

**ALASKA STATE LEGISLATURE**  
**SENATE SPECIAL COMMITTEE ON ENERGY**

February 12, 2009  
11:11 a.m.

**MEMBERS PRESENT**

Senator Lesil McGuire, Chair  
Senator Bert Stedman  
Senator Bill Wielechowski

**MEMBERS ABSENT**

Senator Lyman Hoffman  
Senator Albert Kookesh

**OTHER LEGISLATORS PRESENT**

Representative Pete Petersen

**COMMITTEE CALENDAR**

SENATE BILL NO. 31

"An Act relating to a geothermal electricity production tax credit under the Alaska Net Income Tax Act."

HEARD AND HELD

SENATE BILL NO. 54

"An Act making sales of and offers to sell certain energy resources by a refiner at prices that are exorbitant or excessive an unlawful act or practice under the Alaska Unfair Trade Practices and Consumer Protection Act."

HEARD AND HELD

**PREVIOUS COMMITTEE ACTION**

BILL: SB 31

SHORT TITLE: GEOTHERMAL ELEC. PROD. TAX CREDIT

SPONSOR(S): SENATOR(S) MCGUIRE

01/21/09	(S)	PREFILE RELEASED 1/9/09
01/21/09	(S)	READ THE FIRST TIME - REFERRALS
01/21/09	(S)	ENE, RES, FIN
02/12/09	(S)	ENE AT 11:00 AM BUTROVICH 205

BILL: SB 54

SHORT TITLE: PRICE GOUGING INVOLVING ENERGY RESOURCES

SPONSOR(S): SENATOR(S) WIELECHOWSKI, ELLIS, FRENCH

01/21/09 (S) PREFILE RELEASED 1/16/09  
01/21/09 (S) READ THE FIRST TIME - REFERRALS  
01/21/09 (S) ENE, RES, JUD  
02/12/09 (S) ENE AT 11:00 AM BUTROVICH 205

**WITNESS REGISTER**

TREVOR FULTON, Aide  
to Senator McGuire  
Alaska State Legislature  
**POSITION STATEMENT:** Presented changes in SB 31.

DAN STICKEL, Economist  
Department of Revenue (DOR)  
Juneau AK  
**POSITION STATEMENT:** Answered questions about SB 31.

JOHANNA BALES, Deputy Director  
Tax Division  
Department of Revenue  
Anchorage AK  
**POSITION STATEMENT:** Answered questions about SB 31.

NICK GOODMAN, CEO  
TDX Power  
Anchorage AK  
**POSITION STATEMENT:** Spoke in support of SB 31.

PAUL THOMPSON, Director  
Policy and Business Development  
Ormat Technologies  
Reno NV  
**POSITION STATEMENT:** Spoke in support of SB 31.

CLAY KOPLIN  
Cordova Electric Co-op and the Alaska Power Association  
Cordova AK  
**POSITION STATEMENT:** Spoke in support of SB 31.

HAP SYMMONDS  
Ocean Beauty Seafoods  
Cordova AK  
**POSITION STATEMENT:** Spoke in support of SB 31.

TOM LAKOSH

Anchorage AK

**POSITION STATEMENT:** Spoke in support of SB 31 and SB 54.

SUE ELY

Alaska Conservation Alliance

Juneau AK

**POSITION STATEMENT:** Spoke in support of SB 31.

KIP KNUDSON, Manager

External Affairs

Tesoro Alaska

Anchorage AK

**POSITION STATEMENT:** Spoke in opposition to SB 54.

MIKE MCCARTHY

Homer AK

**POSITION STATEMENT:** Spoke in support of SB 54.

PETE ROBERTS

Homer AK

**POSITION STATEMENT:** Spoke in support of SB 54.

JUSTIN POWELL

Fairbanks AK

**POSITION STATEMENT:** Spoke in support of SB 54.

MERRICK PIERCE

Fairbanks AK

**POSITION STATEMENT:** Spoke in support of SB 54.

CRAIG MCCONNELL

Northwest Arctic Borough School District

Kotzebue AK

**POSITION STATEMENT:** Spoke in support of SB 54.

MARGARET HANSEN, Treasurer

Northwest Arctic Borough School District

Kotzebue AK

**POSITION STATEMENT:** Spoke in support of SB 54.

JEFF COOK, Director

External Affairs

Flint Hills Resources Alaska

North Pole AK

**POSITION STATEMENT:** Spoke in opposition to SB 54.

ED SNIFFIN, Assistant Attorney General

Department of Law  
Anchorage AK

**POSITION STATEMENT:** Discussed a report he did on price gouging by gasoline refiners and retailers.

**ACTION NARRATIVE**

[11:11:49 AM](#)

**CHAIR LESIL MCGUIRE** called the Senate Special Committee on Energy meeting to order at 11:11 a.m. Present at the call to order were Senators Wielechowski, Stedman, and McGuire.

[11:12:16 AM](#)

**SB 31-GEOTHERMAL ELEC. PROD. TAX CREDIT**

CHAIR MCGUIRE announced the consideration of SB 31. She said it is her bill, and she has a committee substitute (CS) with significant changes. It provides for a production tax credit to incentivize renewable energy in Alaska. The original bill incentivized geothermal energy investment by allowing for a tax credit of \$0.35 per kilowatt hour. The bill now provides the credit for other forms of alternative energy. Many projects have been discussed. Funding by the Alaska Energy Authority is a direct pay-out of money. She has talked with companies, municipal utilities, and co-ops that may be looking at wind, tidal, and geothermal projects. The idea is to attract new investment into these sustainable energy projects that may also create new jobs. She hopes it will push existing projects that might not be economic yet.

CHAIR MCGUIRE said that the bill gives a tax credit to profit-making companies, and municipal utilities would get an earned-tax credit that can be traded on the market. "You might end up with a very unique circumstance where you have alternative energy tax credits being traded on the market, and, for example, a fossil fuel company buying them." That is good for Alaskans and the environment. The bill needs some work. There are some creative financing mechanisms in it, but it is patterned after the film credit incentive bill that passed last year.

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SENATOR WIELECHOWSKI moved to adopt the CS to SB 31, labeled 26-LS0217\C, as a working document. Hearing no objection, Version C was before the committee.

TREVOR FULTON, Staff to Senator McGuire, Alaska State Legislature, said the CS has four main changes from the original bill. The scope of SB 31 is expanded to include other types of alternative energies besides geothermal: solar, biomass, wind, tidal, river, and wave. The tax credit is now transferable so that public utilities can benefit. The original bill was misdrafted, so the third change corrects the amount of credit to \$0.35 cents. It also adds a January 1 effective date to comport with the start date of the tax year.

SENATOR WIELECHOWSKI asked about the fiscal note.

MR. FULTON said the Department of Revenue will address that. He has seen two fiscal notes so far, but neither one really reflects the CS.

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DAN STICKEL, Economist, Department of Revenue (DOR), Juneau, said the CS fiscal note will be indeterminate because no one can know what projects will apply for this credit. The 14-megawatt Lake Dorothy hydro project, for example, would qualify for about \$260,000 per year. It has a \$64 million capital cost. The Department of Energy reports that Alaska has 1.3 billion kilowatt hours of alternative energy generated annually. If it is increased by 10 percent, revenue to the state would be reduced by about \$455,000 per year for four years. But he doesn't know what projects will come on line and if the credit will be used.

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MR. STICKEL said the DOR will have the expense of reviewing, approving, and tracking these credits. "I believe we are requesting either an additional corporate income tax auditor or a partial position for that work in the fiscal note."

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SENATOR STEDMAN asked what expectations the department has.

JOHANNA BALES, Deputy Director, Tax Division, DOR, Anchorage, said there is a federal corporate income tax credit that deals with this type of energy. Alaska adopts that federal credit, so Alaska corporate income taxpayers would get some benefit from the federal credit, but only corporations. The intent is to help public utilities with a transferable credit. It may entice businesses who wouldn't normally get that income tax credit.

MR. STICKEL added that they hadn't looked at the economics of projects "and what this might incent." The press has reported on the Lake Dorothy hydro project, a wind farm in Nome, a wind farm on Fire Island, and a geothermal project at Mr. Spurr. "But we haven't looked at the economics of any of those."

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NICK GOODMAN, CEO, TDX Power, Anchorage, said TDX Power owns and operates regulated utilities and develops power projects around Alaska. It does a number of renewable energy projects, including wind and geothermal. It is looking at hydro projects - from 400 kilowatts to 330 megawatts. "We are extremely supportive of this legislation." It is a wonderful way to attract investments. His company has experience with the federal PTC [production tax credit] on some geothermal projects in the Lower 48. It's safe to say that the federal PTC is the single most significant component to the development of the majority of wind farms in the Lower 48. It has demonstrated itself as a vehicle for attracting investment and getting projects in the ground. This bill would have great benefit to the state of Alaska.

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SENATOR STEDMAN said the credit will be available for the first of four years after the power plant is placed in service. He asked if there is enough of a tax shield on the depreciating out of a hydro dam with its high capital costs. Would it dilute the tax credit?

MR. GOODMAN said hydro would benefit probably the least from this, but it would still be of some benefit. The depreciation depends a lot on the size of the project. Smaller projects depreciate much more quickly.

SENATOR STEDMAN asked if the depreciation life is 50 or 7 years.

MS. BALES said someone could generate a credit for the first of four years and use that credit during the four years. If it wasn't all used it could be sold to someone else who could use the credit until it was exhausted. She did recommend to the sponsor to allow the credit to be generated for four years and then allow its use by the producer until it was exhausted. But expenses are more upfront than on the back end.

CHAIR MCGUIRE said they would continue to work on that.

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PAUL THOMPSON, Director, Policy and Business Development, Ormat Technologies, Reno, NV, expressed support for SB 31. Ormat is very encouraged to see the legislative commitment to develop alternative energy resources in Alaska. Ormat first did business in Alaska in 1976 when it sold remote power units to the Alyeska pipeline company. His chairperson has always pursued the dream of developing a geothermal project in Alaska. Ormat is publicly traded on the NYSE and has over 1,000 employees worldwide. It currently owns and operates 350 megawatts of geothermal power in the United States and is responsible for one gigawatt of power generation around the world. Ormat is evaluating energy opportunities in Alaska and looks forward to trying to develop its recently acquired 36,000 acres at Mt. Spurr. This type of bill will help get meaningful renewable projects in Alaska. Ormat hasn't run all of its financial models, but 0.35 cents won't greatly incentivize large-scale geothermal projects in a state where development costs are high. The federal PTC is 2 cents, and with double the development costs, "we would push for a PTC in the 3.5 to 4.5-cent-per kilowatt hour range."

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CLAY KOPLIN, Cordova Electric Co-op and the Alaska Power Association, said SB 31 is an exciting bill. Cordova Electric depreciates its hydro projects over 50 years. A challenged economy is a good time to invest in energy infrastructure, because there is a good workforce and lower material prices. It is a good time for a bill like this to encourage private industry investment in alternate energy production that provides benefits particularly in rural Alaska. Most of Alaska's energy needs are met by nonprofits and municipalities, so the transferable tax credit is very attractive. Cordova Electric is partnering with a Native corporation in an alternative energy project. They were trying to find ways to tie the federal tax incentives to their tax liability because the projects are on their lands. This bill will encourage those partnerships between electric utilities and the Native corporations. He is pleased that the CS broadens the scope. Different areas of the state will use different technologies. He said that hydro isn't generally considered, at the federal level, renewable or alternative, so he was glad to see it included in SB 31.

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MR. KOPLIN said that Cordova Electric took the \$40,000 of revenue from last year and retrofitted some street lights with LED fixtures, which use one half to one fourth of the energy, greatly reducing winter diesel use. He asked that the credit be claimed for the first 48 months of operation rather than four

years. So if a project went into service on the tenth month of a fiscal year, it could get the full four years of tax credits instead of just three years and two months. He encouraged that it apply to other taxes rather than just state income taxes. It could also apply to existing alternative energy projects.

CHAIR MCGUIRE noted his suggestions.

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HAP SYMMONDS, Ocean Beauty Seafoods, Cordova, said he supports SB 31. Alternative energy is important for seafood processing plants that are located in rural communities and have the prospects of hydro, wind, and tidal energy. It is a great bill for outlying communities with seafood plants. He supports a credit of 3.5 to 4.0 cents rather than 0.35 cents. It would provide even more incentive to get off of diesel.

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TOM LAKOSH, Anchorage, said the bill is a great idea, but it needs work. He concurs with the suggested amendments, including raising the subsidy to match at least the 1.9-cent federal subsidy. He suggested changing line 14 by adding "or btu equivalent of alternative energy ... consumed or sold" after "kilowatt hour". This would encourage production of biofuels for use other than electricity generation. Gas and diesel are consumed for heat. On page 2, line 17, "hydrokinetic" is redundant to "tidal and wave" energy. The bill should provide a definition of hydrokinetic that includes things like ocean currents because the modifying language may be overly restrictive. There are problems with biomass. Alaska doesn't want pollution from biomass energy. "We need a definition for biomass that has some sort of pollution standard."

MR. LAKOSH said he has suggested using a particular biomass generator that produces wood pellets and uses sewage and liquid biomass to produce ethanol as back up to wind in rural communities. Pellets can be used in stoves when not producing electricity, and the alcohol can be used for heat or gasoline. Alaska could subsidize the production of E10 in local communities for alcohol stoves or clean wood pellet stoves. There should be a number of alternatives that should be subsidized if they are clean.

CHAIR MCGUIRE said those are excellent points.

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SUE ELY, Alaska Conservation Alliance, Juneau, said her group represents over 38,000 Alaskans. Alaska is at an energy crossroads, and volatile fuels prices are negatively impacting its citizens. Many electrical generation facilities are at or near the end of their life spans and will need to be replaced. Alaska should take full advantage of its vast clean energy resources. The governor wants to produce 50 percent of Alaska's electricity from renewable resources. An alternative tax credit could help get there. Geothermal, reasonably-sized hydro, wind, solar, biomass, hydrokinetic, and tidal can all provide stable-priced power. It can fill batteries in electric vehicles and warm and illuminate greenhouses to secure Alaska's food source. Germany has already used a clean energy incentive to build an \$8.7 billion renewable energy industry. It created 170,000 jobs. The bill is a strong first step in an energy plan for Alaska.

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CHAIR MCGUIRE set SB 31 aside for continued work.

**SB 54-PRICE GOUGING INVOLVING ENERGY RESOURCES**

[11:47:20 AM](#)

CHAIR MCGUIRE announced the consideration of SB 54.

SENATOR WIELECHOWSKI is the sponsor of SB 54, which is a response to the outcry against high gasoline prices in Alaska. Alaskans have been paying the highest prices in the United States. The bill makes it an unfair trade practice for refiners to charge exorbitant costs to Alaskans. The bill is amending the Unfair Trade Practices Act to add number 56. There are 55 consumer protection items already in statute. Some people are critical of this, but we have always stepped in to help consumers when such issues arise.

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SENATOR WIELECHOWSKI said Alaska historically pays about 10 to 20 cents above the national average. At one time Alaska was actually lower than the national average. Recently Alaskans have spent from \$0.70 to \$1.00 more than average rates. He and Senator Davis asked the attorney general to investigate the matter. The conclusion was that high prices are the result of an oligopoly, which is a small market and not a free one. Essentially there is one refiner, Tesoro, that controls the vast amount of refining capacity in Alaska. So Tesoro can set any price. Tesoro is a good business trying to make as much money as it can, but Alaskans are paying exorbitant prices because of it.

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SENATOR WIELECHOWSKI referred to a chart that indicated a gap between the retail margin and the refiner margin. Refiners have always made a healthy profit, but when oil prices spiked, the margins spiked, and then when oil prices went down, the margin didn't go down. They kept charging the extremely high prices. It's not like labor or transportation costs have increased. Oil and gas is produced here, so there are no transportation costs to add on. It's refined right here in the state. Alaska's gas taxes are the lowest in the nation. Alaskans are rightfully angry. It doesn't make any sense.

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SENATOR WIELECHOWSKI said there are people who don't want to regulate the free market, but "we don't have a free market here." Government has always intervened with energy rates so that consumers can't be gouged. It's exactly why we have the RCA [Regulatory Commission of Alaska]. There is this government system in place to try to regulate prices. The TransAlaska Pipeline and the upcoming natural gas line are regulated by government. He is not asking for RCA oversight. "All we're saying is you can charge what you want to charge, but if you charge exorbitant or excess prices when compared to the charges in the Lower 48.... We're even giving them the benefit of the doubt by tracking it to West Coast, Seattle-based, refiner prices, which are a little bit higher than national prices." The bill is reasonable and will help consumers from being gouged. Alaskans are tired of bailouts - sick and tired of subsidizing large businesses so that large corporations can pay multi-million dollar bonuses to their executives. This is one way to stand up for the consumers in Alaska.

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The committee took a brief at-ease.

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KIP KNUDSON, Manager, External Affairs, Tesoro Alaska, Anchorage, said Tesoro does not own oil or gas; it only refines and markets them. Its plant was built in Nikiski in 1969. It is an exciting year for his employees because the plant was built 40 years ago. The refinery was initially built to process Cook Inlet crude. Production peaked in 1970 at 225,000 barrels. "Today we refine every drop out of the inlet, which is roughly 15,000 barrels." So Tesoro has to buy 50 percent of its crude from the North Slope. "We are having to import roughly 25 percent of our crude slate." It's sad but true. Crude is coming from Norway, Nigeria, and Indonesia. Tesoro is on tide water and

must haul the crude in and products out. Tesoro supplies Southcentral primarily through a clean-products line, which is a 10-inch pipeline to Anchorage. There is a distribution facility at the Port of Anchorage. Tesoro has downstream retail sites, with 31 company-owned stores and 56 independent businesses.

MR. KNUDSON said Tesoro makes commodities: jet fuel, gasoline, propane, and asphalt. Prices are determined by the fundamentals of the commodity market: supply and demand. Commodity markets don't care how much it costs to produce it in the short term. In the long term, it is naturally regulating. That has been effective, but it is not an easy business to be in.

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MR. KNUDSON said fishermen don't set fish prices; it's the buyer at the dock who knows the demand for it. It is the same with oil. When oil was \$140 [per barrel], nobody asked how much it cost to produce. Now that it is \$40, it is the same. No one cares how much it costs to produce it. Refining has gotten exceptionally complicated and "this is just a few areas where the government has gotten involved in the business, in areas that we've had to make investments in order to stay in the refining business. And we have a couple of big ones coming down the pike. In order to stay in the gasoline business, we're going to have to make a fairly significant investment in the plant to remove benzene." Greenhouse gases will be regulated ultimately. He showed a graph of "the oil and gas sector spending on environmental projects." The big chunk in the middle is the refining sector.

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MR. KNUDSON said independent refining is all Tesoro does. It is better at it than the integrated majors. It is a competitive alternative. "We don't make profit from high prices; we make profit or a loss in the difference between the costs of the inputs and the price we can finally charge to our customers." So Tesoro was actually losing money when gas prices were high. It is irritating, and it is difficult to understand.

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MR. KNUDSON said a refinery is fairly static; you turn it on and it runs at a certain rate. Tesoro has a very hard time modulating the amount of production. "You can only turn a refinery down so far; it is a chemical process." There is a limited ability to change the mixture of products that come out. If Tesoro makes 50,000 barrels of product every day, it must sell that much every day. It doesn't matter what the demand is.

Tesoro does not store it. It must sell it. "We're penalized heavily by the financial markets if we end up with too much product ... in our tanks." Tesoro has to move the product every day and uses a multitude of sales channels.

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MR. KNUDSON said Tesoro is in the retail business. It knows it can sell a certain amount to its own stores every day. Tesoro also works with branded distributors that run their own businesses and set their own prices. Tesoro also sells to mom and pop gas stations in convenience stores. Some sales are on contract and some are open. There are rack sales that are public, but the rest of the sales are proprietary. Tesoro also loads a barge with 30,000 barrels of product that goes to coastal communities. Refiners will do exchanges. Five percent of the gas stations in Alaska are owned by Tesoro, and another ten percent are branded. The rest are somebody else's stores. Alaska's market has low demand for transportation fuels, and it has significant seasonal highs and lows.

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MR. KNUDSON compared the gallons sold per retail site in Alaska with Washington and California. A retailer must pass along more costs for each gallon sold. "Jet fuel is king in the state of Alaska." He showed the amount of jet fuel sold in Anchorage and Fairbanks. That is the reason there are refiners in Alaska. About one third of Tesoro's product has no market in Alaska, like asphalt and bunker fuel. It must be shipped south, and it sells it for less than the cost of crude. "So one third of our product is an instant loser."

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CHAIR MCGUIRE asked if there are ongoing efforts to identify Alaskan markets for that product.

MR. KNUDSON said the traditional way a refiner would handle those items is to add an expensive processer to the refinery to make gasoline, diesel, and jet fuel. But there isn't enough demand in Alaska for those.

CHAIR MCGUIRE asked about the innovation in his company to develop more in Alaska.

MR. KNUDSON said the market has determined it wouldn't be worth making a big investment. These are big units that would create a tremendous excess of product that would have no demand. Some refiners in Alaska have just gotten out of the gasoline and

diesel business because investments could not be amortized over the return on the sales.

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MR. KNUDSON said price is determined by the last barrel supplied into the market. He is not aware that transportation fuels are imported into Southcentral. That would mean that the last barrel comes from local refiners, and that price is lower than an imported barrel of product. "We compete with outside refiners. We compete with shipping up a barrel of gasoline to the state of Alaska from a Washington refinery. Ultimately we must have priced it lower than that imported barrel because those imported barrels would come in otherwise and drive the price to that imported price." The West Coast market has gotten significantly more volatile. For a person in the fuel business "you can lose your shirt one day and make money the next and never know if it's all going to balance out in the end."

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MR. KNUTSEN showed a comparison of prices in Seattle, Anchorage, the P & W spot market, and crude. The chart has a pattern. Alaska separates from the western markets occasionally but then meets back up again. After December, the West Coast markets are coming back to meet Alaska again. In a month, the lines will be closer. When "that band" on the chart is narrow, refiners are losing money on the West Coast. Alaska is not losing money, so that is an advantage to Alaska refiners. He said Alaska is in the range of historical price patterns, which is represented by a percentage spread between crude and Anchorage street prices.

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MR. KNUDSON said refining in Alaska is a success story. "We've underpinned the air cargo industry and helped them thrive." Tesoro has provided jobs and tax revenues. Oregon and Arizona have no refineries. Alaska has four. Washington has five. More jet fuel is sold in Alaska than in Washington and Oregon combined. Alaska refiners sell through many channels and compete daily with import barrels. Government price caps will ultimately distort all of the unique aspects of the Alaska market. The proposed legislation is not anti-gouging, but it is a price cap. Government control in a functioning market will be bad for consumers and refiners. SB 54 will damage Tesoro's ability to do business in Alaska and to make future investments. It will damage value-added industries in the whole state.

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MIKE MCCARTHY, Homer, said he testified in 2008 and wrote to assistant attorney general Ed Sniffen and got no response. He has been a detective on the Portland police bureau and he worked on organized crime detail in the FBI office. He found it most baffling that Representative Ramras claimed that the [indecipherable] refused to provide the actual cost to produce a gallon of gasoline, claiming that it was proprietary. If this is true, the attorney general needs to open the same type of investigation that revealed the truth in the Enron fraud that victimized millions of people. SB 54 is the exact strategy the state needs to pursue. The November 20, 2008, Department of Law press release states that Governor Palin directed it to investigate gas prices. The result had 8 bullet points, and he took serious exception to bullet point 5, which reads: "The price of gasoline in the Lower 48 is not a good indicator of what prices should be in Alaska. The competitive forces that operate to control gasoline prices in the Lower 48 are completely different from Alaska. The dynamics of supply, demand, and competition are unique in Alaska." If this is a fact, how does a person reconcile the existence of the Henry Hub index pricing for natural gas? Enstar pushes that index as gospel. "You can't have it both ways." SB 54 addresses the constitutional responsibility of the state to ensure that natural resources are used to the maximum benefit of Alaskans, not to the benefit of giant, multinational corporations.

MR. MCCARTHY said that former attorney general Talis Colberg was correct when he said that an investigation on price fixing or other consumer fraud would be time consuming, complicated, and expensive. It was proven in the three-year study done by the DOL in 2002. The salient feature of SB 54 is that no complicated investigation is required, but only that the average wholesale price of a comparable energy resource charged by refineries in Washington cannot be exceeded by more than 10 percent. This is most logical. It is the best solution to this Alaska crisis. The Homer newspaper has had numerous articles about people who have to choose between food, heat, and medication.

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MR. MCCARTHY said his daughter in Portland told him that diesel is \$2.49 and regular is \$1.99 [per gallon], and in Homer diesel is \$3.67 and regular is \$2.73.

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PETE ROBERTS, Homer, seconded Mr. McCarthy's testimony. Crude oil has had about a 5 percent surplus on the market until the last couple of years. That tends to keep prices down somewhat.

As soon as the reserve came down to 2 percent, there was considerable speculation, driving prices up to as high as about \$146 per barrel. That tripped up the "whole financial deal, and what we see here is that we need to have free enterprise and free markets, but there do need to be regulations and an even playing field." The banks and the oil companies don't have that. Two weeks ago his son bought gas for \$1.55 per gallon in Santa Cruz, California. It is \$2.80 here, and crude oil futures were \$38.40 - that's less than a quarter of the high prices, "and we need to regulate the companies." Their books should be open. He said they have a right to get a 20 percent return, but "I'll bet you one hundred bucks that in the last six months ... they are in the hundred percent and maybe considerably more." Big companies do very well for themselves, but the legislators should be protecting the citizens of Alaska. One of government's prime duties is reasonable regulations. "I'm a Republican, and that has been given short shrift in recent years, but that's what we need to do."

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JUSTIN POWELL, Fairbanks, said it was unfair for Mr. Knudson to compare fish prices to gasoline prices. Tesoro controls 85 percent of the gasoline market and 100 percent of the diesel market so prices aren't influenced by demand. It produces enough to meet the demand, and it has a vested interest in preventing a surplus situation. If demand did influence prices, prices would drop in the winter because gasoline demand drops 25 percent. In reality, it is the opposite with winter prices spiking. He imagines that this committee has read the House Judiciary Committee's report on gas prices. There are several omissions from the report that dramatically affect the conclusion of the committee chair. The burden of high prices in Alaska is real. The prices over the past year are unjustified. Gasoline, diesel, and heating oil are not luxury items that households can go without. Energy in the winter is a life and death matter.

MR. POWELL said high energy prices have a ripple effect throughout the economy. The high prices have been highly visible and contentious, but there are also the higher freight costs for food, clothing, and retail products. "We pay more to heat our homes, and then, in turn, have to pay more for goods and services as businesses are forced to pass on their additional energy costs." Quantitative information was lacking from the committee report. Annual gasoline consumption in Alaska is 285 million gallons per year, and so consumers are paying at least \$230 million per year more for gasoline alone. This money leaves the state and has no direct or indirect benefit. The report also

said that Ft. Greely, Eielson, and Ft. Wainwright could be shut down. The supplier for all military installations in Alaska is the Petro Star refinery, which is exempt under this bill. In conclusion, lower gas prices will have a positive impact on Alaska's economy. The benefits far outweigh the potential impacts to the airline industry. Fishing, tourism, and ground transportation are no less important than air transportation. The \$230 million in extra gas costs could be used in the state rather than go to the large airlines.

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TOM LAKOSH, Anchorage, said [the bill] is a good idea but it needs work. "I think what you're trying to do is gain parity with the Washington prices." It might be better to restrict the profit margins by establishing a timeframe for the term "average" on page 2, line 5. Instead of adding 10 percent of that price, add a phrase such as "110 percent of the transportation costs" that can be added to that average price, rather than a 10 percent gross profit above the average price. It will probably work out to be similar, but it is not as much of a price cap as a profit cap.

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MR. LAKOSH said there may be some gouging by fuel wholesalers too. He would add fuel wholesalers in two places in the bill. "We don't need to be subsidizing the airline industry or the heavy fuel oil sales of Tesoro." Those may be invested illegally because they ship crude into the Aleutians and have refined products throughout the Aleutians without the necessary spill prevention and response equipment. Consumers would be much better off not having to deal with refined products that are created by Tesoro. "We want to be able to subsidize the use of geothermal heat."

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MERRICK PIERCE, Fairbanks, said he is involved with the Alaska Gasline Port Authority, but he emphasized he wasn't representing it now. He said SB 54 seeks to remedy obvious price gouging. It is a positive step because of the significant cost to consumers of price gouging by Flint Hills and Tesoro. There are additional remedies to reduce the cost of energy to Alaskans, and one is to reduce transportation costs by building energy infrastructure. That will also promote competition and put downward pressure on wholesale gasoline prices. The best alternative to gas is compressed natural gas (cng), and the highest priority of the legislature should be getting the all-Alaska gasline built. That will insure that Alaskans will have ready access to low-cost

natural gas, particularly in the Interior. Vehicles can be converted to run on it. Some are already built to do so. The benefits of cng vehicles are enormous, including a cost of 50 cents per gallon. Natural gas prices are collapsing because there are vast shale gas deposits being developed in North America. Vehicles that use cng have cleaner emissions. A vehicle like the Honda Civic GX has tailpipe emissions that are cleaner than the air of a polluted city. Here is an opportunity for a state that has hundreds of trillions of cubic feet of natural gas to demonstrate some real leadership to the rest of the country.

MR. PIERCE said that in 1970 the U.S. imported about 24 percent of its oil, and in 2008 it was 70 percent. Those imports cost us almost \$700 billion in 2008. That contributes to the massive trade deficit and weakens the U.S. economy. So Alaska should be doing three things. First, build the infrastructure with direct equity investment so Alaska has access to its natural gas. Second, the state should be purchasing or converting its vehicles to run on cng. Thirdly, the political subdivisions in Alaska should be encouraged to run vehicles on cng.

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CRAIG MCCONNELL, Northwest Arctic Borough School District, Kotzebue, said he supports SB 54, and he would like the bill to include wholesalers. Crowley Marine is the prime supplier of heating fuel, propane, and gasoline in western Alaska. It has a true monopoly. Heating fuel was recently selling for \$12.10 [per gallon] in a village in the region. It could get worse as the winter progresses. "We can't afford these prices." Other options for getting fuel to the area haven't been found. Crowley buys up the competition, like Yukon, which was a good supplier at one time. In the anti-trust agreement there were provisions like renting tank space from Crowley. Mr. McConnell pursued that but ran into roadblocks; he was stalled or blocked in every way he attempted to lower fuel costs for residents. Western Alaska is paying three to five times the price of fuel beyond Alaska urban areas. "We support this bill in western Alaska, and we would like to include language that addresses wholesalers."

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MARGARET HANSEN, Treasurer, Northwest Arctic Borough School District, Kotzebue, said she supports SB 54 and wants to add wholesalers to the language. Many other states have price gouging laws, and Alaska should too. The rate that Alaskan prices have been higher than the Lower 48 has consistently exceeded historical norms during these recent high prices.

Alaska prices increased while Lower 48 rates declined, even though Alaska suspended its gasoline tax. The House Judiciary Committee showed that the price disparities have arisen because of the prices that refineries sell products to retailers, and then the wholesaler, Crowley, has no competition. A person had to walk away from the community to cut wood and drag it back to keep houses warm and keep the plumbing from freezing. The state has put millions of dollars into water and sewer infrastructure. Selawik is an AVEC [Alaska Village Electric Cooperative] community, and it owes \$200,000 to AVEC and is working on a payment plan. Selawik owes \$22,702 for the water plant. AVEC has to pay \$18,955 for fuel charges. They get \$7,300 credit in "PCE", thanks to the state, so that cuts down their kilowatts, but the price of fuel is enormous. In one month, Selawik's electric bill to AVEC, not including the cost of fuel to heat the facilities, is \$65,558. January is going to be a problem. Many Alaskans have to decide to buy stove oil, food, or pay their electric and water bills.

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MS. HANSEN said an elderly woman in Noatak got on the VHF asking for food. She had no electricity, but she had heat. The community came together to help her. Fuel is \$9.90 a gallon in Shugnak, and it is over \$12.00 in Noatak. She has seen suicides increase in the region. "I think teens feel the economic crisis, so we have a sense of hopelessness." Working together has stopped some suicides, she believes. The school district is paying \$1.5 million more for energy. It takes money out of the classroom. "How can we do better teaching our kids with less money?" They need more vocational training to prevent dropouts and suicides. Taking money out of the classroom to pay for energy is drastic. Alaska has the constitutional responsibility to insure that natural resources are used to the maximum benefit of the Alaskan people. This bill will prohibit refineries from charging exorbitant prices that are detrimental to the welfare of individual Alaskans. It is an economic emergency.

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JEFF COOK, Director, External Affairs, Flint Hills Resources Alaska, North Pole, said SB 54 will adversely affect his business, harm consumers, and have long-term impacts for the people of Alaska. Flint Hills does not produce crude or own retail stations. All of its products are sold on the wholesale market. It makes less than one fifth of the gasoline used in Alaska and a third of the heating fuel in the Fairbanks area. His employees are proud of their contributions to Alaska. "We run a very efficient and very safe refinery." It has over 60

years of experience and has owned and operated the North Pole refinery since 2004. It also owns refineries in Minnesota and Texas. The North Pole facility has had modifications since it opened in 1977. It is a topping plant and lacks the sophisticated processing capability to refine all the crude oil coming into the plant into finished products. It takes between 180,000 and 220,000 barrels per day and distills it into a few basic products that it sells, and the rest is returned to the TransAlaska Pipeline. "We keep only about 50,000 barrels a day of saleable products, the majority of which is jet fuel." It also keeps fuel to run the refining process. "That energy to run the refinery is the second largest cost other than crude." It's energy cost is 2.6 times higher than the state of Washington.

MR. COOK said there were many topping plants in the United States in 1977, but now there are just a few. Increased environmental emissions regulations caused many to shut down. Increasingly stringent federal requirements on the types of fuel produced forced others to close. The North Pole refinery has kept pace with the new environment regulations, but the changes in the types of fuel required has impacted the amount of gasoline and diesel fuel that it can produce. Federal mandates to lower sulfur content have substantially diminished the ability to produce fuels. While it still produces some gasoline and off-road diesel, "we now buy gasoline and diesel fuel from other sources in order to meet the full needs of our consumers." So supplies are tight and margins for refineries like the North Pole one are small. The company is working with the Department of Natural Resources to understand the circumstances that threaten their viability in the state. "Even though our refinery has been profitable recently, that has not always been the case, and we must explore all options to deal with that uncertainty." If SB 54 becomes law it will be a very serious threat.

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MR. COOK said SB 54 caps prices at 10 percent above Washington prices, and it subjects refiners to penalties ten times the amount of the economic benefit from an unlawful sale or \$50 million dollars. Such a measure would be so oppressive that Flint Hills Resources may be forced to cease refining and distributing in the state. Consumers can seek the lowest price for any commodity. Government intervention ultimately creates far more harm than good. Producers react to price controls in a number of ways and none are good for consumers. Producers may choose to produce only when it can be profitable. Investment decisions will be based on whether the price is sufficient. All this leads to shortages, and a lower price is not good for the

consumer if there is no fuel. Trying to out-guess the market by setting a price cap is a dangerous game and Flint Hills will not engage in it. The bill has good intentions but could shut down his facilities. High fuel prices are a hardship for many families, but North Pole workers pay the same price for gas as anyone else.

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CHAIR MCGUIRE noted his statement that it is 2.6 times more expensive to operate his refinery in Alaska than his refineries in the Lower 48. Is that cost passed along to the consumer?

MR. COOK said, "You're not always able to do that." Prices are based on the market. He referred her to the fall quarterly of the Fairbanks North Star Borough, which compares the energy index of Fairbanks with Anchorage and Seattle. It is high in Fairbanks because there isn't natural gas. He has to run his refinery on refined products of crude.

SENATOR MCGUIRE asked if his company considered switching to alternative energy to lower the cost of operations.

MR. COOK replied that his company is following the discussions of a bullet line and the coal-to-liquids project, but it has found no other source.

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CHAIR MCGUIRE asked if there are adequate incentives for lowering the cost of running the refinery.

MR. COOK said they do everything they can to minimize the costs. The refinery was losing money from mid-2007 to 2008. The refinery wants to be there for the long term.

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SENATOR WIELECHOWSKI said many people are concerned about the health of the North Pole refinery, and because of that there was a hearing last week. Mr. Cook was invited to testify but he canceled at the last minute. "I was very disappointed at that." The state has reached out to Flint Hills many times. It already gets significant government subsidies in the form of royalties. "You pay less for oil than what many people pay for our oil, and you've asked for many government subsidies for years. And you've been threatening to shut down unless you got those subsidies since long before this bill came along."

MR. COOK said, "We have never asked for a subsidy or a bailout." But the company has talked about ways to structure its agreement with the state. In times of low margins there may be a risk-sharing arrangement with the state. During higher margins, the state might actually get more for the oil. "We pay fair-market value plus a premium for the crude oil." People don't realize another cost, which is 22 cents a gallon for every gallon sold in 2008.

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MR. COOK said he felt it prudent to hold off last week when the House Labor and Commerce committee canceled its hearing. He hadn't seen the attorney general's report either.

CHAIR MCGUIRE said the committee just received the report: The 2008 Alaska Gasoline Pricing Investigation.

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ED SNIFFIN, Assistant Attorney General, Department of Law, Anchorage, said he is responsible for enforcing Alaska's consumer protection and antitrust laws. He thought Senator Wielechowski did an excellent job summarizing the frustration that consumers feel. It's frustrating and there isn't an easy answer. The report concluded that there wasn't evidence that there was illegal activity occurring with respect to gasoline pricing. That doesn't mean that the prices aren't high; it just means there wasn't any illegal collusion that his department could find. Pricing isn't a cost-based phenomenon. It's tempting to look at how much it costs per gallon to produce, but commodities aren't priced that way. Supply and demand is what matters and how much a company can actually sell it for in a competitive market. But we don't have very competitive markets here. There are two refineries that produce gasoline. Tesoro has the lion's share of that market. So competition doesn't work nearly as well in Alaska as in other parts of the country.

MR. SNIFFEN said he looked at Hawaii as a comparison because it is geographically isolated and it has two refineries: Tesoro and Chevron. The market structure is an oligopoly just like Alaska. Looking at both, Alaska prices were "a little higher at times," but he found the same general pattern. The price of crude oil last year drove prices up and "they couldn't increase it fast enough to keep up with the rising cost of crude oil." Competition is what brings prices down, so when oil prices fell, gasoline prices dropped quickly in the Lower 48. There is always a little lag between the run up in prices. The unprecedented rise in crude oil prices last summer followed an even more

unprecedented fall, and that lag was exaggerated tremendously. That lag was what made Alaskans angry. The best economist he could find came to the same conclusion that in an oligarchic market those kinds of spreads occur. The prices are starting to come closer now. So there are some market-based explanations, but it doesn't make it any easier to handle. Perhaps legislation is the only way to address it, but "we couldn't substantiate any kind of law enforcement action against the distributors, refiners, or retailers."

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CHAIR MCGUIRE noted page 11 of the report. Under the language on Unfair Trade Practice Laws, it states that this wouldn't fit under the price gouging law. "But when you get into a potential application of Alaska's Unfair Trade Practice and Consumer Protection Act, which we worked together on over in Judiciary, then you go on to define 'unfair' and then you include the Alaska Supreme Court's factors for unfairness." But on page 12, it says "no cases applied the test to the price of gasoline except in connection with a price-gouging statute that prohibits excessive prices during an emergency." It goes on to say that it may seem that gasoline prices are unfair or perhaps excessive or unconscionable, "and there you're using the exact terminology - the terms of art listed in the Act and in the Supreme Court language. You then go on to say the attorney general's investigation did not uncover, however, evidence that Alaska gasoline prices were unconscionable or oppressive in light of the market structure."

CHAIR MCGUIRE said she doesn't know where that test comes from. She sees the report going through the various layers of laws. It is clearly not an illegal act, but it may be an unfair act, and the report sites the reasons why it could be unfair. But then Mr. Sniffen determined that it's not unfair based on a standard that Chair McGuire is not familiar with.

MR. SNIFFEN said the test for unfairness is fairly subjective. The State v. O'Neill Investigations, Inc. case in the Alaska Supreme Court lists those factors. The second factor is if something is immoral, unethical, oppressive, or unscrupulous, "and that's what we say on page 12; we look to see whether or not a gasoline price is to be unfair or excessive or unconscionable - relying on some of the terminology that the Alaska Supreme Court has used." He spoke of a case from North Carolina where the court looked at gasoline pricing under their laws and tried to determine if it was unscrupulous, and it was found not to be. Mr. Sniffen gave the example of a person with

access to a vaccine that cost one dollar that people will die without, and that person charges \$10,000 for it. That seems obviously unscrupulous and unfair because it is a life-saving vaccine and there is no need for the cost to be that high. This investigation of Alaska gasoline found that there was some evidence that the volatility in the market supported the swing in prices and didn't conclude that prices were unscrupulous, oppressive, or unfair.

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SENATOR WIELECHOWSKI said that is the supreme court definition of unfair. However, the legislature has the right to add to the 55 acts that are already considered unfair, and then the supreme court would be required to accept that definition.

MR. SNIFFEN replied that was correct.

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SENATOR MCGUIRE referred to page 20, which states that many consumers assume that there's collusion among gasoline stations when prices increase and decrease at nearly the identical time. She said that is the impetus for many of the discussions because constituents ask how that can be. She finds it interesting that this report changes from an investigative style to a general report style at different points. "Here's a place where ... that broad statement is made, and then below it, it doesn't say, 'and so we investigated this and we subpoenaed emails, we asked for methods of communication that could be possible between gasoline stations.'" Instead it just suggests other ways that retail gas stations might possibly know of each other's prices. She wants to know what was done in the investigation so Alaskans can be assured that it was thorough and included subpoenas.

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MR. SNIFFEN said the stylistic changes within the report might be the result of two different authors: himself and an Econ-1 consultant. Parallel pricing is not unusual, because the prices are displayed for everyone to see. As soon as one price sign changes the next one does. Alaska is a small market with stations close together. Anchorage gasoline retails in a 10-cent range. The range in Seattle is about 40 cents. He did issue subpoenas and "CIEs". He interviewed station owners about how they make their pricing decisions. That data is extremely confidential and proprietary. "I believe we thoroughly investigated all of those issues, and we're satisfied with the conclusions."

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SENATOR MCGUIRE said it's a commodity, but it ends up being a utility. There are price gouging laws in other states. She noted the RCA, and said that energy in the form of electricity and natural gas are necessities, especially in Alaska. There could be extremely high prices and people would pay them because of a lack of alternatives. Rates have to go through the RCA for that reason. "I guess you could argue that [driving a car] is a privilege and it's not a right." But if someone is going to the hospital to deliver a baby or to respond to a life-threatening situation, "I think you could argue it is a necessity, and yet it is a commodity." What have other jurisdictions done to deal with this issue besides price gouging legislation?

MR. SNIFFEN said there have been recent attempts to regulate gas prices. In 2005 Hawaii passed a statute to give their public utilities commission the authority to set the wholesale rates for gasoline. It was allowed to sunset because the prices went right up to the cap and stayed there. It may have kept prices higher than they would be in some instances. The legislation created a "safe harbor" instead of letting competition drive prices down. Some people attribute Hawaii's failure to politics or hurricane Katrina. One of the features of the legislation was tying the price to a Gulf Coast price.

CHAIR MCGUIRE closed public testimony and adjourned the meeting at 1:13 p.m. SB 54 was held over.

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