HOUSE FINANCE COMMITTEE
March 21, 2011
9:05 a.m.

9:05:32 AM

CALL TO ORDER

Co-Chair Stoltze called the House Finance Committee meeting to order at 9:05 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 Charisse Millett; Former Representative John Harris; Bryan Butcher, Commissioner, Department of Revenue; Margaret Brown, President and Chief Executive Officer, Cook Inlet Region, Inc. (CIRI); Ethan Schutt, Senior Vice President, Land and Energy, Cook Inlet Region, Inc.; Aaron Schutt, Senior Vice President, Chief Operating Officer, Doyon, Limited; Tara Sweeny, Senior Vice President of External Affairs and Communications, Arctic Slope Regional Corporation (ASRC); Eric Fox, Vice President of Operations, Camp Services NANA Management Services (NMS); Joe Mathis, President, NANA Pacific; Isaac Nukapigak, President, Kuukpik Corporation; Joe Nukapigak, Former President and Chairman of the Board, Kuukpik Corporation; Tom Leonard, Communications Manager, Calista Corporation.

SUMMARY

HB 110 PRODUCTION TAX ON OIL AND GAS

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

[Note: This meeting took place in Anchorage.]

#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."

9:05:46 AM

MARGARET BROWN, PRESIDENT AND CHIEF EXECUTIVE OFFICER, COOK INLET REGION, INC. (CIRI), discussed her personal background and that she had been the head of the oil and gas division of CIRI for 35 years prior to her current position as president. She discussed that CIRI was headquartered in Anchorage and that its regional boundaries represented the traditional territorial boundaries of the Dena'ina Athabascan Indians in Alaska. The company had operating investments inside and outside of the state and had recently developed energy projects in Southcentral Alaska such as the Fire Island Wind farm and Underground Coal Gasification. The company had also been involved in the oil and gas business for many years. The company had acquired land through Alaska Native Claims Settlement Act (ANCSA) that included legacy oil fields and had participated in exploration primarily in Cook Inlet and in a well on the North Slope. The company was concerned about exploration in Cook Inlet and on the North Slope and was excited that it currently had a well underway on CIRI's

Kenai Peninsula property. She emphasized CIRI's belief that North Slope development and exploration efforts had a very significant impact on the state's entire economy.

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Ms. Brown discussed CIRI's ownership interest in two companies that conducted a significant amount of work on the North Slope, including Peak Oilfield Service Company (Peak) and Alaska Interstate Construction LLC (AIC). The companies were known for their work that included moving oil rigs, building ice roads, moving heavy modular pieces, etc. The company had reviewed its budget and had been very concerned that the estimated income derived from Peak and AIC reflected the decline in work on the North Slope. The company had seen the effects in the numbers projected by Peak and AIC in addition to a reduction in work force for the two companies. Both Peak and AIC had begun a workforce reduction the prior year given the decline in work projects. She was alarmed by the magnitude of the decline and how the economy as a whole would be impacted. She had seen reports which had indicated that Alaska was not business friendly and did not welcome private investment. The difficulty of doing business in the state had "hit home" in her office. She discussed a recent dinner with Governor Parnell and business leaders that included telecommunications leaders, Alaska native corporations, oil companies, and tourism leaders. The overall concern that had been expressed was that private enterprise and private investment in the state were being "squeezed out." She explained that CIRI had seen a lot of resistance towards the ability to put private investment dollars into the region, specifically related to the Fire Island Wind project. She highlighted that she had also been personally looking for business opportunities outside the State of Alaska. She believed that private capital would move towards the highest likelihood of investment return and a balance between return versus risk. She did not want to see private investment dollars slip away in Alaska and believed it was necessary to examine aspects of the business climate that were resulting in the decline. She relayed that her husband was a geologist who had worked in harsh and challenging conditions in Prudhoe Bay. She thought he would agree that some of the easy oil had already been found.

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Ms. Brown opined that it was important to see the appropriate return for the risk taken by investors and to recognize that the oil that remained on the North Slope would be difficult to produce. A balanced risk versus return would create a "robust" economy. She discussed that the decline in the throughput on the North Slope had been obscured by the significant rise in oil prices in the past several years. The state had benefited from high oil prices; however, because the throughput decline had been masked, there was a lack of understanding about the true vulnerability of the pipeline. She believed that there was a need for legislative reform and that HB 110 worked to address concerns of the oil industry and the general public. She did not believe the status quo was an option. She disagreed with the approach that focused on how much the state would be "giving away" to the oil companies and emphasized that without a competitive environment on the North Slope, there would be no oil companies to invest and develop in the area. Business leaders throughout the state were concerned and there were several grass roots organizations that were researching where the competitive nature could be improved in the state. She thought it was indicative of the broad concern that people shared across all business segments about the lack of competition on the North Slope. She did not profess to know every nuance about HB 110, but believed the bill was on the right track. She noted that Alaska had a royalty stream that allowed for benefits when production and oil prices were high and she thought that the focus should not be on squeezing every cent from oil companies in the tax structure. She contended that Alaskans were looking for a balance that would allow a long-term robust business climate to persist on the North Slope that would spread to the rest of the state.

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ETHAN SCHUTT, SENIOR VICE PRESIDENT, LAND AND ENERGY, COOK INLET REGION, INC., was responsible for leasing of oil and gas production on CIRI land in Cook Inlet and for general energy development. He relayed that CIRI had encountered a significant amount of resistance to the Fire Island Wind project, primarily because CIRI was a for-profit business. He had heard several times in the past year behind closed doors that there was no place in the railbelt electrical market for a for-profit energy company. He believed that the idea that there should not be a profit motive was an unacceptable premise and had been a significant obstacle to the project on Fire Island. The company was currently looking at several wind farm investments outside Alaska, which essentially diverted investment money away from the state. He expressed that when local businesses felt unwelcome they would take their business outside. He had visited Calgary, Alberta in the spring and had discovered that Calgary had been rewarded for an abundance of energy development in oil fans, oil and gas leasing, unconventional oil and gas, CO2 tertiary recovery, etc. His visit to Calgary coincided with two negative pieces of news for Alaska. During his visit to Calgary there had been Nigerian engineers looking at the Agrium plant in Nikiski for possible dismantling of the energy infrastructure in Cook Inlet.

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Mr. Ethan Schutt had also heard the announcement that ConocoPhillips was closing the LNG (Liquid Natural Gas) export terminal in Nikiski. He believed the state had overreached its power to tax and had in turn driven business away. He did not think that it was helpful to make "hysterical" pronouncements in the press about the high profits that oil companies were making and the implication that profit motive was bad. He relayed that exploration was both very costly and very risky and that the state needed exploration investment dollars. He added that the chance of oil and gas exploration success was less than 10 percent; therefore, companies needed to be rewarded for successful investment. He vocalized that HB 110 was a good vehicle for change and that CIRI appreciated the governor's efforts.

Representative Doogan wondered whether Mr. Ethan Schutt did not believe that law makers were making enough effort to incentivize exploration. He believed that law makers had been under the impression that they were working hard to incentivize exploration. Mr. Ethan Schutt responded that there were exploration tax credit incentives for companies who did not have a significant amount of production; however, companies who had "real" production paid significantly higher taxes. He elaborated that the tax credit incentivized companies that were new to the state and was not in balance when there was both exploration and production. Additionally, there was a difference between the power to tax and the current royalty system. Resource owners had a royalty interest and it was important to not "squeeze" too much out on the tax structure because the power to tax was a governmental function. The sentiment that the oil belonged to Alaskans and that the state should get its fair share was specific to the "royalty regime." He explained that the tax regime related to what was fair in relation to the state as a government and its power to tax.

Representative Doogan expressed interest in any information that would help law makers know whether they were not doing something right. He was under the impression that approximately half of the $900 million spent in the prior fiscal year had gone to established oil companies in order to incentivize exploration and development.

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Mr. Ethan Schutt recommended further thought about the belief that incentivizing oil companies to invest more in the established fields, particularly in Prudhoe Bay was not in the state's interest. He believed that the legislature may want to look at tweaks to incentivize additional production and production enhancement investment within established oil fields, because the reserves on Prudhoe Bay that were not attainable with primary and secondary types of recovery may have been the state's largest oil asset on state land. The best place to find more oil was in an established oil field and the reserves left in Prudhoe Bay were significant; however, the tax incentive structure in Alaska related to true exploration outside of established units. He relayed that CIRI was not present to carry the water for big oil and that it would be necessary to get answers from oil companies directly.

Vice-chair Fairclough asked about CIRI's perspective on actions related to oil taxes that the state could consider in order to help create a business friendly environment. Ms. Brown responded that CIRI would like to see an established fair tax rate that was not overreaching and that would allow the free enterprise system work. The idea that the profit motive of private enterprise was not appropriate was the most alarming to CIRI. It was important to have an appreciation for where private enterprise, including native corporations, small companies, and oil companies, fit in Alaska in order to move forward. She explained that in Cook Inlet investments CIRI had experienced permitting delays and had run into the notion that private enterprise did not belong in the production of power generation. The state was founded by people with a "can do" attitude and she worried that Alaska had come to a place where people no longer had that attitude and could not design a future to move towards. Additionally, she thought that discussions related to the type of work commitments that would be obtained under lower taxes were beyond the scope and did not represent healthy dialogue regarding the tax regime. She believed that the demand for a particular work commitment would happen in unit operating and lease agreements required by royalty owners.

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Vice-chair Fairclough wondered how many workers had been impacted and how CIRI would reposition those workers who were no longer employed at Peak and AIC as a result of what was characterized as "dramatic" decline. Ms. Brown did not know the exact number of workers that had been impacted, but the decline had been more dramatic than expected. She explained that both companies had made workforce reductions and that although it was not always possible, each company worked hard to find work for employees in other locations. The companies did not want to lose trained and qualified workers; however, the reality was that without available work it was not possible to retain employees. The companies worked hard to maintain the balance between retaining a trained workforce without running into the red.

Representative Wilson asked whether it was state regulation, federal regulation, or non-profit organizations that did not support private business. Ms. Brown replied that CIRI had currently only had dealings with state regulation through the Department of Natural Resources permitting process and were pleased with the agency. She believed that the problem for people was caused by a rattling of the status quo. She knew it was not easy, but it was important to be able to embrace change and recognize that there were systems in the state that were not serving the people of Alaska the way that they should. She did not think that Alaska's unique and special status could be used as an excuse anymore. She professed that Alaska was not that unique and companies were going to North Dakota, Alberta, and overseas for oil exploration and development.

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AARON SCHUTT, SENIOR VICE PRESIDENT, CHIEF OPERATING OFFICER, DOYON, LIMITED, discussed that Doyon was the ANCSA regional corporation for Interior Alaska. The company was headquartered in Fairbanks and 13,697 shareholders out of 18,158 lived in Alaska. He expressed that Doyon supported HB 110, but preferred to see certain portions, such as "bracketing," implemented during the current year. Like CIRI, the company believed it was time for change. The two primary goals set forth by the board of directors were to be as profitable as possible and employment opportunities for shareholders. Doyon had three primary pillars of the business that produced revenue and jobs, including oil field services, government contracting, and natural resource development. There were four oil field businesses that operated primarily on the North Slope: Doyon Drilling, Inc. had approximately 300 year-round employees and operated drilling rigs; Doyon Universal Services employed approximately 850 workers and was a food services, security, maintenance, and emergency medical company; Doyon Associated, LLC was a pipeline and oil field infrastructure construction company that employed 150 seasonal employees and much fewer year-round; Doyon Emerald was an engineering and technical consulting firm that had 40 employees. He emphasized that approximately 90 percent of the employees were Alaskans working in Alaska. Approximately 75 percent or $300 million of the corporate assets were invested in the combined oil field services primarily on the North Slope.

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Mr. Aaron Schutt discussed Doyon's second pillar, natural resource development. Doyon was Alaska's largest private landowner and had 12.5 million acres and roughly half of the acreage had been selected for its resource development potential. He explained that roughly half of the lands selected for resource development had been selected for oil and gas potential. The company had partnered in 2005 on a multi-year commitment with the State of Alaska in a gas exploration project at Nenana on lands owned by the state, Alaska Mental Health Trust, and Doyon. A well had been drilled in 2009 without the hoped success, but the company would run another seismic exploration during the upcoming winter in the Nenana basin. Doyon also owned two million acres in the Yukon Flats with 500,000 selected for oil and gas potential. In 2010 Doyon had conducted a 100 percent ownership seismic program near Stevens Village and would continue ongoing efforts in the Yukon Flats. As a service contractor and investor in exploration activity, Doyon was aligned with the State of Alaska regarding the success of the oil and gas industry in Alaska. The bottom line was that the company believed that it was time to adjust the oil and gas tax structure in Alaska. Doyon had 1,500 employees that relied on the success in the oil fields. The company believed that there were still vast underdeveloped oil and gas opportunities in Alaska. Like CIRI, Doyon believed that the best production opportunities were in existing fields. There had been a loss of jobs and revenue in Doyon's business segments during the past several years. The company believed that the current oil and gas tax policy was a part of the problem. He reiterated that Doyon supported the bill but did want to see portions of the bill implemented during the current year.

Representative Guttenberg wondered whether there was any part of the oil and gas tax structure, administrative codes, or permitting that should be changed to incentivize or motivate exploration and development. He expressed that many law makers pointed to Doyon's success in the Interior as a game changer for energy in the state. Mr. Aaron Schutt replied that the exploration incentives that the state provided were very motivating for exploration outside of existing fields. At the beginning of the Nenana project Doyon was a 20 percent working interest owner. He explained that Doyon was very committed to the project, but that its partners who at one time owned up to 50 percent owner interest were not Alaskan companies and looked at the lifecycle of an oil and gas development project. Some of the companies were purely exploration and the major oil producers were involved with the exploration to production stages. It was important to look at each opportunity and the players at the table. A detriment to the company was its inability to attract major producers that would be present for the "long haul" from exploration through production. The major producers that could invest hundreds and billions of dollars in Alaska had not expressed the interest that Doyon hoped.

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Representative Gara asked whether the tax structure in the Yukon Flats was much lower than the ACES tax structure. Mr. Aaron Schutt did not know. He explained that due to the ANCSA 7(i) structure, the company strategy was to jumpstart exploration activity. He added that Doyon would not be a significant working interest owner in any development in the Yukon Flats.

Representative Gara wondered whether the difficulty Doyon had experienced in attracting producers to the project could have been due to a reason other than the tax structure given the possibility that tax was lower in the Yukon Flats. Mr. Aaron Schutt replied that it was not entirely clear why the company had not been able to attract major players to the Yukon Basin. He expounded that at the forefront of a rank exploration project there was major risk and that more than 90 percent of rank exploration ended in dry wells or less than successful wells. The exploration credits helped and were driving Doyon's activity in the Yukon Flats and Nenana. He relayed that the lifecycle of business opportunity included an analysis and predictability of the tax structure.

Vice-chair Fairclough referenced that from some people's perspective "everyone in the world could make large profits except oil." She asked about the difference between an exploration and a development company. She explained that exploration seemed to have credits that were doing what the tax structure had intended to do and were attracting smaller explorers who were interested in locating smaller pools of oil or another Prudhoe Bay. Mr. Aaron Schutt responded that he was not an oil and gas expert, but provided his perspective. He explained that major producers had the ability to conduct exploration and to see the project through to production; however, because production on large or remote fields were billion dollar investments, smaller companies with smaller balance sheets, such as Armstrong Gas Company LLC, needed to "sell down" their working interests to major producers after finishing the exploration period.

Vice-chair Fairclough explained that a conversation on the House floor had lead Alaskans to believe that everything was fine because there were incentives for exploration companies who were aware of the tax base and consequently there was no need to address the severance tax; however, it was important to understand that the equation had multiple parts and involved both exploration and production. Mr. Aaron Schutt agreed. Explorers were important, but the primary goal was production. He elaborated that when there was a transition from the explorer to the producer that often there were delays related to locating the appropriate partner, the transactional process, and the short exploration season.

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Representative Edgmon wondered what advice Mr. Aaron Schutt had to help find a balance between increasing business to address the "precipitous" production decline and the possible impact of a budget shortfall. As a legislator that represented rural communities he recognized the importance of increased business but was weary of the consequences of a potential budget shortfall and the impact it would have on rural Alaska. Mr. Aaron Schutt replied that there had been little discussion about the secondary impact of oil tax policy on contractors. Doyon was aware of the investment and activity decline as commodity prices had increased and they had not seen an increase in contracts, opportunities, and in secured contractor rates. It seemed that with high commodity prices that there would be more activity and higher wages, but Doyon had not been able to command higher contract rates. The contractor rates directly impacted employee wages and Doyon had been struggling to maintain their workforce level.

Representative Doogan wondered whether Doyon's work on the 250,000 acres in the Yukon Flats was primarily related to oil or gas. Mr. Aaron Schutt responded that it was aimed at oil exploration.

Representative Doogan asked for a definition of a "contractor" as it related to the oil industry. Mr. Aaron Schutt responded that "service provider" was a more appropriate term. He explained that Doyon contracted with major oil producers to provide various services, including drilling, security engineering, food service, construction, etc.

Representative Doogan thought that major oil companies had reduced exploration prior to the implementation of ACES and; therefore, a direct correlation may not have existed between the changes that were attributed to ACES and the decline.

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Representative Costello asked what portion of HB 110 Doyon wanted to see implemented immediately. Mr. Aaron Schutt responded that an immediate change from progressivity to the bracketed tax provision would be helpful. He noted that it could take companies years to implement a plan; therefore, earlier implementation of the bracketing provision would result in more activity sooner rather than later.

Representative Neuman wondered how changes in the tax structure over the past seven to eight years had impacted job security at Doyon. He asked how changes to the current system would affect employment opportunities at Doyon in the future. Mr. Aaron Schutt replied that five years earlier commodity prices were high and Doyon had experienced difficulty finding technically qualified employees. The lower commodity prices that followed made it hard to keep contracts; however, Doyon had been fortunate and had maintained a significant number of its contracts. He detailed that industry competitors had not been as fortunate and the loss of qualified workers had reduced the trained job pool in Alaska and was bad for all companies.

Representative Neuman asked whether changes in the tax structure were needed in order to revive oil and gas job opportunities that had been strained. Mr. Aaron Schutt believed that investment decisions by major producers were influenced by the tax structure and as a result there were fewer job opportunities in Alaska.

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Co-Chair Thomas asked how to keep money and jobs in Alaska. He did not want to provide oil tax breaks just to see the money leave the state for other locations such as North Dakota and Mississippi. Mr. Aaron Schutt replied that it was in the purview of the legislature to determine the appropriate balance between incentivizing investment and the tax level. Doyon believed that it was time to make a change given that its principal concern was higher activity.

Co-Chair Thomas did not have a problem providing tax relief to oil companies; however, he reiterated his concern that easier and cheaper production in other states would take money away from Alaska's economy. Mr. Aaron Schutt responded that the highest investment return was in existing fields and it was important to discuss what could be done to increase production in areas like Cook Inlet and

Prudhoe Bay that had seen little investment for many years. Investment decisions on items such as tertiary recovery in existing fields were related to tax policy. He expounded that development of infrastructure in places like North Dakota was more expensive and riskier than the production of oil on known fields.

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TARA SWEENY, SENIOR VICE PRESIDENT OF EXTERNAL AFFAIRS AND COMMUNICATIONS, ARCTIC SLOPE REGIONAL CORPORATION (ASRC), discussed that ASRC had been established pursuant to ANCSA in 1971. The corporation was headquartered in Barrow and had subsidiary offices in Anchorage and across the U.S. She relayed that ASRC was owned by 11,000 Inupiaq shareholders who lived in various villages in Alaska. The corporation was the largest locally owned and operated business in Alaska and had five diverse lines of business that included construction, resource development, government services, energy support services, petroleum refining and marketing. The corporation also operated a BIDCO financial lending service. She explained that ASRC Energy Services, Inc. was the largest Alaska based oil and gas services company, had over 3,000 employees across the state, and had the only Alaskan owned refining and fuel marketing operation in the state. The corporation worked with Alaskan businesses of all sizes across all economic sectors, had 4,000 employees working across the state, and approximately 6,000 working in the Lower 48. She communicated that ASRC represented a broad population with diverse political views, cultural experiences, and personal beliefs, who shared the goal of job protection and growth in Alaska.

Ms. Sweeny urged the legislature to reform ACES. She emphasized that the state needed a competitive tax structure to attract new investment and production on the North Slope and to put an end to the decline. She stressed that the state could not expect to attract new investments with the ACES tax rate that imposed double and triple the rates of Wyoming, Texas, and North Dakota. She vocalized that the oil and gas industry was the "bedrock" of the Alaskan economy. The industry accounted for approximately one-third of the state's economy and generated close to 90 percent of its general fund revenue. The industry also helped to provide jobs in other sectors as well throughout the state. She stressed that oil had peaked at nearly two million barrels per day in the late 1980s and currently the number had been reduced to approximately 600,000 barrels per day. She stated that at the current rate of decline the pipeline could shut down within a decade and that the loss of jobs and damage to the economy could be irreversible.

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Ms. Sweeny strongly believed that reform of ACES would increase investment and job opportunities. She accentuated that ACES reform was not about saving money for producers but was for employee job protection, job growth for future generations, and to create a sustainable future for the company. She delineated that ASRC Energy Services had heard from large and small, international and national companies that were excited about investing in Alaska, but were waiting for ACES to become more competitive. She shared that without ACES reform the clients would invest dollars elsewhere. She relayed that lost work opportunities were devastating at ASRC Energy Services and that the company continued to lose out on new work related to engineering, construction, operations, and maintenance. She acknowledged the complexity of the issue and stressed the importance of reform to attract new investment to the state.

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Representative Hawker wondered about the market that the Petro Star refineries had in Interior Alaska and who depended on them. He explained that management of the Trans Alaska Pipeline System (TAPS) had testified the prior week that the shutdown of TAPS and the refineries (one of which was owned by ARSC) would be a risk to health, life, and safety particularly in the Interior. Ms. Sweeny replied that there was a large client base that was dependent on the products that were sold and distributed by Petro Star. The refinery was located in North Pole and Petro Star had a significant presence in rural Alaska including the Bristol Bay and Koniag regions. She was happy to get the committee specific numbers.

Representative Hawker requested a market report that would provide detail of the statewide dependence on TAPS. Additionally, he wondered whether she could provide detail on why a tax change would bring a stronger and more robust economy to ASRC and its shareholders. He referred to her earlier testimony that the lost opportunities had been devastating for ASRC subsidiaries. He also discussed Co-

Chair Thomas' concern that the state may provide tax breaks only to have the money invested outside of Alaska. Ms. Sweeny answered that there had been conversations with potential investors and without ACES reform it would impact ASRC's ability to do more business in Alaska. The corporation employed Alaskans, shareholders, and other Alaska Natives and the impacts felt in rural Alaska were real in that jobs were a very good economic indicator and provided stability for the company's people.

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Representative Hawker understood that ASRC needed to protect corporate business plans, but surmised that Ms. Sweeny had corporate experience that led her to believe very strongly that investment dollars would come to Alaska in the event that ACES was reformed. Ms. Sweeny responded in the affirmative.

Co-Chair Thomas explained that his concern about money leaving the state was directed at "big money" and not at regional corporations. He was a regional corporation board member and he did not want money that would have filtered down to regional corporations to be taken away from Alaska. He emphasized that was not directing an attack at regional corporations.

Representative Doogan asked Ms. Sweeny for more detail about what she meant by "reforming ACES" and how she thought reform should take place. Ms. Sweeny responded that ASRC was supportive of HB 110 and of a climate that would increase certainty, stability, and jobs in Alaska. The corporation believed that the current system was not working and that the specific structure of the reform was at the purview of the legislature.

Representative Wilson wondered whether Alyeska was correct in its prediction that there would only be two weeks' worth of oil for the Interior in the event of a pipeline shutdown. Ms. Sweeney replied that she would get the numbers.

Representative Wilson asked whether ASRC wanted the effective date of the bracket provision in HB 110 to be changed to the current year. Ms. Sweeney verified that ASRC was supportive of immediate implementation of the bracket provision that had been discussed by Doyon Vice President, Mr. Aaron Schutt.

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Representative Gara wondered why ASRC thought that a reduction to the tax rate would increase oil activity when there had not been increased activity when the tax rate had been zero on most fields on the North Slope until 2006. He discussed that there were two different items being weighed, one of which was an increase to tax credits to incentivize exploration. He explained that the state could increase the credits to 50 percent and that companies would not get the money unless the exploration wells were built. He was more sympathetic to the tax credits compared to the second item that related to a reduction in the tax rate, which had not worked well in the past. He expounded that despite an oil price increase from $20 a barrel to $40 a barrel in 2004, two years later there had been less employment and less investment on the North Slope than there was currently. He elaborated that the production decline was approximately 40 percent between 1998 and 2006. He understood that it was difficult to speculate which change would alter the behavior of oil companies. Ms. Sweeney replied that from a service provider standpoint that the current system was not working. She could not speak directly to the decisions that were made by the industry, and although ASRC employed thousands of Alaskans and provided good services to the industry, it was losing out due to the current tax structure.

Representative Hawker was concerned that prior questions had presumed that big oil had quit exploring before ACES and that nothing had occurred during the ELF [Economic Limit Factor] tax period. He asserted that previous testimony had provided an extensive list of insignificant developments that had taken place during the ELF tax structure. He stated there had also been a significant number of businesses that had failed because of unsuccessful efforts.

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ERIC FOX, VICE PRESIDENT OF OPERATIONS, CAMP SERVICES, NANA MANAGEMENT SERVICES (NMS), discussed that NMS was a subsidiary of Nana Development Corporation (NDC). He explained that Nana Regional Corporation was owned by 12,500 Inupiat who had originated in Northwest Alaska. He began working for Nana 20 years earlier on the North Slope and he was proud to be an owner/shareholder of his employer. He relayed that NANA supported HB 110. The corporation believed that the bill would lead Alaska to be in a more competitive global position. The increased competitive environment would also increase oil and gas exploration and development. Increased oil and gas exploration would allow several of NANA's companies to compete for increased work. The corporation would then be able to help the Alaska economy grow with private sector jobs and could provide opportunities and employment to NANA shareholders. He discussed that unemployment was a problem in most of the 11 Northwest Alaska regions. He emphasized the importance of NANA's mission to improve the quality of life for its people by maximizing economic growth and protecting and enhancing its land.

Mr. Fox shared that NANA had a long history of serving the oil patch in Alaska and had started working on the North Slope not long after the passage of ANCSA. Nana Oilfield Services, Inc. had provided services for the industry for four decades and NMS had served the industry for over 30 years. In recent years NANA WorleyParsons had designed and engineered new North Slope facilities and NANA Construction had built modules for use on the oil fields. He provided a quote from NDC President, Helvi Sandvik regarding the state of the oil industry:

> The State of Alaska's taxes and the federal government's regulation oversight of Alaska's resource development industry are not good for business investment. Many of our companies serve the oil industry. Until the state changes its tax structure the oil industry will not spend the kind of money it has…to further develop Alaska's oil fields. The industry will look to other places in the world to spend its money, so our companies that serve the oil industry will continue to face tough times. If the companies we serve are discouraged from investing in Alaska that means less work for our businesses and our people.

Mr. Fox was honored that he had been named shareholder of the year at the NANA annual meeting the prior week and took his responsibility seriously. He stressed that ACES was having a negative impact on the interests of NANA, his region, and his people. He communicated that NMS had seen the direct impact of the lack of growth of the oil and gas industry in the state. The company had 2,400 employees and was among the 10 largest employers in Alaska. Over half of its revenues came from providing services to the oil and gas industry, including, food service, housekeeping, facilities management, maintenance, remodeling projects, wastewater management, logistics and security, and crime prevention and investigation, emergency medical response, leak detection, transportation, environmental and safety training, and temporary staffing. The company was committed to providing employment and career advancement for its shareholders. Nearly one quarter of the workforce was Alaska Natives and 12 percent to 14 percent were NANA shareholders. The company provided air transportation for NANA shareholders to travel to work on the North Slope. He emphasized that any contraction of the oil industry reduced jobs, earnings, and the ability for rural Alaska Natives to work close to home. As oil production declined in Alaska the oil producers were forced to demand cost cuts from suppliers like NMS. The company was faced with cutting its costs, including the benefits it provided to its employees. The lack of investment from the oil and gas industry was evident when NMS Camp Services recently lost a $5 million contract that it had serviced since 1989. He explained that the winning bid had cut employee wages from the existing contract by 20 percent and that NMS Camp Services could not have made that wage reduction in good conscience, especially in light of increased health insurance premiums.

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Mr. Fox shared that he had spent several days on the North Slope with NMS President Mary Quin the past November. Employees had communicated their fears and distress about greater health care costs and lower profit margins. He explained NANA was not the only company that had been impacted by the decline and that the oil industry had shed 1,700 jobs over the past two years.

JOE MATHIS, PRESIDENT, NANA PACIFIC, discussed that NANA Pacific was a subsidiary of NDC. He had been a NANA employee for close to three decades and was proud of the work that the company did for its shareholders and for its contribution to the Alaskan economy. He relayed that despite the vast oil resources remaining on the North Slope that production continued to decline at a serious rate. He stressed that North Dakota could surpass Alaska's production in three to four years. Without new oil coming on line, production would be down to approximately 250,000 barrels per day in 2020, which would cause serious operational challenges for the pipeline. The reduced exploration and work on the North Slope made it harder for NANA to help its region, shareholders, and Alaska. He observed that Alaska had once been the top oil producer in the nation, but it was currently number two and would soon slip to number four. He contended that investment dollars were bypassing Alaska for North Dakota, Alberta, Australia, and Russia. He discussed that there would be only one exploration well drilled on the North Slope in the winter of 2011 compared to approximately 170 active drill rigs in North Dakota. The prior week he had attended RES 2011, the largest conference of tribes and native peoples in the U.S. and had met with tribes that were based in North Dakota, Montana, and Oklahoma. He wished he could have been as excited about Alaska's oil field future as the tribes were about the growth prospects and new oil field development in their states. He emphasized that Alaska was not competitive compared to other oil regions and that the total marginal government take on a barrel of $100 oil was 82 percent, compared to 55 percent in Alberta and 43 percent in the Gulf of Mexico.

Mr. Mathis stressed that Alaska's investment climate was driving away business and it was necessary to reverse the trend. He stated that a new drill site would include goods and services, engineering, permitting, building roads and gravel pads, materials for local vendors, modules, power supply from source to drill site, backup power, transportation, operators, and fulltime maintenance. NANA had invested $20 million in the NANA Construction Big Lake facility where modules for the resource industry were built. He stated that an increase in Alaska's competitiveness would mean there would be direct work for NANA Construction to build modules. There would be 20 to 70 new jobs for residents in the Mat-Su Valley, Eagle River, and Anchorage. He discussed that the NANA subsidiary NANA WorleyParsons was an industrial engineering company that had been hurt by the downturn. He explained that NANA WorleyParsons directly benefited from new projects by oil and gas companies because of its role in the engineering and design of new facilities. When the company had new projects it hired new employees and helped the entire economy grow. He reported that the impact of ACES was currently hitting the state hard.

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Mr. Mathis elaborated that the combination of the recent recession and ACES had been devastating to the oil industry. He discussed that NANA WorleyParsons had peaked in 2008 with 675 employees and $115 million in revenue and was currently operating at about half that size. Highly qualified employees had left the state for more attractive career opportunities and were creating a "brain drain" in Alaska. He explained that senior designers were looking to learn about new software that was used in offshore industry and without change in the exploration action they would look to a future outside of the state. He voiced that other oil producing regions had recovered from the recession and that some areas were currently growing or booming. There were new projects occurring in Texas, Alberta, Australia, and throughout the Middle East; however, Alaska was no longer an attractive place to do business. He accentuated that investment in new projects took years and without action the way of life in Alaska would change dramatically. He highlighted four reasons why HB 110 would create jobs and increase production. First, the brackets for the progressive portion of the production tax would reduce one of the highest marginal tax rates in the world. The brackets would be similar to income tax brackets; therefore when the price of a barrel increased, only the incremental portion of the barrel would be taxed at the higher rate. Second, the bill promoted infield drilling with tax credits that were increased to 40 percent on the North Slope and to equal tax credits in the other parts of the state. Third, the bill calculated taxes on an annual basis of average prices and costs as opposed to volatile monthly calculations. Fourth, HB 110 allowed companies to take tax credits in one year instead of spreading them over two years. He emphasized that he had come to the state to help build the Trans Alaska Pipeline and did not want to see it torn down.

Co-Chair Stoltze related personal experience regarding his father's work at NANA Purcell Security. He expressed that the current discussion had been less about the details of

HB 110 and more about the story of the industry in Alaska and the economy.

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Representative Gara wondered whether there were producers in Alaska that were leaving the state to work in North Dakota. He observed that the committee had received very little information regarding development in North Dakota. He understood that the developers in North Dakota represented a different group that did small fields, used the fracking method, and used different technology and production than was used in Alaska. He did not believe there was a major overlap between the companies that were conducting business in Alaska and the companies in North Dakota; therefore, unless there was proof that companies were leaving the state for North Dakota, the idea that companies in Alaska were fleeing to North Dakota did not hold water. Mr. Mathis did not know which producers were taking business to North Dakota. He thought that ConocoPhillips may have been interested in working there, but that it would be necessary to get the answer from the producers. There were service companies that had not necessarily been leaving but had been sending operations to North Dakota. In an email received that day, the Mandan Tribe in North Dakota had asked Mr. Mathis whether he would be interested in providing them with oil field service work. He explained that North Dakota was working to attract industry and that he would hate to see the valuable expertise in Alaska leave the state. He elaborated that the expertise would be driven by the amount of work that was available and that it would move wherever it was needed.

Representative Gara asked whether it was understood that the actual tax rate paid by an oil company was much less than the marginal tax rate. He explained that the marginal tax rate at $100 a barrel only measured the tax rate between $99 a barrel and $100 a barrel. Mr. Mathis did not know.

Representative Neuman wondered how to show that there would be increased oil in the pipeline as a result of a change to the tax system. Mr. Mathis replied that it was very difficult to provide a guarantee regarding how oil companies would spend their money. There were no more guarantees on how companies would spend their money than there were on how and where Alaska residents would spend their Permanent Fund Dividend checks or how people would spend an energy check that was provided to offset high energy costs. He emphasized that there would not be a different outcome in production without a change.

Vice-chair Fairclough believed that committee member input was important; however, it was not helpful to make accusations that were based on personal opinion. She discussed that Cruz Construction was a service provider in Alaska that had experienced the secondary effects of the current taxation structure. She understood that it was subjective that the tax structure was the cause and effect; however, from the perspective of Cruz Construction it was the cause and effect. The company was repositioning all of its assets in North Dakota and the number of employees in Alaska had been reduced from two hundred down to ten and the number could potentially go down to three or four. She emphasized that the claim that there had been no evidence of loss of jobs on the North Slope represented a perspective. She encouraged committee members to ask questions that could be answered with fact. She thought the question regarding the difference in development strategies in North Dakota from Alaska was important. She explained that development in North Dakota was occurring on private property and that the same government regulations and permitting processes were not required.

Vice-chair Fairclough asked Mr. Fox how to reframe the conversation with Alaskans related to the difference between explorers and producers and who would be put to work under each scenario.

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Mr. Fox responded that exploration and production were outside of the services that NMS provided. The company was involved in the production phase with services such as security, camp services, facility management, etc. The jobs that NMS provided were frequently available to shareholders. There was a charter flight to Kotzebue that had previously operated once a week because there were enough jobs on the North Slope to call for a frequent flight; however, currently the flight operated every two weeks given the decline in jobs, particularly in Deadhorse. He explained that the shareholders were experiencing the decline first-hand and that the company had pumped millions of dollars in revenue into the NANA region that was whittling away. He emphasized that rural Alaska desperately needed the income.

Vice-chair Fairclough wondered whether the company had seen job loss from service organizations. Mr. Fox responded in the affirmative. He explained that exploration did not fall into the NMS realm and that the job loss was on the technical end.

Mr. Mathis added that NANA WorleyParsons had seen a 50 percent decline from 678 employees down to fewer than 300.

Representative Doogan referred to earlier testimony regarding 1,700 lost jobs in the past few years and wondered where the loss had occurred. Mr. Mathis responded that the job loss had occurred in the oil industry.

Representative Doogan asked for clarification that the job loss was within the oil industry in Alaska. The Department of Labor and Workforce Development (DLWD) data showed that oil and gas employment had gone from 12,900 in 2008 to 13,000 in 2009 and was projected at 12,700 in 2010. The department's numbers did not reconcile with the statement that 1,700 jobs had been lost. Mr. Mathis replied that he would provide the committee with the source of the 1,700 figure.

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Representative Gara explained that the committee had not heard any evidence that producers had been leaving the state for North Dakota and that he would be concerned to find out that they were. He discussed that there was evidence that completely substantiated Vice-chair Fairclough's point that contractors were looking for work wherever they could get it, whether it was in Alaska, North Dakota or both. Mr. Mathis replied that he did not mean to infer that producers had been closing up and leaving the state.

Vice-chair Fairclough remarked that the major producers were currently repositioning their assets and competing in a global market. She would continue to pursue her belief that because the state was competing with a global market, the tax structure was causing Alaska to lose out on its larger investments.

Representative Guttenberg had heard concern that the firm CH2M Hill had been consolidating work on the North Slope instead of outsourcing it. He wondered whether NMS had lost work to another company. He discussed that it was difficult to reconcile all of the different factors including the job loss at NMS and other companies and the DWLD numbers. Mr. Mathis replied that job loss had been a result of canceled projects and was not due to competition. He could not speak for CH2M Hill.

Representative Guttenberg was concerned that there was a conflict between different perceptions and some of the statistics provided by DWLD.

Representative Joule hoped that the state never lost sight of the importance that Alaska Native corporations played in the overall state economy.

Co-Chair Stoltze explained that although the topic was on oil tax, the discussion was an opportunity to help Alaskans understand that the corporations were important engines for the state economy.

11:20:40 AM

ISAAC NUKAPIGAK, PRESIDENT, KUUKPIK CORPORATION, discussed that the corporation was under ANCSA for the village of Nuiqsut located in the Colville River delta. Nuiqsut was eight miles from the Alpine oilfield processing facility and four miles from Nanuq, one of the Alpine oilfield satellites. The Alpine oil field was located on the western edge of existing oil and gas development on the North Slope and Nuiqsut was located within the National Petroleum Reserve Alaska (NPRA). He delineated that Alpine was discovered in 1992 by ARCO Alaska (now ConocoPhillips Alaska Inc.) and was the first oil discovered on ANCSA land. Many of the facilities were expected to be located on land owned by Kuukpik, the village corporation of Nuiqsut. Kuukpik had negotiated for environmental and other protection for subsistence on behalf of its shareholders and the residents of Nuiqsut. Kuukpik was able to reach an agreement to ensure that Alpine and future Alpine oil field satellites would be developed in a balanced and environmentally responsible way. The corporation was in favor of balance and environmentally responsible development on the North Slope. Kuukpik depended on oil and gas resources and many shareholders and their families worked in the oil industry. He explained that Joe Nukapigak, the former Kuukpik president and chairman of the board, would testify for Kuukpik and on the impact of ACES on jobs and the people of Nuiqsut. Kuukpik was in the business of providing services for the oil and gas industry on the North Slope and other. The corporation had two wholly owned subsidiaries that provided oil field services, including drilling, construction of ice roads, pads, roads, and pipeline. Kuukpik also had a business partnership that provided services that included geophysical, transportation logistics, catering, surveying, engineering, and oil field security.

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Mr. Nukapigak relayed that through its business ventures Kuukpik had firsthand experience with the oil and gas industry on a daily basis, including the wealth of the industry and the changing level of activity. He emphasized that the oil industry needed to move west to the NPRA in order to make and develop significant new discoveries onshore on the North Slope. One of the biggest problems that blocked development on the NPRA was the failure of the Army Corps of Engineers to issue a bridge permit for the Nigliq Channel on the Colville River for the "CD-5" or "Alpine West" project. He expounded that the Environmental Protection Agency (EPA) opposed the CD-5 bridge. He explained that without the bridge and other potential satellites, oil fields that ConocoPhillips had proposed were unlikely to be built in the foreseeable future, which would delay and prevent other oilfields in the NPRA to be developed. He relayed the bridge permits would do no good without the interest of the oil and gas companies. He stressed that the current ACES tax regime was a major obstacle to the oilfield development on NPRA. He stated that even if the permits for the bridge and three potential oil field satellites were obtained that Kuukpik oil field services companies had seen reduced activity levels across the North Slope. He believed that the ACES concept of sharing the upside of higher oil prices made good sense along with a substantial reduction to the state's severance tax when the price of oil reached $40 a barrel as it had in 2008. The concept of sharing was positive for oil and gas in the state; however, the profit share that the ACES tax regime took during high oil prices was too high. He opined that the development of oil and gas fields needed to be environmentally balanced and responsible. Similarly, the

State of Alaska needed to balance its desire for revenue from oil and gas development in the non-renewable oil resources with the business need of the oil companies that powered much of the state economy. A balance would be a win-win situation for the state and the oil industry. Without ACES reform and a more balanced structure, the state and the oil companies would eventually lose. He expounded that the oil companies would leave the state for better opportunities in the competitive global market.

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Mr. Nukapigak emphasized that without the oil industry the Inupiat people and their children could not move forward without risking their culture and lifestyle; therefore, Kuukpik supported HB 110 as a promising step in the right direction. He opined that ACES reform was the first step towards promoting an increased level of oil and gas exploration and development in NPRA and the State of Alaska.

JOE NUKAPIGAK, FORMER PRESIDENT AND CHAIRMAN OF THE BOARD KUUKPIK CORPORATION, discussed that he had been the president of Kuukpik when the Alpine oilfield had been discovered. The Alpine facility had been built partially on land that was owned by Kuukpik. He had been the chairman during the discovery, development, and completion of the first two Alpine satellite fields, Nanuq and Fiord. He had been involved in resource development, particularly in the oil and gas industry for over 20 years. He was currently the president of Nanuq, Inc., a wholly owned civil construction subsidiary of Kuukpik. He discussed that almost all of the residents of Nuiqsut were Kuukpik shareholders. Subsistence was the foundation of the Inupiat culture, but they were also in favor of balanced and environmentally responsible development of the North Slope's oil and gas resources. Many of the shareholders worked or had worked for the oil companies and the jobs helped residents to buy fuel, ammunition, whaling boats, snow machines, and equipment to pursue their subsistence lifestyle. Profits from Kuukpik's oil field services businesses helped the company pay dividends to its shareholders. He discussed that the majority of oil and gas exploration on the North Slope over the past 10 years had been in NPRA. He relayed that permits had delayed three ConocoPhillips satellite fields called Alpine West (also called CD-5), Lookout, and Rendezvous. The satellites would make it more economical to develop fields farther west through the use of existing pipelines, roads, and potentially other facilities. He explained that the Nuiqsut residents had seen gas flares from a number of exploration wells over the past 10 years as they traveled their hunting grounds in NPRA.

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Mr. Joe Nukapigak shared that Kuukpik believed that discoveries had been made by several oil companies, but no projects had been built in NPRA. There had been no exploration in NPRA over the past couple of winters because federal agencies did not allow companies to build facilities. He accentuated that permits for CD-5 were critical, but a reasonable and fair severance tax was also extremely important. Kuukpik had seen a decline in oil field activity and in jobs across the North Slope. The problem was not only a result of the economic downturn and permitting delays, but was due to the ACES tax structure as well. The state deserved a fair share of oil produced in Alaska; however, the current ACES share was too high at higher oil prices. The share of the profit that the state took away needed to be reduced to encourage onshore development in NPRA. The oil companies needed to be rewarded for the risk they took on new development. He emphasized that it was necessary to have a balance that worked for the state, the oil companies, and for Nuiqsut.

Representative Gara relayed that he and others had written letters to the Army Corps of Engineers to urge them to allow the bridge across the Colville River to go through. He wondered whether Kuukpik would feel comforted and open to a system that focused on increased credits instead of a reduced profits tax, provided that it was possible to show that the credits would increase development. He believed that the portrayal that some members of the legislature did not want to see expanded oil development was inaccurate. He explained that there were just different approaches. He relayed that there had been a discussion about increasing the exploration credit to 40 percent or 50 percent to address the decline in exploration. He discussed that ConocoPhillips and British Petroleum (BP) both reported Alaska profits and had made over $15 billion over the past four years. He was concerned that companies would spend the savings from a reduced tax outside of Alaska; however, with exploration credits the companies would only receive money for working in the state.

Mr. Isaac Nukapigak believed that it was likely that the state and the industry could reach a compromise. There were options that Kuukpik would need to explore. He remarked that he could not speak for the industry.

Representative Joule remarked that Kuukpik had been the only village corporation that the committee had heard from that day. He discussed that at one point local entities had not been on the same page related to the Colville River bridge but the federal government had been close to providing the permits; however, now that local entities were united, the federal government was deterring the process. He hoped that the project would be allowed so that NPRA and NPRA west development could occur.

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Mr. Isaac Nukapigak replied that Kuukpik had worked to unify the community and had looked at both economic and social areas. The leadership of the community of Nuiqsut and Kuukpik had passed a joint resolution to have Kuukpik take the lead on oil and gas negotiation for Nuiqsut. Kuukpik worked to make certain that oil and gas development continued and was done in the most environmentally practical way.

Mr. Joe Nukapigak added that when Prudhoe had first been discovered many years earlier that the residents of the North Slope had been skeptical. He communicated that over time the residents had learned how the oil and gas industry worked and their skepticism had changed to support. Kuukpik was the first village corporation that had owned part of Alpine. He explained that Alpine provided a significant benefit to Nuiqsut and to other Alaska communities.

11:45:32 AM

TOM LEONARD, COMMUNICATIONS MANAGER, CALISTA CORPORATION, read a prepared statement from Andrew Guy, Calista Corporation president and chief executive officer.

Dear Committee members:

Calista Corporation supports a more competitive environment for Alaska's oil and gas exploration and development. We support legislation encouraging the increase in oil production on the North Slope.

Development of Alaska's resources should be considered a long term investment of long term projects. A more balanced long term strategy could benefit Alaska and the nation in many ways, from the potential of a more consistent oil and gas supply, to steady employment for hundreds of Alaskans.

The current tax structure, "ACES," can be improved. CNBC's report last summer placed Alaska as the worst state in which to conduct business in the nation. The survey determined Alaska was ranked last for the fourth year in a row.

Additionally, higher well credits can help encourage new and existing field development. Alaska has a strong history of exploration, and the state laws and regulations need to better support continued exploration and business development in Alaska. The jobs oil and gas provides for our Shareholders enables them to work rotational schedules and still live a subsistence lifestyle.

Again, Calista supports utilizing our states natural resources in a safe and responsible way, while providing a more balanced business environment for the oil and gas industry. Calista thanks you for your time in this important matter.

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

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ADJOURNMENT
11:48:36 AM

The meeting was adjourned at 11:48 AM.