

HOUSE FINANCE COMMITTEE
March 14, 2011
8:02 a.m.

8:02:31 AM

CALL TO ORDER

Co-Chair Stoltze called the House Finance Committee meeting to order at 8:02 a.m.

MEMBERS PRESENT

Representative Bill Stoltze, Co-Chair
Representative Bill Thomas Jr., Co-Chair
Representative Anna Fairclough, Vice-Chair
Representative Mia Costello
Representative Mike Doogan
Representative Bryce Edgmon
Representative Les Gara
Representative David Guttenberg
Representative Reggie Joule
Representative Mark Neuman
Representative Tammie Wilson

MEMBERS ABSENT

None

ALSO PRESENT

Representative Mike Hawker; Bryan Butcher, Commissioner, Department of Revenue; Bruce Tangeman, Deputy Commissioner, Department of Revenue.

SUMMARY

HB 110 PRODUCTION TAX ON OIL AND GAS

HB 110 was HEARD and HELD in committee for further consideration.

#hb110

HOUSE BILL NO. 110

"An Act relating to the interest rate applicable to certain amounts due for fees, taxes, and payments made and property delivered to the Department of Revenue; relating to the oil and gas production tax rate; relating to monthly installment payments of estimated oil and gas production tax; relating to oil and gas production tax credits for certain expenditures, including qualified capital credits for exploration, development, and production; relating to the limitation on assessment of oil and gas production taxes; relating to the determination of oil and gas production tax values; making conforming amendments; and providing for an effective date."

8:04:37 AM

BRYAN BUTCHER, COMMISSIONER, DEPARTMENT OF REVENUE, provided a PowerPoint presentation titled: "CS HB 110 (RES) Introduction, Proposed Changes to the Oil & Gas Production Tax." He discussed that HB 110 was related to Alaska's future and that its goal was to make changes to the current tax system that would make Alaska more competitive both nationally and globally, to produce more jobs for Alaskans, and to increase Alaska's oil production. He discussed that a recent projection that North Dakota would pass Alaska in oil production in the next five years, was a real wakeup call for Alaska. The state needed to maximize the production on its state lands given that the federal government had been a deterrent to development in the Outer Continental Shelf (OCS) and on federal lands. Many of the credits and incentives that had been created over the past few years had helped but production continued to decline. He delineated that there continued to be a significant amount of oil available for development on Alaska's state lands. The two main goals of HB 110 related to the development of unexplored oil fields and to the increase of production from the legacy fields that currently provided over 80 percent of the oil to the Trans Alaska Pipeline System (TAPS). He stated that oil provided over 85 percent of the revenue that was required to run the state's government. He explained that the challenge was significant and that the bulk of the easiest to recover oil had already been extracted. The state was looking at the production of viscous oil, heavy oil, and development in areas that had very little to no infrastructure; therefore, the challenge was greater than it had been previously. This was a main component of the administration's multi-tiered process in

order to increase TAPS production. The process also involved the Department of Transportation and Public Facilities (DOT) Roads to Resources program; improvements to and expediting of the permitting process by the Department of Natural Resources (DNR); focus on federal road blocks by the Department of Law (DOL); work by the Department of Labor and Workforce Development (DLWD) to train Alaskans for additional work that would arise in the future; and, continued work by the Department of Environmental Conservation (DEC) to ensure that development would continue to be done in an environmentally sound manner.

Commissioner Butcher discussed that the bill aimed to improve the investment climate for existing players on the slope and to invite new entrants. The bill also worked to create jobs for Alaskans and to increase production and extend the life of TAPS. There had been a pipeline shutdown in January 2011 for almost one week and due to the extreme cold on the North Slope it had been eye-opening and was very evident just how fragile the pipeline really was. The pipeline could have frozen and the fact that it was only one-third full drew attention to the production level in the state and to the potentially limited longevity of TAPS. Once the pipeline reached a point where it could no longer provide the work that needed to occur, the pipeline system would shut down. Up to that point an increased amount of work and money would be required for heating and other items to keep the oil flowing. It would be more expensive and would cut into funds that would have gone to the state treasury.

Representative Gara referred to the term "pipeline shutdown" and did not think that a reduction to the pipeline volume was in the state's best interest; however, a number of years earlier TAPS owners conducted a number of retrofits to allow the pipeline to operate at a lower volume.

Co-Chair Stoltze informed the committee that there would be a thorough conversation at the end of the week.

Commissioner Butcher discussed Page 4 titled: "North Slope Production." The chart showed the sharp increase in oil production that occurred in 1977 and peaked in FY88 at a little over two million barrels of oil per day. It detailed the rather quick production decline that occurred in the

years that followed FY88. He emphasized that from the peak in 1988 through 2010 that the barrels per day had dropped over 68 percent. From that point the decline had been an average of five percent to six percent on an annual basis. The legacy fields continued to decline; however, the state expected that half of its oil production would continue to come from these fields in 2020. It was important to focus on new field development and on the continued production at existing legacy fields. He discussed that Page 5 "Forecasted ANS Production FY 2010 - 2020," provided a forecast from the Department of Revenue's (DOR) fall forecast book from 2000 through 2020. The light gray portion of the chart represented that currently producing fields followed the traditional decline curve and were the easiest and most certain for DOR to predict. The darker gray section represented fields such as Liberty that were under development for expected production in the next couple of years and were currently receiving a significant amount of money and work. The most speculative were areas that were under evaluation for potential development and were represented by the dark black section on the chart. He delineated that the bill could potentially be very valuable to oil fields that were under evaluation and to other areas that had not been seriously considered due to the current tax regime. More detail on the chart would be provided at a production forecast meeting with DOR's production economist Frank Molly that was scheduled later in the week.

Commissioner Butcher discussed a chart titled: "North Slope Development Drilling" (Page 6) that provided information on development and service wells. Development wells aided in the development of existing fields, whereas, service wells were injection wells that helped development wells to recover more oil from the fields. A green line on the chart represented the Alaska North Slope West Coast (ANS WC) price. Through the early 2000s the price was close to \$200.00 then it slowly dropped and popped up slightly in 2010 with the price of oil.

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Commissioner Butcher addressed the chart on Page 7 titled: "North Slope Exploration Drilling" that provided a snapshot of exploration well locations. There had been 18 wells drilled in 2007 at the time that Alaska's Clear and Equitable Share (ACES) legislation passed. When the bill passed at the end of 2007 the locations for exploration had

already been decided for 2008 and as a result the number of locations dropped to nine in 2009 and four in 2010. Two of the four wells were not in the true exploration category as they were drilled in the previously developed Point Thompson field. He communicated that DNR expected that only one exploratory well would be drilled in 2011.

Commissioner Butcher discussed Page 8 titled: "There's Lots of Oil Left in Alaska." The cumulative production from the beginning of TAPS through 2010 was 16 billion barrels. The Department of Natural Resources estimated that the remaining North Slope reserves exceeded five billion barrels; however, geology based estimates of total oil volumes were much higher. He explained that the five billion to six billion barrels in the forecast did not include approximately 20 billion barrels in the giant Ugnu deposit or offshore volumes from the Chukchi or Beaufort Seas. The Ugnu deposit would be factored into the DOR revenue forecast when it became economic to produce heavy oil.

Commissioner Butcher addressed Page 9 titled: "Areas of North Slope are Underdeveloped" that showed oil and gas activity in 2010 and 2011. The dark shaded areas at the top of the map represented the primary oil production areas from the past few decades, such as Prudhoe Bay and Kuparuk. The lighter gray area that was circled in red was indicative of areas that had not experienced exploration. The undeveloped area included much of what the developers Armstrong, Repsol, and Great Bear Petroleum were focused on. The governor believed that the 15 percent oil taxes could be of benefit in the unexplored fields and that the state should encourage the development and exploration of oil in the region.

Commissioner Butcher pointed to Page 10 titled: "How Can We Reverse the Trend?" The list of sample investor criteria included prospectivity or opportunities that existed for oil companies; geopolitical stability, which was a tremendous benefit to the U.S.; regulations, access to resources, development permitting, environmental constraints, which had all been a challenge federally; and, operations, the location of the existing infrastructure, experienced workforce availability, costs, and market proximity. He explained that Alaska's limited infrastructure and workforce availability combined with expensive transportation costs due to its distance from

market, made production in Alaska more challenging than in Texas, North Dakota, and many of the other oil producing states. Given all of the challenges in Alaska, the bill focused on making a change to the tax regime. He believed that the difficulties contributed to the decline of investment in Alaska's oil industry and as the price of oil had increased over the past few years there had been increasing investment in North Dakota, Texas, and in many other states and countries.

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Representative Doogan asked whether there would be a chance to ask questions about the presentation.

Co-Chair Stoltze responded that they would see whether time allowed for questions during the meeting. He informed the committee that there would be time for questions the following day.

Commissioner Butcher moved to Page 12: "Production Tax Overview." He explained that the production tax value (PTV) was the market price less transportation costs and allowable lease expenditures. Allowable lease expenditures included both operating and capital expenditures. The current PTV base tax rate was 25 percent and it would not change under the proposed legislation. The current progressive surcharge rate was triggered when a company's PTV reached \$30.00 per barrel. He explained that from \$30.00 dollars per barrel to \$92.50 per barrel the surcharge added 0.4 percent to the tax rate of each additional \$1.00 increase until the combined tax rate equaled 50 percent. He relayed that the additional tax applied to the entire cost of the barrel; therefore, higher progressive rates experienced marginal tax rates with 93 percent government take and the cost of the barrel increased by 1 percent.

Commissioner Butcher explained that the bill would shift from progressivity to a bracket system, where a tax rate would be applied with each additional bracket. The tax increase would only apply to a particular portion of the barrel and would result in a more gradual progressivity slope. The state would continue to take a higher share when oil prices were high. He discussed that from \$92.50 per barrel and \$342.50 per barrel the surcharge dropped from 0.4 percent to 0.1 percent for each additional \$1.00

increase in PTV until the combined tax rate reached the maximum of 75 percent. The bill would reduce the cap to a maximum of 50 percent. He relayed that the department would provide a comparison between the current law and the changes that would take place under HB 110.

Commissioner Butcher addressed a second page titled: "Production Tax Overview" (Page 13). He explained that the total tax before credit was calculated by adding the progressive surcharge rate that was applied above 30 percent, to the base tax rate of 25 percent. A company's final tax bill was calculated by subtracting the credits that had been applied against the taxes from the total tax before credit. Page 14 titled: "FY 12 Production Tax Projected," provided detail on the FY12 fall revenue forecast that totaled \$82.67 per barrel with the production estimate at 622,182 barrels. He pointed out that the numbers would change in the revised spring revenue forecast that would be released in the last few days of March or in early April. He explained that the annual production value of \$18.774 billion was determined by multiplying the price per barrel and the number of barrels. The royalty and federal barrels were not taxed and were subtracted from the \$18.774 billion, which resulted in \$15.9 billion. The \$1.229 billion ANS marine transportation and tariff on tax cost was subtracted from the \$15.9 billion. The FY12 PTV was estimated to be \$9.675 billion and was determined by subtracting the deductible operating expenditures that were estimated at slightly under \$2.5 billion and the deductible capital expenditures that were estimated at slightly over \$2.5 billion. The total \$2.754 billion production tax for FY12 was determined by subtracting the base tax rate of \$2.4 billion, the progressive tax rate of \$785 million, and the estimated tax credits of \$450 million. He reiterated that the numbers would change in the spring revenue forecast.

[8:26:08 AM](#)

Commissioner Butcher pointed to the "Production Tax Credits Overview" on Page 15 that listed numerous current credits. The qualified capital expenditure credit was 20 percent, and a 40 percent credit for well lease expenditures outside the North Slope had been implemented to encourage more development in Cook Inlet. When a company had a carried forward annual loss it received a 25 percent carried-forward annual loss credit or net operating loss credit

(NOL). The small producer and new area development credit was up to \$12 million per year for small producers and up to \$6 million per year for production outside the North Slope and Cook Inlet. The alternative credit for exploration was 30 percent to 40 percent of eligible exploration expenditures provided that certain criteria were met. The Cook Inlet jack-up rig credit was 100 percent to 90 percent to 80 percent for the first three exploration wells drilled using a jack-up rig in Cook Inlet. He relayed that the jack-up rig credit had motivated companies to explore in the Cook Inlet area and that Escopeta Oil and Buccaneer Energy were currently working to bring jack-up equipment into the state.

Commissioner Butcher discussed that the bill was comprised of three major components and that it would make a number of smaller changes to state statute. First, the progressivity rate would be changed to a bracket system that would have a similar structure to the federal income tax system. He used federal income tax as an example and explained that an income of \$0.00 to \$30,000 would have a 10 percent tax, income of \$30,000 to \$40,000 would have a 13 percent tax, and that the tax would continue to increase as income increased. He explained that the higher tax bracket was not applied to the entire amount of earned income from the year and a person would still pay the 10 percent rate on the first \$30,000 that they earned. Under the current oil tax system the taxes picked up a higher and higher percentage of the entire barrel of oil.

Co-Chair Stoltze noted that petroleum economist Roger Marks would present to the committee the following day and would be available for questions on bracketing.

Commissioner Butcher discussed Page 17 titled: "Main Proposed Changes." The base tax rate would remain at 25 percent; however, in order to motivate production and exploration the base tax rate would be reduced from 25 percent to 15 percent for exploring leases or properties that had not been unitized or producing on or before December 31, 2010. The bill would reduce the maximum cap on the tax rate from 75 percent to 50 percent and for the unexplored fields the rate would decrease from 50 percent to 40 percent. He delineated that the tax rate would start 10 percent lower and would be capped 10 percent lower. The third major component of the bill would extend the 40 percent North Slope well lease expenditure tax credit in

order to motivate additional development on the existing fields. The current 20 percent well lease expenditure credit was increased to 40 percent for areas south of 68 degrees north latitude. Under the legislation tax credits could be claimed in one year and would benefit smaller independent companies that had cash flow issues. The current process required tax credits to be claimed in two years and made it difficult for DOR to deal with the credits because they had to split multiple years. He explained that annually the department dealt with the second year of a previous tax credit and the first year of the new two-year credit. Ultimately the revenue effect was negligible given that the amount of money the department would handle would not change under the one-year claim period. The bill also changed the monthly tax calculation that was impacted by short term price and cost peaks to an annual tax calculation that was based on average prices and costs. The annual calculation was easier for DOR to administer and helped the industry to move away from the peaks and valleys that were present in the monthly calculations. He directed attention to the effective dates that would be implemented as a result of the legislation (listed on the right-hand side of Page 17). The effective date of the change from progressivity to brackets, new-area 15 percent tax, and the yearly calculation would be January 1, 2013 and would give DOR time to work on regulations and to prepare the tax for implementation. The extension of the well lease credits from 20 percent to 40 percent would be January 1, 2012 and did not require the preparation time that was required for the other modifications.

[8:33:06 AM](#)

Commissioner Butcher relayed that Page 18 titled: "Nominal Production Tax Rates" showed the current ACES nominal rate (in blue). Changes that would occur under HB 110 were indicated with a red line that represented unitized fields nominal rates and a green line that was 10 percent less and represented the nominal rates of non-unitized fields that were not currently producing or being developed. The brackets were set up on the same progressivity curve as ACES but increases would not be applied to the entire barrel and would only impact the brackets.

Representative Gara wondered where the loss was under the bracketed system. He communicated that at \$90.00 per barrel the ACES nominal rate and the HB 110 unitized fields

nominal rate were not the same. He remarked that the chart made it look like the tax rate would be the same under each system, but that Commissioner Butcher had explained that the rates would not be the same. Commissioner Butcher responded that the tax rates would be at the same place at \$90.00 per barrel.

BRUCE TANGEMAN, DEPUTY COMMISSIONER, DEPARTMENT OF REVENUE, explained that the bracket for the particular section would cover a range of \$80.00 to \$92.50; therefore, \$92.00 would be slightly different when comparing ACES to the bracket system.

Representative Gara asked whether there was a chart that showed the actual tax rate at \$90.00 per barrel for all of the oil under the new law compared to the actual tax rate under the old law.

Co-Chair Stoltze asked the department to have the chart available for a future hearing.

Representative Hawker reported that Roger Marks would discuss the difference between nominal and effective rates in the meeting the following day.

Commissioner Butcher addressed Page 19 titled: "Marginal Government Take." He explained that marginal referred to the percentage taken by government for each additional \$1.00 that the price of oil increased. He explained that the slope of the ACES marginal take increased at a much sharper rate given that under the current system an increase applied to the entire barrel of oil. Under HB 110 the government share would continue to increase with the price of oil; however, the rate increase would not be as extreme as it was under ACES. He relayed that at \$92.50 the PTV of the federal and state government take would be 93 percent and the producer take would be 7 percent. He discussed the concern that producers had over the distribution between government and producer take given their front-end financial contribution to exploration. The prospect of receiving very little on the back-end when oil prices were high made investment in Alaska less attractive than it was in other locations.

Commissioner Butcher discussed Page 20 titled: "Share of Total Profit - ACES" that related to the percentage share of the profit under ACES that was based on the price of oil

that ranged from \$40.00 to \$265.00. He reminded the committee that when oil production first began off of the North Slope that former Governor Jay Hammond and the legislature had believed in an "even share" between the producers, the state, and the federal government. He relayed that the state did not currently have control over the federal share, but that it did have control over its own share. He discussed that using the recent oil price of \$115.00 per barrel, the state's share would be 57 percent, the producer's share would be 28 percent, and the federal share would be 15 percent. At the current price the state would earn between half and two-thirds of the profit, producers would receive less than one-third and the federal government would receive less than the producer share. He discussed that under HB 110 at \$115.00 per barrel the state's share would be 45 percent, the producer's share would be 35 percent, and the federal share would be 19 percent. The share of the total profits would increase with the price of oil and the state would continue to receive its fair share under the governor's proposed legislation. Page 22 titled: "Share of Total Profit CS HB 110 (RES): Non-Unitized Fields," outlined the non-unitized fields where no exploration had occurred. To provide incentive for producers when oil was at \$115.00 per barrel the state would receive a smaller portion at 38 percent, the producers would receive 40 percent, and the federal share would be 22 percent. He explained that an increase in oil price would increase the state's share and decrease the producer's share.

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Commissioner Butcher reiterated that the goals of HB 110 were to improve the investment climate for the state, to increase production, and to create jobs for Alaskans. He relayed that increased oil prices over the past few years had encouraged significant development in Texas despite that it was a far more mature oil producing state than Alaska. The administration believed that a reduction in the upper level tax rates would contribute to an improved investment climate that would in turn increase production and create jobs in Alaska.

Representative Doogan wondered when the committee would see actual numbers that would illustrate how the changes in the bill would impact Alaska. Commissioner Butcher replied that there would be an in depth discussion on the fiscal note

during the department's time in front of the committee that week. They would discuss the short-term impacts as well as different investment scenarios for the future. He communicated that it was impossible to determine exactly what the figures would be, but a number of scenarios would be provided.

Representative Doogan queried whether DOR would be able to tell the committee what the cost of the bill would be. Commissioner Butcher responded that the department would provide estimates on the short-term costs; however, they would not be able to provide the exact production that would result 10 years in the future. He added that the administration could outline its solution to the problem and it could lay out various scenarios; however, it would ultimately be the industry's responsibility to present a compelling case to the legislature on why it believed a material change was necessary to do business in the state.

Representative Doogan wondered when the committee would be able to ask specific questions about the presentation.

Co-Chair Stoltze responded that the committee would be able to ask questions over the next couple of days. He explained that it would be helpful for committee members to provide complex questions ahead of time in order to give the department time to prepare.

Vice-chair Fairclough referred to Page 7 titled: "North Slope Exploration Drilling." She requested that the administration provide its perspective on why only one well had been drilled in 2003. She also wanted to hear from producers or others on why they believed the 2003 decline had occurred.

Representative Gara wondered whether DOR planned to amend fiscal notes based on information that had surfaced in prior testimony. He relayed that prior committees had determined there would be a cost associated with the governor's proposal to tax on an annual basis as opposed to a monthly basis. Under the proposed legislation the cost would have been approximately \$600 million in lost revenue three years earlier. He referenced that Commissioner Butcher had stated the average lost revenue could be approximately \$200 million; however there was no reflection of the loss in the fiscal note. Commissioner Butcher responded that DOR would provide a slide that would

estimate the future loss. He communicated that it was possible to account for the fact that 2008 was the most volatile oil price year in history, but it would not be a reflection of the norm. He stated that the department would provide the information to the committee.

8:46:16 AM

Representative Gara wondered whether there would be a fiscal note related to the cost. He observed that a fiscal note was typically required when there was a cost to the state. Commissioner Butcher replied that the figure would be listed in the fiscal note and an adjustment would be made in the department's spring revenue forecast that would be released in several weeks.

Representative Joule knew that it was hard to project all of the variables looking into the future; however, he wondered how the bill would have applied looking back for the past couple of years. He asked how the bill would have impacted taxes historically. Commissioner Butcher responded that DOR would provide the information to the committee. He added that the department would only be able to show how the reduction in tax would have impacted the state and not what the state would have seen in increased production as a result of the tax.

Representative Wilson asked why the federal government share of total profits that was shown on Pages 20-22 would increase extensively. She wondered why the federal government would receive as much profit as the oil companies. Commissioner Butcher replied that oil companies were able to deduct the percentage of their state taxes from their federal taxes. He explained that a lower state tax would increase a company's federal taxes because they would lose the ability to deduct the state tax from their federal tax. He offered to provide more detailed information at a later time.

Representative Wilson asked the department to provide additional information in the future.

Representative Neuman asked for detail on the restoration and redevelopment wells that were included in the chart titled: "North Slope Development Drilling" (Page 7). He did not believe that the rediscovery and redevelopment of old wells with new technologies should be classified as new

exploration. He thought the breakout would help to differentiate the new exploration wells from wells that already existed. He believed that the differentiation was relevant to the portion of the bill that discussed credits or improvements towards the expansion of development, drilling, and access to Alaska. Commissioner Butcher replied that DOR would provide the detail to the committee. The Department of Natural Resources would be present at future meetings and would be able to answer questions as well.

Co-Chair Stoltze noted that DOR was carrying the bill for the administration and that it would be the conduit for the other departments.

Representative Guttenberg hoped that DOR would provide the rationale on why and how the changes in the bill would result in modified industry behavior and increased production and development. He asked what had led the department to believe that the proposed changes would result in the desired outcome. He wondered what changes to historical tax scenarios would have created a shift in the behavior of the industry when they were or were not conducting development. Commissioner Butcher replied that DOR would do their best to get that information to the committee. He believed that there was not historical data related to all of the changes given that oil taxes had not been reduced before.

Representative Guttenberg emphasized that there was a certain amount of evidence of historical information. He communicated that at different times the tax rates had been different and they did not always stay the same. He referred to the chart titled "North Slope Production" (Page 4) that showed a spike in production in 1977 and a decline in later years. He said that the state had been faced with the issue of production decline in the past and many people had asked what the tax rates had been and why further development was not underway. He remarked that Alyeska had looked at what their capabilities would be in advance. Commissioner Butcher replied that the questions would be good ones for the industry. He discussed that there had been questions about the dip at the tail end of the Economic Limit Factor (ELF). There were many elements that played into the dip and that the price of oil and a company's forecast were important to factor in. He believed that in light of the spike in oil prices over the past

several years that it was shocking Alaska had not increased production spending like other states had.

Representative Edgmon wondered whether the administration would make budget plans and projections for items such as corrections, energy, education, and everything on the spending side that may not be discussed in depth like the revenue and economic development side. He discussed that when the operating budget had recently reported out of the committee the co-chair had discussed that a handful of state agencies, retirement funds, and debt service expenses were driving about 75 percent of the general fund. Commissioner Butcher replied that DOR would present a slide that would provide its view of the revenue picture overlaid with its view of the state budget. He communicated that the department was working with the Office of Management and Budget (OMB) and that there would be a reasonable increase in the budget due to items such as Medicaid and other.

8:55:16 AM

Representative Edgmon wondered whether there would be detailed fiscal planning related to the expenditure side of the legislation. He understood that in order to plan for the legislation to take effect that there was a projection forward that included assumptions on the exploration and the revenue side. Commissioner Butcher did not know what OMB was factoring in specifically and would be surprised to find that they had looked at details at that level. In work with OMB the department had examined what would make sense based on historical terms to determine a snapshot of the budget that was as accurate as possible. He communicated that the department would ask OMB to follow up on the question.

Representative Gara thought that the commissioner had made conflicting statements about current oil production in Texas. He wondered whether production had been increasing or whether it had maintained at the same level. Commissioner Butcher responded that the amount of company spending in Texas had been increasing but production had plateaued and was currently down approximately five percent.

Representative Gara relayed that in 2006 when ELF had still been in place, 15 out of 19 oil fields had paid a zero percent to less than one percent production tax. He

communicated his intention to ask about that point in history given that it appeared to be a model of what would occur under a lower tax structure.

Representative Neuman wondered whether there would be a way to model how changes in tax rates applied to different production levels. He surmised that there was not really a cost to the bill but a change in tax rates. He referenced earlier questions about plans related to future budget shortfalls and hoped that the changes to the tax structure would result in increased production and a neutral revenue stream. He provided an example about bread at a Carr's grocery store that had originally been priced at \$1.25 and went on sale for \$1.00. He asked whether the store was losing \$0.25 or whether it hoped to sell more bread and provide job security for the bakery employees.

Representative Neuman shared that the goal was to determine how changes to the current system would result in more oil production and to extend the length of TAPS, which equated to 90 percent of the state's general fund revenue. He explained that restoration and rehabilitation legislation had encouraged more oil exploration and that subsequently the decline in TAPS had slowed by more than one percent. He believed that past events provided some proof on how the tax changes would impact the state. He discussed historical taxation, ELF and low tax rates, and that new technology made it easier for producers to recover some of the oil that had not been available in the past despite the lower tax rates. He emphasized that the oil that had been easy to recover no longer existed in Prudhoe Bay and Kuparuk.

Representative Doogan wondered what production increases the department expected under the legislation. He expressed that the proposed legislation included significant changes to the current system and that the department should inform the committee on the expected impacts. He requested information on the changes beginning with the bill's effective date and moving forward. Commissioner Butcher replied that it would be difficult for the department to provide its best guess out of an infinite number of possibilities; however, a small range of scenarios would be provided to the committee.

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Representative Doogan replied that he would expect the administration to defend the legislation on both the profit side and the cost side. He wondered when the industry would speak to the committee about the bill.

Co-Chair Stoltze replied that the schedule for the remainder of the week would be completed that day.

Vice-chair Fairclough requested a budget model to reflect a scenario in which oil stopped flowing through the pipeline. She opined that there was a risk that the oil flow would stop, but that some people believed that the pipeline would continue to run in perpetuity. She understood that the pipeline had recently been shut down and had been restarted despite an existing hole because the temperature had dropped at a faster rate than anticipated. She understood that if the temperature got too cold that there would be one large "piece of licorice" that would be required to be disassembled and shipped away. She noted that Alyeska, the pipeline operator, may have been able to speak to the statement more specifically.

Co-Chair Stoltze wondered how DOR would handle the revenue side of a pipeline shutdown.

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Representative Doogan asked to hear from the industry on whether the introduction of several additional heaters could have prevented the pipeline problem.

Representative Costello was interested in a comparison between the nominal, effective, and marginal tax rates. She wondered how Alaska compared to the rest of the world in the three areas.

Representative Hawker discussed the tax proposal evaluation process that had taken place in the legislature over many years. The Legislative Budget and Audit Committee (LB&A) had been charged with securing and providing professional consultation services to support the legislators in their deliberation and understanding of the issues. Approximately a year and a half earlier LB&A had undergone an extensive request for proposal (RFP) process to secure the services that would support gas-line and tax change discussions. Roger Marks had spent over 25 years as the state's senior petroleum economist and would be available all week for

questions. He relayed that Mr. Marks would provide a technical analysis of the governor's bill the following day. Dan Dickinson, the state's former tax director was also on contract and would be available to discuss tax code and statutes. The resources were intended for the use of the committee and he encouraged anyone with questions to contact his office to set up a meeting.

Commissioner Butcher looked forward to working with the committee on the legislation.

Co-Chair Stoltze made his office available for any questions related to the committee process regarding the bill. He encouraged members to provide detailed questions ahead of time to provide preparation time for presenters.

Commissioner Butcher expressed that DOR would be very happy to meet with members at anytime regarding the bill.

HB 110 was HEARD and HELD in committee for further consideration.

ADJOURNMENT

[9:13:52 AM](#)

The meeting was adjourned at 9:13 AM.