revenue and the Department of Natural Resources in coordination with the Department of Law, the administration is comfortable that it would allow a gas-to-liquids facility or a petrochemicals facility, such as the Agrium facility, to qualify under the manufacturing definition, but the sale of natural gas for a major pipeline or LNG facility would not qualify.

[1:40:48 PM](#)

REPRESENTATIVE GUTTENBERG inquired whether a chemist was involved in drafting the language for Conceptual Amendment 3 to ensure that all possible processes were addressed.

MR. STICKEL responded that a number of people were involved but he does not know their chemistry backgrounds.

CO-CHAIR JOHNSON inquired whether the administration would support this legislation with Conceptual Amendment 3 in place.

MR. STICKEL replied that with this amendment in place the administration could support this bill.

CO-CHAIR JOHNSON withdrew his objection. There being no further objections, Conceptual Amendment 3 was passed.

[1:42:12 PM](#)

REPRESENTATIVE P. WILSON moved the adoption of Amendment 4, labeled 26-LS0816\R.3, Bullock, 2/23/10, written as follows [original punctuation provided]:

Page 3, lines 26 - 27:

Delete "return is due under AS 43.55.030(a) for the calendar year for which the election is made"

Insert "installment payment of estimated tax is due under AS 43.55.020(a) for the month in which the election is made. The election applies to the production of gas in each month for which the election is made"

CO-CHAIR JOHNSON objected for discussion purposes.

[1:42:23 PM](#)

REPRESENTATIVE NEUMAN deferred to Mr. Stickel for an explanation of the amendment.

MR. STICKEL explained that Amendment 4, as presented, would allow for the producer to take the election for the preferential tax treatment - or not - at the time the producer makes its monthly estimated payment. Under this amendment, the producer could make an election to either take the 17.7 cent tax rate or to include the natural gas along with the rest of its production and could make that election on a monthly basis. However, Alaska's Clear and Equitable Share (ACES) tax is calculated on an annual basis, so there is a potential that when the producer files its annual tax return the state could owe interest for overpayments for the monthly estimated payments depending upon the elections that the producer took on a monthly basis. He said the department is flagging this as a concern because it was unknown whether that was the intent of this amendment. The department has some recommended language that would remedy this potential.

1:43:57 PM

REPRESENTATIVE P. WILSON surmised the department would like to have this amendment but would like to have it worded differently while meaning the same thing.

MR. STICKEL answered that that would better address the intent of this amendment. A way to remedy that particular situation would be to have the producer make the election for which tax rate would apply to its manufacturing gas at the time the first estimated payment is made and then have that election apply for the entire year, given the tax is levied on a calendar year basis.

1:45:04 PM

CO-CHAIR JOHNSON said he does not see a way to change the language of Amendment 4 to make this happen.

REPRESENTATIVE NEUMAN said his problem with the department's suggestion is learning about it right now. He reminded members that the reason for this part of the bill is because of concerns expressed by committee members that the current rates being paid by people for home heating and electrical generation could increase because of the way credits are done.

CO-CHAIR JOHNSON asked whether just not adopting Amendment 4 would address the problem.

MR. STICKEL responded he believes that without the amendment a producer could make estimated payments based on either taking the election or not taking the election.

REPRESENTATIVE P. WILSON directed attention to page 3 of Version R, line 25, and suggested that after election the words "either monthly or annually" be inserted.

1:47:38 PM

MR. STICKEL, in response to Co-Chair Johnson, noted that this is not necessarily a showstopper; it is just one issue the department wanted to bring to the committee's attention because of the potential to game the system. One possible change if members wanted to make the election annual would be to have the election made at the time the first monthly installment payment of estimated tax is due under AS 43.55.020(a) for the calendar

year for which the election is made. Thus, at the end of February when a producer makes its first estimated payment, which is for the January production, the producer would choose whether to make this election and that would then hold for the entire calendar year.

MR. STICKEL, in response to Representative P. Wilson, stated that the department's suggested amendment would be made at the same place as Amendment 4, but the inserted language would instead be "first monthly installment payment of estimated tax is due under AS 43.55.020(a) for the calendar year for which the election is made".

[1:49:28 PM](#)

REPRESENTATIVE TUCK inquired what would happen if the producer waited until June or July to make that election rather than making it in February, or would the department's suggested amendment require that the election always be made in February.

MR. STICKEL replied that under the language he just read, the election would be made at the time the producer makes its first estimate.

[1:50:31 PM](#)

REPRESENTATIVE GUTTENBERG posed a scenario in which a gas producer produces 10 billion cubic feet (Bcf) but only uses 2 Bcf for manufacturing. He asked whether the producer could take this credit, which might be the lower of all the possible credits that the producer can take, and apply it to all of its product.

REPRESENTATIVE NEUMAN answered that it is not credits that are being talked about here, but a reduction in production taxes.

[1:51:30 PM](#)

REPRESENTATIVE GUTTENBERG asked whether a reduction of credits could be taken across everything that a producer produces.

MR. STICKEL provided a history of where this election comes from. The department was working with the sponsor on some of the questions that were raised by the committee to look at what the possible impact on a producer's tax liability would be from the lower tax rate of 17.7 cents per thousand cubic feet (Mcf). It was found in the original bill that rolling the manufacturing

gas into a producer's existing portfolio of oil and gas would, in most cases, lower the producer's tax liability. However, there were some situations where the producer's tax liability would actually increase, and that is why the election language came to be. The last thing wanted is to raise a producer's tax liability because the producer started selling gas to a manufacturing facility. The election allows the producer "to take the lower of" on the tax.

[1:52:56 PM](#)

REPRESENTATIVE SEATON remarked that the statement about not wanting it for the month because it could game the system and require the state to pay interest exemplifies his problem with the structure. The only time he sees this as being valuable is when there can be a modeling of the figures, something which he requested but has not yet received. The state would be providing 55-65 percent of the investment in the field through credits and the taking off of production tax and progressivity percentages, but the state would receive back in tax almost zero or 5 percent because this would allow the producers to elect at the end. The state would not even recover its expenses and that is his problem with this, he opined. This is a small gaming of the system that is a big gaming component. While he understands that the intent of HB 217 and Amendment 4 is to stimulate gas-to-liquids (GTLs), which he favors, he fears it will cost the state big-time if the election is tied to when the election is made and not to the time the gas is produced and applied against the producer's oil taxes.

[1:55:49 PM](#)

CO-CHAIR JOHNSON understood that skirts what is being talked about with Amendment 4. However, it is the concept of the overall bill that Representative Seaton has a problem with as much as this particular amendment, he said interrogatively.

REPRESENTATIVE SEATON responded that it is, but the discussion is about when the election is taken. If the talk in this amendment is about the difference between monthly and annual, then his discussion is for later. If the talk in this amendment is about allowing the election to be taken annually when the producer chooses rather than at the start of development, then it is on point now. For example, at the time that development starts at Point Thomson the producer would decide to pay the 5 percent tax for gas to be used in manufacturing and would not take off 60 percent from its oil taxes.

1:56:47 PM

CO-CHAIR JOHNSON surmised that Representative Seaton is more comfortable with the monthly language.

REPRESENTATIVE SEATON noted that such an amendment is not before the committee, but the amendment that would allow the election to be made at a calendar year is what creates the obstacle because it allows a producer to make the election when it is best for its bottom line instead of the start of drilling, and this is where he has a problem. It is an election timing issue, but he is willing to let it go and come back to it later.

1:57:57 PM

CO-CHAIR JOHNSON said he understands where Representative Seaton is coming from, but once the gas is manufactured and producers are electing to do this, the state already has the manufacturing and that is a commercial deal between the two entities that would best play into whoever deals with that and he can see where both would justify.

REPRESENTATIVE NEUMAN argued that nobody is gaming anyone and such comments are inappropriate. The first nine pages of the bill were written by the Department of Revenue, Department of Natural Resources, and Department of Law to make sure the state does not get gamed. He said he has no objection to Mr. Stickel's suggested amendment to Amendment 4.

1:59:54 PM

REPRESENTATIVE TUCK posed a scenario in which a producer elects the Alaska Gasline Inducement Act (AGIA) method for the production tax credit and progressivity and that this is done at the time of first payment, but later in the year the producer begins providing feedstock for manufacturing. He asked whether the producer would be able to take advantage of this bill proposal.

MR. STICKEL deferred to Mr. Gary Rogers.

GARY ROGERS, Oil & Gas Revenue Specialist, Tax Division-Administration, Department of Revenue (DOR), answered that the producer certainly would because the tax calculation that is going to be reported on the producer's annual return is an annual calculation. The producer may not know at the beginning

of the year that it will be producing and selling gas to be used for manufacturing in the state, but at the end of the year that will be known. Perhaps the election should be made at the earliest possible time that the taxpayer knows when it is going to have gas used in state. The Department of Revenue's concern is that a taxpayer could intentionally overpay its monthly estimates and the state would not know that until sometime after March 31 of the following year when the taxpayer files its annual return. The state would then have limited time to determine that there was overpayment and the taxpayer would be earning interest on all those monthly installments for the whole year. There may be a better way to wordsmith this, he added.

[2:03:15 PM](#)

CO-CHAIR JOHNSON inquired whether Mr. Rogers thinks it would be sound business practice to overpay taxes with the expectation of getting interest.

MR. ROGERS replied no, but the potential is there.

CO-CHAIR JOHNSON asked whether Mr. Rogers believes the companies the state is dealing with participate in good business practices; he then added that Mr. Rogers did not have to answer.

[2:03:48 PM](#)

REPRESENTATIVE SEATON inquired whether the election for gas utilized for manufacturing in state is a proportional amount of the total gas.

CO-CHAIR JOHNSON answered if it is not proportional, it should be. He surmised it would be a small portion of the exploration tax credits that Representative Seaton is talking about, given that current law says it must be under 0.5 Bcf per day and not all of the gas would be going to manufacturing.

REPRESENTATIVE NEUMAN stated that if 4.0 Bcf per day was going to manufacturing to create more jobs in the state he would be happy because right now there is nothing. Something is better than nothing and that is what he is trying to make happen. He said he is confused because this is the administration's language and the administration keeps amending its own language.

CO-CHAIR JOHNSON shared Representative Neuman's frustration.

[2:05:51 PM](#)

REPRESENTATIVE SEATON reiterated his question as to whether it would be only the proportion of a taxpayer's gas that is used for manufacturing, heating, or power generation.

MR. STICKEL responded yes, the department's understanding of this legislation is that the election would apply only to that gas which qualifies under the definition of manufacturing.

[2:06:35 PM](#)

CO-CHAIR JOHNSON asked whether the sponsor is comfortable with adopting the administration's suggested language.

REPRESENTATIVE NEUMAN replied that he comfortable with the conceptual amendment that is being offered by the administration through Mr. Stickel.

CO-CHAIR JOHNSON removed his objection to Amendment 4.

REPRESENTATIVE P. WILSON withdrew Amendment 4. There being no objection, Amendment 4 was no longer before the committee.

[2:07:22 PM](#)

REPRESENTATIVE P. WILSON moved the adoption of Conceptual Amendment 5, written as follows [original punctuation provided]:

Page 3, lines 26 - 27:

Delete "return is due under AS 43.33.030(a) for the calendar year for which the election is made"

Insert:

"first monthly installment payment of estimated tax is due under AS 43.55.020(a) for the calendar year for which the election is made."

CO-CHAIR JOHNSON asked whether Conceptual Amendment 5 addresses Mr. Stickel's concerns.

MR. STICKEL answered yes, this amendment would take care of the issue of a taxpayer potentially overpaying to receive a refund with interest at the end of the year.

There being no objection, Conceptual Amendment 5 was passed. The bill was now before the committee.

2:08:14 PM

REPRESENTATIVE SEATON said he had previously asked for an analysis [which he did not receive] that looks at a 1.5-2.0 Bcf per day in-state manufacturing usage to see what it would look like economically for the state with this later election. He said that would probably preclude exporting the gas through Canada because he does not think the state has enough gas to build both a 1.5 Bcf in-state gasline and a 4 Bcf out-of-state gasline. This would therefore mean that all of the gas produced would be produced under this tax regime, whether it is for heating, electrical generation, or manufacturing; yet, when drilling for the gas the producers would be able to write off the taxes on the oil value 25 percent production tax and the progressivity. This would dig the state into a big hole for its future economics and he does not believe this has been fully considered.

2:10:26 PM

CO-CHAIR JOHNSON said he believes the state will be in bigger trouble than anything this bill would allow if the state's only gasline is a 2.0 Bcf line to Southcentral Alaska with all the spurs because the other line is not practical. At least this way the state will have a manufacturing base and a heating base in Southcentral if the big pipeline is not built. While he shares Representative Seaton's concern about the future economics of the state, he is not comfortable resting the economics totally on the big pipeline. This is a step in generating the jobs for Alaska to become a more self-sufficient state rather than an oil province. If it gets to the point that the big pipeline is out of the question, then the legislators in place at that time can address that. In the meantime, this is a signal that the state is open for business and wants anchor tenants, and for that reason he will be supporting HB 217.

2:12:01 PM

REPRESENTATIVE NEUMAN stated that a 4.5 Bcf per day gasline through Canada would provide only 30-50 long-term legacy jobs. However, an in-state gasline of up to 1.0 Bcf per day would create thousands of long-term legacy jobs. This is an opportunity to have a tremendous amount of jobs and payroll for Alaskans as opposed to a smaller amount that will never replace the oil going down the Trans-Alaska Pipeline System. The state needs to diversify and have hundreds of companies paying corporate taxes rather than just the three companies that are

currently paying 90 percent of the state's bills. Where would the state be if one of these three companies left and the state has not taken the opportunity to use its resources to create jobs for Alaskans?

2:14:05 PM

REPRESENTATIVE SEATON asked whether the sponsor or the Department of Revenue has done the analysis or has the information that he previously requested.

MR. STICKEL responded that the department is in the process of doing some more sophisticated and detailed analysis of gas-to-liquids and has been working with Representative Seaton's office in this regard, but the analysis is not yet completed. The department did look at some hypothetical scenarios as to what the effects would be on an existing producer that starts selling gas for manufacturing that qualified under HB 217. It was found that, generally speaking, at higher oil prices and lower gas prices it would be advantageous to a producer to have that manufacturing gas taxed under the existing statute. At lower oil prices or higher gas prices, it would generally be more advantageous for the producer to pay the 17.7 cents rate. Beyond that information, the department does not have anything to release at this time.

REPRESENTATIVE SEATON said the question he is getting at is the state's participation in a development through the production tax and progressivity offsets and then the switching to the lower tax rate. However, he continued, it does not sound like that analysis is available yet.

2:16:25 PM

CO-CHAIR JOHNSON, in response to Representative Edgmon, stated that the next committee of referral is the House Finance Committee. He added that it is his inclination to move the bill, but he must insist that the sponsor get these questions answered before HB 217 is heard in the House Finance Committee.

2:17:44 PM

REPRESENTATIVE P. WILSON moved to report Version R of HB 217, labeled 26-LS0816\R, Bullock, 2/8/10, as amended, out of committee with individual recommendations and the accompanying fiscal notes.

REPRESENTATIVE SEATON objected.

A roll call vote was taken. Representatives P. Wilson, Olson, Edgmon, Tuck, Neuman, and Johnson voted in favor of HB 217. Representatives Seaton and Kawasaki voted against it. Therefore, CSHB 217(RES) was reported out of the House Resources Standing Committee by a vote of 6-2.

The committee took an at-ease from 2:19 p.m. to 2:25 p.m.

HJR 40-COOK INLET/KACHEMAK BELUGA POPULATION

[2:24:47 PM](#)

CO-CHAIR NEUMAN announced that the next order of business is HOUSE JOINT RESOLUTION NO. 40, Opposing the proposed designation by the National Marine Fisheries Service of 3,000 square miles of upper Cook Inlet, the mid-inlet, all of the inlet's western shores, and Kachemak Bay as critical habitat for beluga whales.

[2:25:23 PM](#)

REPRESENTATIVE CHARISSE MILLETT, Alaska State Legislature, sponsor of HJR 40, stated that the resolution is of utmost importance to the entire state of Alaska because a critical habitat listing in Cook Inlet would impact the port through which 85 percent of the state's goods and products travel. The resolution would tell Washington, D.C., that Alaska thinks a critical habitat listing is ahead of its time. The listing was preceded by the over-harvest of belugas from subsistence hunting. A revised harvest management plan was instituted in 2000 and since then the belugas have increased about 4 percent a year. The National Marine Fisheries Service (NMFS) has proposed a critical habitat of 3,000 square [miles], which would affect every business that comes through the Port of Anchorage, as well as Representative Seaton's district.

REPRESENTATIVE MILLETT pointed out that it is possible to stop a critical habitat designation by putting together a good economic base for why critical habitat should not be administered. In this situation, the National Marine Fisheries Service has grossly understated the economic impacts. For example, the service has stated that the impact would be \$600,000 over the next decade; however, other folks have said \$600,000 is the cost of just one permitting application and the impact statements on that permit. This resolution asks the National Marine Fisheries

Service to slow the process down and take into consideration the economic impacts of a 3,000-square-mile critical habitat area.

2:28:01 PM

CO-CHAIR NEUMAN moved the adoption of the proposed committee substitute (CS) for HJR 40, labeled 26-LS1376\E, Kane, 2/4/10, ("Version E"), as the working document.

REPRESENTATIVE EDGMON objected for discussion purposes.

2:28:43 PM

JEFF TURNER, Staff, Representative Charisse Millett, Alaska State Legislature, explained that the three changes in Version E are based on recommendations received from the Municipality of Anchorage. On page 2 of the original resolution, lines 13, 14, 16, 19, and 27, the word "will" was replaced by the word "may". He related that the municipality is in the process of trying to persuade the National Marine Fisheries Service that the needs of the beluga whales around the city and in Cook Inlet have already been completely addressed; therefore, the municipality wanted to soften the language a little bit. On page 2 of the original resolution, lines 22 and 23 were struck and a different whereas was inserted which expands on the whereas that was replaced by stating that the Port of Anchorage has already fully addressed the conservation needs of Cook Inlet beluga whales. On page 3, lines 7-10, of the original resolution, the whereas was removed that talked about the potential increased cost of treating wastewater that is discharged into Cook Inlet. The city asked this be deleted because it feared this might insinuate that the current wastewater discharge into the inlet could be harming the belugas or needs to be changed. The city steadfastly believes that the current wastewater discharge is not harming the beluga whales or the environment of Cook Inlet.

2:30:23 PM

MR. TURNER, in response to Co-Chair Neuman, said three people are available via teleconference to answer questions regarding the wastewater discharge.

REPRESENTATIVE EDGMON removed his objection to adopting Version E as the working document. There being no further objection, Version E of HJR 40 was before the committee.

REPRESENTATIVE MILLETT stated she does not think the Endangered Species Act (ESA) is a management plan that works for Alaska and managing by the ESA is detrimental to the state. The more vocal Alaska is to the federal government, the better the state controls its destiny. In response to Co-Chair Neuman, she requested that Mr. Arne Fuglvog be able to testify.

[2:32:49 PM](#)

ARNE FUGLVOG, Legislative Assistant to U.S. Senator Lisa Murkowski, pointed out that the public comment period ends March 3, 2010, should the legislature's goal be to submit the resolution by the deadline. He added, however, that the agency typically allows a little bit of leeway for other government bodies. He said this issue goes back to the first petition in 1999 and there have been multiple petitions since then. The listing was made in 2008. Under the Endangered Species Act an agency is required by law to designate and in this case the National Marine Fisheries Service is the agency of jurisdiction. The State of Alaska is working on extensive comments and he thinks it would be helpful to have the resolution go back as a comment from the legislature.

MR. FUGLVOG noted that the Secretary of Commerce has a lot of discretion, unlike a listing decision which is based only on science and in which economics do not matter. For example, a \$100 million economic loss was projected from listing the Steller's sea lion and that did not play a factor in the listing decision. After lawsuits shut down the fisheries, the cost was somewhere between \$50 million and \$100 million.

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MR. FUGLVOG said the National Marine Fisheries Service had three alternatives: 1) list everything in Cook Inlet, 2) list nothing in Cook Inlet, and 3) the alternative that was chosen. He maintained that the data describing some of the areas is weak, especially along the western Cook Inlet shore, and he urged that this go into the comments.

MR. FUGLVOG pointed out that the National Marine Fisheries Service and the U.S. Fish and Wildlife Service treat critical habitat very differently. For example, in a U.S. Fish and Wildlife Service document, out of 1,231 species listed as either threatened or endangered, critical habitat has been designated for only 150. Thus, a little over 10 percent of species have critical habitat designated for them. The U.S. Fish and

Wildlife Service basically stopped the declaration of critical habitat in the mid-1990s because it was expending so much staff and dollars on critical habitat that it could not get to all the litigation and petitions to list species. The exception is the polar bear for which the agency has proposed to list critical habitat.

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MR. FUGLVOG related that the U.S. Fish and Wildlife Service has stated that critical habitat designations usually afford little extra protection to most species, and in some cases it can result in harm to the species. This harm may be due to a negative public sentiment to the designation or inaccuracies in the initial area designated. However, the National Marine Fisheries Service disagrees with that and will be designating by law. He said he thinks that if the National Marine Fisheries Service does not do this, it would get litigated.

MR. FUGLVOG added that with this resolution the legislature has an opportunity to provide meaningful comments for the public comment record. Given all the issues in Alaska related to the Endangered Species Act, he thinks the legislature would be wise to pay attention to this one and provide input. For example, as part of his work for Senator Murkowski he is currently dealing with 10 listings in Alaska.

[2:38:52 PM](#)

REPRESENTATIVE TUCK requested Mr. Fuglvog to provide examples of how critical habitat designation has been harmful to a species.

MR. FUGLVOG related that the U.S. Fish and Wildlife Service believes that in some cases the designation of critical habitat highlights where the species is found and people then know where the animals are located to the animals' detriment. Regarding this critical habitat listing for beluga whales, the National Marine Fisheries Service is saying that the benefits to the species are clear; the U.S. Fish and Wildlife Service takes a different approach.

[2:40:02 PM](#)

REPRESENTATIVE SEATON clarified that the endangered species listing has already taken place, so critical habitat designation would mean that human impacts on the habitat must be looked at. However, even if critical habitat is not designated, all the

government agencies and industries will still have to look at the impacts on the beluga whales themselves. The resolution is not challenging that, it is challenging the designation of the entire [3,000 square mile] unit.

MR. FUGLVOG replied correct. The benefits of the listing to the species, and interactions between activities, will still occur regardless of whether there is critical habitat designation. The agency says the added benefit is the Section 7 consultation which provides that any activity in the critical habitat must consult with the National Marine Fisheries Service. In this consultation the agency evaluates a project and how it might adversely affect both the species and the critical habitat, and a determination is made as to whether there needs to be mitigation of the impacts on both the species and the critical habitat. Therefore, it is an extra layer.

[2:41:32 PM](#)

REPRESENTATIVE SEATON surmised that in regard to an activity taking place where there are whales, the consultation and mitigation will have to take place no matter what. However, if critical habitat is designated for areas like the west side of Cook Inlet where whales have not been seen for 10 years, the consultation would be required because it might influence what has been designated as critical habitat even though there might not be any whales there.

MR. FUGLVOG answered correct.

[2:42:16 PM](#)

RICHARD BERKOWITZ, Pacific Coast Director, Transportation Institute, offered his organization's support of HJR 40. He said the members of his organization are all U.S. Registry with U.S. crews, U.S. built, and U.S. flagged vessels. Members most directly impacted by this critical habitat designation include Horizon Lines and TOTE. With respect to safety, these companies have made up to five transits per week into Cook Inlet in all sorts of weather in every season and have an unblemished record of safety and risk avoidance, as well as no spills and no whale strikes in all that time. They do not pollute the waters with ballast because TOTE has no ballast and Horizon Lines does not discharge ballast in Cook Inlet.

MR. BERKOWITZ said one of the key issues is that because of the numerous trips each week that these companies are able to

provide into Anchorage, which in turn supplies much of the state, the whole system is just-in-time. Because of this frequent service, the cargo can be moved straight out so there is no warehousing. This saves Alaska's consumers over \$70 million in annual warehousing distribution costs and provides Alaskans with fresh vegetables and milk. The potential changes that could occur as a result of this critical habitat designation could seriously impact that just-in-time cargo distribution. He urged the resolution be moved in time to meet the March 3, 2010, public comment deadline.

[2:45:15 PM](#)

REPRESENTATIVE TUCK asked how a whale strike is determined, given the large size of the vessels.

MR. BERKOWITZ responded that "to their knowledge, there has not been a whale strike." He allowed that there have been strikes in other ports in other areas and when this happened the whale ended up on the bulbous bow of the vessel and could be seen.

REPRESENTATIVE TUCK requested Mr. Berkowitz to elaborate on how critical habitat designation would affect TOTE and Horizon Lines.

MR. BERKOWITZ replied the key issue is that Cook Inlet has lots of ice and up to 22-foot tides. Missing the tide can mean a 12-hour delay getting into port and the just-in-time system does not afford this kind of variability. If a vessel was asked to go slow or to wait it would impact the just-in-time cargo and also the safety of the vessel, particularly in ice.

[2:47:05 PM](#)

REPRESENTATIVE TUCK asked whether critical habitat designation would require the vessels to slow down.

MR. BERKOWITZ answered that that is unknown, but in the right whale situation on the East Coast ships have been required to slow significantly during certain times of the year and to avoid certain areas. He added that there are also significant problems with silt in Cook Inlet and the last thing the Transportation Institute wants to see is a ban on dredging which could affect vessel safety. It is known what has happened elsewhere and his organization does not want to see it replicated in Cook Inlet.

2:47:57 PM

JOHN MCCLELLAN, P.E., Tyonek Native Association, testified that his association supports HJR 40 because it believes that designating all of this area would raise a barrier to the \$18 billion-worth of new development that is seen for west Cook Inlet on or near Tyonek's land. Tyonek does not believe that all habitat is critical habitat and this is regulatory over-reach.

MR. MCCLELLAN said Tyonek believes that the cause for the beluga whale not restoring its population is the lack of king salmon. The villagers who have lived with the beluga whale and the salmon for years know that the beluga whale is dependent upon king salmon during the critical nursing period and the belugas will not come back until the king salmon come back. He cited recent examples of similar events. In San Francisco, CA, the sea lions disappeared from Pier 39 and scientists there said the sea lions left because their food source left. In Puget Sound a researcher has tied the killer whale population to the salmon population. He related that when Tyonek asked the National Marine Fisheries Service if it had correlated the drop of Cook Inlet's belugas with the drop of king salmon, the service said no, it did not have the data available.

2:51:51 PM

JASON BRUNE, Executive Director, Resource Development Council (RDC), supported HJR 40. He spoke from the following written statement [original punctuation provided]:

RDC members include all of the major, and many of the minor, parties who will be adversely impacted by the proposed designation of over 3,000 square miles of critical habitat in Cook Inlet. From local communities, to oil and gas, mining, tourism, and fisheries members, all stand to be negatively affected by this proposal. Meanwhile, this designation will result in no added benefit to the belugas.

RDC members who live, recreate, and work in and around Cook Inlet are committed to the recovery of the beluga whale. It is important to remember that NMFS' biologists have acknowledged the sole cause for the population decline of Cook Inlet beluga whales was the subsistence harvest that transpired in the 1990s. The multitude of activities in Cook Inlet that will

absolutely be impacted by this critical habitat proposal were not the cause of the decline, nor are they an ongoing threat to the whale's recovery.

Since statehood, economic and community development activities have occurred in Cook Inlet. Indeed, these activities have long co-existed with the belugas. Responsible community and economic development have in no way adversely impacted these whales or impeded their recovery. Unfortunately, this designation, if finalized will lead to additional requirements, costly delays, and lengthy 3rd party litigation. There is no other way to put it.

The ESA requires economic effects to be taken into account when designating critical habitat. In fact, areas may be excluded from critical habitat if it is determined that the benefit of such exclusion outweighs the benefit of specifying such areas as critical habitat.

The economic analysis that has been completed as part of this proposal is grossly inadequate. In fact, only direct consultation costs are acknowledged as "costs" in this analysis. Nothing further is considered. The agency's estimates are less than \$600,000 over the next decade. Frankly, this is naïve and way understated.

Because of this, RDC has hired a contractor, Resource Dimensions, to undertake an independent economic analysis to attempt to more accurately identify the costs of this proposal. These economists have been conducting in person and telephone interviews with many of the potentially affected entities. We are working very closely with the State of Alaska Department of Fish and Game as well as the Office of Economic Development on the development of this analysis and we will be providing the results of this analysis to the agency. We hope NMFS will use these results as a boilerplate to conduct a more robust economic analysis and to that end, I wholeheartedly endorse the second action item of this resolution which calls for a more robust economic analysis.

In conclusion, the benefits of designating critical habitat in most, if not all of the areas that have

been proposed is outweighed by the economic impacts it will have. In addition, critical habitat will provide no added benefit to the Cook Inlet belugas and therefore, I enthusiastically endorse HJR40.

[2:55:41 PM](#)

BRUCE WEBB said he is the manager of land and regulatory affairs for Aurora Gas, a small independent gas exploration and production company in Cook Inlet. Aurora Gas supplies about six percent of the gas to the Cook Inlet market. He recently attended the North American Petroleum Expo in Houston, Texas, where he was shocked to learn of the stigma that has happened from this proposed critical habitat designation; for example, some people at the expo thought drilling could no longer occur in the Cook Inlet because of the beluga whale. He predicted that if the habitat designation goes through it will open the floodgates to frivolous litigation that will delay and possibly cancel oil and gas exploration in the Cook Inlet. He therefore supports HJR 40 because critical habitat designation would negatively impact oil and gas exploration and development.

[2:58:12 PM](#)

STACY SCHUBERT, Intergovernmental Affairs Director, Mayor's Office, Municipality of Anchorage, supported the proposed committee substitute for HJR 40 on behalf of Mayor Dan Sullivan. She said this is a significant issue to the Anchorage community and its partners across the state. She testified from the following written statement [original punctuation provided]:

The Municipality of Anchorage (MOA) is committed to ensuring the long-term health and productivity of the Cook Inlet and to the conservation of its beluga population. Cook Inlet supports significant oil and gas production, fishing, mining and a year-round tourism industry to the benefit of all Alaskans. The Port of Anchorage is the essential conduit through which passes an astounding 85% of all goods entering the state, and 26% of the tonnage of U.S. international air freight moves through the city via Ted Stevens Anchorage International Airport.

Anchorage's strategic location continues to be vitally important to our nation's overall defense strategy. We are an excellent staging point for an array of military operations and equipment that is deployed -

and redeployed - through our Port in support of our national strategic interests.

The proposed critical habitat designation adds nominal value to the protection of the Cook Inlet beluga. It is fundamentally vague, and because the Endangered Species Act already applies, the MOA is addressing the needs of the beluga responsibly, directly, and with best available science. The projections of economic costs associated with the proposed designation do not pass the red face test; the potential for new regulations, delayed development and increased costs will most certainly total more than the \$575,000 that NMFS included along with its proposal.

MS. SCHUBERT stated that for the aforementioned reasons the Municipality of Anchorage opposes the proposed critical habitat designation. She urged expeditious passage of the resolution so it can be included in the NMFS's public record.

[3:00:32 PM](#)

GRAHAM SMITH, Communications and Membership Director, Alaska Support Industry Alliance, supported HJR 40 and urged it be passed in time to meet the public record comment deadline. He testified from the following written statement [original punctuation provided]:

The Alliance is a trade organization representing nearly 500 businesses, organizations and individuals that provide goods and services to Alaska's oil, gas and mining industries and more than 40,000 jobs for Alaskan workers. Our livelihoods depend on a healthy Alaska oil & gas industry and investment climate.

As a result of depressed business activity in Alaska's oil patch, hundreds of Alaskan oil field workers and professionals have been laid off in recent months. New exploration and development efforts are necessary to sustain Alaska's economy and the livelihoods of our members. A critical habitat designation would have a crippling impact on the already-struggling oil and gas operations in Cook Inlet. It would risk billions of dollars in future projects and could ultimately cost Southcentral Alaska residents and companies hundreds of millions of dollars to comply with new regulations and standards.

As you have already heard, National Marine Fisheries Service biologists have acknowledged the sole cause for the population decline of Cook Inlet beluga whales was the subsistence harvest that transpired in the 1990s.

Oil and gas operations in Cook Inlet have gone on for decades without contributing to the population decline or impeding the recovery of the Beluga whales, and we believe that further exploration and development of Cook Inlet resources can occur without adversely affecting the Beluga population.

3:02:52 PM

CO-CHAIR NEUMAN closed public testimony after ascertaining no one else was available to testify.

REPRESENTATIVE SEATON stated that he will be writing and submitting personal testimony on this issue as he believes designation of the full Cook Inlet is way too broad. He is not opposed to designating critical habitat, but the current proposal of the entire range of the animal is too much. He offered his support for HJR 40.

REPRESENTATIVE TUCK related that for years he has heard the beluga decline is directly tied to the king salmon runs, as was stated by the Tyonek Native Association. Therefore it is hard to say that industry, shipping, or drilling has had anything to do with the decline.

3:04:03 PM

CO-CHAIR JOHNSON moved to report the proposed committee substitute for HJR 40, labeled 26-LS1376\E, Kane, 2/4/10, out of committee with individual recommendations and the accompanying zero fiscal note. There being no objection, CSHJR 40(RES) was reported from the House Resources Standing Committee.

ADJOURNMENT

There being no further business before the committee, the House Resources Standing Committee meeting was adjourned at 3:05 p.m.