

**ALASKA STATE LEGISLATURE  
SENATE RESOURCES STANDING COMMITTEE**

March 2, 2012

3:34 p.m.

**MEMBERS PRESENT**

Senator Joe Paskvan, Co-Chair  
Senator Thomas Wagoner, Co-Chair  
Senator Bill Wielechowski, Vice Chair  
Senator Bert Stedman  
Senator Lesil McGuire  
Senator Hollis French  
Senator Gary Stevens

**MEMBERS ABSENT**

All members present

**OTHER LEGISLATORS PRESENT**

Senator Cathy Giessel

**COMMITTEE CALENDAR**

SENATE BILL NO. 192

"An Act relating to the oil and gas production tax; and providing for an effective date."

- MOVED CSSB 192(RES) OUT OF COMMITTEE

**PREVIOUS COMMITTEE ACTION**

BILL: SB 192

SHORT TITLE: OIL AND GAS PRODUCTION TAX RATES

SPONSOR(s): RESOURCES

|          |     |                                 |
|----------|-----|---------------------------------|
| 02/08/12 | (S) | READ THE FIRST TIME - REFERRALS |
| 02/08/12 | (S) | RES, FIN                        |
| 02/10/12 | (S) | RES AT 3:30 PM BUTROVICH 205    |
| 02/10/12 | (S) | Heard & Held                    |
| 02/10/12 | (S) | MINUTE(RES)                     |
| 02/13/12 | (S) | RES AT 3:30 PM BUTROVICH 205    |
| 02/13/12 | (S) | Heard & Held                    |
| 02/13/12 | (S) | MINUTE(RES)                     |
| 02/14/12 | (S) | RES AT 3:30 PM BUTROVICH 205    |
| 02/14/12 | (S) | Heard & Held                    |

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02/28/12 (S) RES AT 3:30 PM SENATE FINANCE 532  
02/28/12 (S) Heard & Held  
02/28/12 (S) MINUTE(RES)  
02/28/12 (S) RES AT 6:00 PM SENATE FINANCE 532  
02/28/12 (S) Heard & Held  
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03/01/12 (S) MINUTE(RES)  
03/02/12 (S) RES AT 3:30 PM BUTROVICH 205

**WITNESS REGISTER**

JEFF STEPP, Staff  
Senator Joe Paskvan  
Aide  
Senate Resources Standing Committee  
Alaska State Legislature  
Juneau, AK

**POSITION STATEMENT:** Explained the changes in CSSB 192(RES), version E.

MIKE PAWLOWSKI, Staff  
Senator McGuire  
Alaska State Legislature  
Juneau, AK

**POSITION STATEMENT:** Answered questions regarding an amendment to CSSB 192(RES), version E.

**ACTION NARRATIVE**

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**CO-CHAIR JOE PASKVAN** called the Senate Resources Standing Committee meeting to order at 3:34 p.m. Present at the call to order were Senators Stedman, McGuire, Stevens, Wielechowski, French, Co-Chair Wagoner and Co-Chair Paskvan.

**SB 192-OIL AND GAS PRODUCTION TAX RATES**

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**CO-CHAIR PASKVAN** announced consideration of SB 192 [CSSB 192(RES), labeled 27-LS1305\B was before the committee].

**CO-CHAIR WAGONER** moved to adopt CSSB 192(RES), labeled 27-LS1305\E.

**CO-CHAIR PASKVAN** objected for discussion purposes.

He also noted Senator Geissel, Department of Revenue (DOR) Commissioner Butcher, Deputy Commissioner Bruce Tangeman, and Chief Economist Stickle were in the audience.

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JEFF STEPP, staff to Senator Paskvan, explained the changes in CSSB 192(RES) version E. He said in addition to retaining the progressivity rates and the progressivity cap, the CS contains four significant additions to Alaska's oil and gas production tax statutes as follows:

- it rewards increased production as proposed in Amendment B.9
- it establishes a gross minimum tax
- it creates an oil information system
- it separates oil and natural gas for purposes of calculating the progressivity portion of the production tax

He explained that the CS lowers both the rate of progressivity and its cap. It retains the original PTV trigger of \$30, but changes the progressivity tax rate from .4 percent to .35 percent per dollar increase up to 50 percent (or approximately \$101.43). At 50 percent, the CS adds a second trigger lowering the .35 percent to .1 percent up to 60 percent (approximately \$201.43) of PTV. Version E also reduces the maximum tax rate of 75 percent to 60 percent. Initial calculations from the DOR indicate that this reduction in progressivity to the oil companies will result in decreased tax revenue to Alaska of approximately \$200 million to \$250 million annually. The goal is to return upside potential to industry at high oil prices to incentivize more production.

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MR. STEPP said the next component of the CS, rewarding increased production, was advanced last week as Amendment B.9. The purpose is to reward companies that increase their North Slope production levels from one year to the next, helping to increase the flow through TAPS. Companies that achieve this goal will earn a \$10 allowance on new barrels of oil they produce above the prior year. However, the allowance for incremental oil will not be applied to the PTV calculation for progressivity per Legislative Legal's advice.

He said this allowance should not be confused with the tax credit or a lowering of tax rates. It's a reduction in the PTV used to calculate production tax. So, if a company produced, for example, 100,000 barrels in 2012 and increased that by 110,000 barrels in 2013, that company would be eligible for an allowance on the new 10,000 barrels. The allowance would reduce their PTV by \$10 multiplied by the number of barrels of new oil produced. He said the allowance would not influence the tax rate itself and it would not count as a lease expenditure and isn't part of the calculation that determines average profits per barrel.

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To accomplish this, he explained that the DOR would determine the average daily state-wide production for each producer for the previous tax year. This figure would be adjusted by eliminating any day or days in which there was a significant slowdown in North Slope production or transportation (the adjusted average). This calculation would also exclude any new oil as a result of acquisition or mergers. For instance, if ConocoPhillips bought Pioneer it would not get a new oil allowance for the existing production at Oooguruk unless it increased production levels above those achieved by Pioneer.

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MR. STEPP said the next component of the CS establishes a gross minimum tax and was presented as Amendment B.13; it establishes a production tax floor of 10 percent of the gross value of oil at point of production for legacy fields in Alaska. The floor would apply only to fields that have already produced 1 billion barrels of oil and are still producing an average of 100,000 barrels a day. Prudhoe Bay and Kuparuk are the only fields that currently meet that definition. The vast majority of Alaska's oil production comes from these fields and most facilities associated with them were fully depreciated long ago. The amendment does not apply to new fields or smaller fields in order to avoid any potential that it could put new field development or development of smaller reservoirs at risk.

He explained that ACES currently has a production tax floor of 0 to 4 percent depending on the price of oil and that can be brought even lower by credits. This means the state could actually owe companies production tax in a low price environment (when at the same time it has a cash flow deficit and is struggling to pay for the most essential state services). This provision is intended to alleviate those concerns and doesn't allow legacy field producers to apply tax credits to reduce their production taxes below the 10 percent gross floor. And at \$70 the state may take in more with the 10 percent gross floor than it would with ACES.

Industry has said that ACES does not work for them in an extremely high price environment; conversely it does not work for the state and is not durable in a low price environment. Oil prices won't necessarily remain above \$100 forever, as history has shown them to be extremely volatile, and the new floor will ensure that Alaskans get some production tax for their oil even when prices are below \$50 per barrel. Just three years ago this month oil was selling for \$47 per barrel. Further, consultants

have said ACES needs to be durable in a wide range of price environments and this provision helps achieve that goal.

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MR. STEPP moved on to the oil information system provision that was advanced as Amendment B.16. Much information is confidential under law, but a considerable amount is public but scattered among several agencies and difficult to find. This provision begins the process of making information more available to policy makers, the public and oil and gas companies who may be seeking to do business in Alaska's oil fields.

This provision requires the Alaska Oil and Gas Conservation Commission (AOGCC) to develop an electronic petroleum information management system that will contain public information currently gathered by the commission as well as the Departments of Revenue, Natural Resources and Labor and Workforce Development. The system will consolidate available public oil and gas information that is currently scattered among the several agencies for the purpose of improving the administration of the oil and gas production tax and to facilitate exploration, development and production of oil and gas resources. As more information becomes publicly available it can be incorporated into the information system.

He said the information list in the CS is taken from a 2007 Gaffney Kline report that provided an overview of how the acquisition, distribution and publication of oil company data is handled in other oil and gas producing regimes. The legislation directs the departments that have control over the various aspects of the information to provide what is not confidential to the commission in a form suitable for distribution. It directs the AOGCC to develop and implement the system.

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MR. STEPP said the last change is what is known as the "decoupling" provision. The legislature's consultant, Pedro van Meurs, in the Joint Senate Resources and Finance Committee hearings on February 13 and 14, 2012 warned of deficiencies in the current ACES system and one was that the barrel of equivalent (BOE) concept results in "the nonsensical cross subsidization of gas" and would result in massive government revenue losses on oil production if incremental gas were to be developed at the same time. That would in turn impede gas project development. Dr. van Meurs said it is essential that any revision of ACES deals with this problem in advance and this

provision would permit adding gas terms to the package later or immediately without having to change oil terms again.

MR. STEPP explained that the CS separates oil and natural gas for purposes of calculating the progressivity portion of the production tax. The progressivity surcharges for oil in Cook Inlet and in-state gas would be calculated together but distinct from export gas instead of the current practice of combining oil and gas. The progressivity structure itself would be changed to conform to the rates set forth in the CS.

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MR. STEPP explained that currently oil and gas are calculated according to the combined British Thermal Unit (BTU) value of oil, and gas and oil and gas can and do have vastly different values on a BTU basis. Currently a BTU of oil is worth much more than a BTU of gas. Accordingly, once a major gas sale starts, overlaying the existing oil production the BTU value of the combined oil and gas would be much lower than it was for oil alone. This has been referred to as the "dilution effect" and could cause a significant reduction in oil taxes if a major gas sale occurred. The existing tax structure in conjunction with the inherent uncertainty of future oil and gas prices exposes the State of Alaska to significant financial risk were a major gas to occur. The structure also creates economic instability for entities looking to participate in the development and financing of a natural gas pipeline project in Alaska.

MR. STEPP said that removing the dilution effect will not result in any reduction in oil taxes from a major gas sale. The CS gives the DOR authority to adopt regulations to allocate costs between oil and gas with the added instruction that a method based on relative BTU barrel of oil equivalent should be considered. The effective date is January 1, 2013.

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SENATOR FRENCH asked where the decoupling provision came from.

MR. STEPP answered that the drafter, Mr. Bullock, was asked to incorporate HCS CSSB 305(FIN) from the 26th Alaska legislature - a bill that passed the Senate in 2010.

CO-CHAIR PASKVAN withdrew his objection and asked if there were any further objections.

CO-CHAIR WAGONER objected to say that on February 24 the Senate Bipartisan Working Group said they wanted three things out of

this bill: increased oil production, more jobs for Alaskans and sustainable state revenue over the long term. He didn't think this bill did any of them. This version\E was sent out at 10:23 last night they finally have decoupling language. No one on the committee knew about this. It had no public testimony or hearings in the last two years. The bill started out as two pages and it's now 21 pages long.

CO-CHAIR WAGONER continued that legislators have publicly patted themselves on the back that an open and transparent process has taken place as a result of this bill, but that isn't the case. Some amendments that were conceptually presented a scant week ago are included and others weren't. The bill has been heard in committee 21 times; of that, only one time has there been any meaningful dialogue and that is what they are doing today.

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CO-CHAIR WAGONER said he had planned to offer an amendment dealing with the tax holiday and received it today at 1:00 p.m.; it was completed by Legislative Legal at 10:56 p.m. on March 1. The bill was read across February 8, and 20 days later the Senate Resources Committee finally heard from the public on version B. As a result of that input according to his count there were 45 yeas, 96 nays and 15 not sures. Some of the amendments should receive modeling before moving from this committee. He finished by maintaining his objection to adopting version E.

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At ease from 3:56:09 to 3:57:29 p.m.

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CO-CHAIR PASKVAN asked for a roll call vote. Senators Stedman, Stevens, Wielechowski, French and Paskvan voted yea; Senators McGuire and Wagoner voted nay; therefore CSSB 192(RES), labeled 27-LS1305\E, was before the committee.

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SENATOR MCGUIRE moved Amendment 1, E.16 [old 27-LS1305\B.4].

27-LS1305\E.16  
Nauman/Bullock

**A M E N D M E N T**

OFFERED IN THE SENATE

TO: CSSB 192(RES), Draft Version "B"

Page 1, line 1:

Delete "oil and gas production tax"

Insert "tax rates applicable to oil and gas production when the average production tax value for a BTU equivalent barrel of oil and gas is more than \$30"

Page 1, line 3, through page 2, line 6:

Delete all material and insert:

"\* **Section 1.** AS 43.55.011(g) is repealed and reenacted to read:

(g) For each month of the calendar year for which the producer's average monthly production tax value under AS 43.55.160(a)(2) for each BTU equivalent barrel of the taxable oil and gas is more than \$30, the amount of tax for purposes of (e)(2) of this section is determined by multiplying the monthly production tax value of the taxable oil and gas produced during the month by the following tax rates, as applicable:

(1) if the producer's average monthly production tax value of a BTU equivalent barrel of the taxable oil and gas for the month is not more than \$42.50, the tax rate is 2.5 percent of the difference between that average monthly production tax value of a BTU equivalent barrel and \$30;

(2) if the producer's average monthly production tax value of a BTU equivalent barrel of the taxable oil and gas for the month is more than \$42.50 but not more than \$55, the tax rates are

(A) 2.5 percent on the first \$12.50 of monthly production tax value for each BTU equivalent barrel that is greater than \$30; and

(B) 7.5 percent of the monthly production tax value for each BTU equivalent barrel that is greater than \$42.50;

(3) if the producer's average monthly production tax value of a BTU equivalent barrel of the taxable oil and gas for the month is more than \$55 but not more than \$67.50, the tax rates are

(A) 2.5 percent on the first \$12.50 of monthly production tax value for each BTU equivalent barrel that is greater than \$30;

(B) 7.5 percent of the next higher \$12.50 of monthly production tax value for each BTU equivalent barrel; and

(C) 12.5 percent of the monthly production tax value for each BTU equivalent barrel that is greater than \$55;

(4) if the producer's average monthly production tax value of a BTU equivalent barrel of the taxable oil and gas for the month is more than \$67.50 but not more than \$80, the tax rates are

(A) 2.5 percent on the first \$12.50 of monthly production tax value for each BTU equivalent barrel that is greater than \$30;

(B) 7.5 percent of the next higher \$12.50 of monthly production tax value for each BTU equivalent barrel;

(C) 12.5 percent of the next higher \$12.50 of monthly production tax value for each BTU equivalent barrel;

(D) 17.5 percent of the monthly production tax value for each BTU equivalent barrel that is greater than \$67.50;

(5) if the producer's average monthly production tax value of a BTU equivalent barrel of the taxable oil and gas for the month is more than \$80 but not more than \$92.50, the tax rates are

(A) 2.5 percent on the first \$12.50 of monthly production tax value for each BTU equivalent barrel that is greater than \$30;

(B) 7.5 percent of the next higher \$12.50 of monthly production tax value for each BTU equivalent barrel;

(C) 12.5 percent of the next higher \$12.50 of monthly production tax value for each BTU equivalent barrel;

(D) 17.5 percent of the next higher \$12.50 of monthly production tax value for each BTU equivalent barrel; and

(E) 22.5 percent of the monthly production tax value for each BTU equivalent barrel that is greater than \$80;

(6) if the producer's average monthly production tax value of a BTU equivalent barrel of the taxable oil and gas for the month is more than \$92.50 but not more than \$105, the tax rates are

(A) 2.5 percent on the first \$12.50 of monthly production tax value for each BTU equivalent barrel that is greater than \$30;

(B) 7.5 percent of the next higher \$12.50 of monthly production tax value for each BTU equivalent barrel;

(C) 12.5 percent of the next higher \$12.50 of monthly production tax value for each BTU equivalent barrel;

(D) 17.5 percent of the next higher \$12.50 of monthly production tax value for each BTU equivalent barrel;

(E) 22.5 percent of the next higher \$12.50 of monthly production tax value for each BTU equivalent barrel; and

(F) 25 percent of the monthly production tax value for each BTU equivalent barrel that is greater than \$92.50;

(7) if the producer's average monthly production tax value of a BTU equivalent barrel of the taxable oil and gas for the month is more than \$105 but not more than \$117.50, the tax rates are

(A) 2.5 percent on the first \$12.50 of monthly production tax value for each BTU equivalent barrel that is greater than \$30;

(B) 7.5 percent of the next higher \$12.50 of monthly production tax value for each BTU equivalent barrel;

(C) 12.5 percent of the next higher \$12.50 of monthly production tax value for each BTU equivalent barrel;

(D) 17.5 percent of the next higher \$12.50 of monthly production tax value for each BTU equivalent barrel;

(E) 22.5 percent of the next higher \$12.50 of monthly production tax value for each BTU equivalent barrel;

(F) 25 percent of the next higher \$12.50 of monthly production tax value for each BTU equivalent barrel; and

(G) 30 percent of the monthly production tax value for each BTU equivalent barrel that is greater than \$105;

(8) if the producer's average monthly production tax value of a BTU equivalent barrel of the taxable oil and gas for the month is more than \$117.50, the tax rates are

(A) 2.5 percent on the first \$12.50 of monthly production tax value for each BTU equivalent barrel that is greater than \$30;

(B) 7.5 percent of the next higher \$12.50 of monthly production tax value for each BTU equivalent barrel;

(C) 12.5 percent of the next higher \$12.50 of monthly production tax value for each BTU equivalent barrel;

(D) 17.5 percent of the next higher \$12.50 of monthly production tax value for each BTU equivalent barrel;

(E) 22.5 percent of the next higher \$12.50 of monthly production tax value for each BTU equivalent barrel;

(F) 25 percent of the next higher \$12.50 of monthly production tax value for each BTU equivalent barrel;

(G) 30 percent of the next higher \$12.50 of monthly production tax value for each BTU equivalent barrel; and

(H) 35 percent of the monthly production tax value for each BTU equivalent barrel that is greater than \$117.50.

**\* Sec. 2.** The uncodified law of the State of Alaska is amended by adding a new section to read:

APPLICABILITY. Section 1 of this Act applies to oil and gas produced after December 31, 2012.

**\* Sec. 3.** The uncodified law of the State of Alaska is amended by adding a new section to read:

TRANSITION: REGULATIONS. The Department of Revenue may adopt regulations to implement this Act. The regulations take effect under AS 44.62 (Administrative Procedure Act), but not before the effective date of the provision of this Act implemented by the regulation.

**\* Sec. 4.** Section 1 of this Act takes effect January 1, 2013.

**\* Sec. 5.** Except as provided in sec. 4 of this Act, this Act takes effect immediately under AS 01.10.070(c)."

CO-CHAIR PASKVAN objected for discussion purposes.

SENATOR MCGUIRE explained that this amendment is "bracketed progressivity" and adds two top brackets - at \$105.50 to \$117.50 and \$117.50 and up - making it slightly more favorable to the state's take. Consultants have shown them that at particularly high cost development economics (what you're largely dealing with in Alaska) the CS doesn't move the needle far enough. They

showed that SB 192 runs along the line of ACES in the \$70 range of the decline curve and there isn't any significant change until \$140, and that is the range in which Alaska is missing development opportunities.

SENATOR MCGUIRE said when she voted for ACES she made an error and wishes she would have better understood progressivity. The 25 percent base rate was thoroughly vetted and she was "very comfortable" with it, but she did not understand just how high of a government take progressivity would mean at high oil prices. Amendment E.16 is designed to reduce progressivity into brackets much like an individual IRS return; it would equal out the government take and industry profit.

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She cited the spring 2007 forecast (the last one produced before voting on ACES) in which the DOR projected Alaska would be producing 807,000 barrels of oil/day in 2012, but today it's only producing 584,000 barrels.

Judge Gleason relied on data prepared by [Dudley Platt] and his forecasting is what she was citing now. She said she didn't believe in taxing our way to prosperity, but she knows we are in a decline and that it's an aging field. But she believed that tax reductions could incentivize development that would lead to production. As an example two years ago, SB 309 led to a renaissance in Cook Inlet and while they hadn't seen as much government take as a result, they have seen an injection of capital into the private sector. She wanted to emphasize this as the state moves forward; circulating dollars into the private sector will be key to our recovery in the future.

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Further, she said this progressivity reduction in E.16 does something else Dr. van Meurs talked about as one of the inefficiencies in the current ACES system that prices over \$140 barrel (high marginal tax rates) leads to irrational behavior. Companies will spend more money in an effort to try to reduce their overall tax rate, which could lead to what is referred to as gold plating.

SENATOR MCGUIRE said she recognized members concerns about industry pledging to invest \$5 billion on the North Slope, but she understands their limitations in their unit sharing agreement and other things and thinks they have made as strong a statement as they can. And she is prepared to trust them. She trusts that like all of Alaska they want to see these fields

succeed and these projects come on line. They want to argue in the board rooms in Houston that the system in Alaska is now more competitive and as a result that more capital should be invested here.

She used the simile of how she was taught to get out of a tail spin years ago in flight school that applies here. When she was told to go into a controlled stall she was terrified; every instinct told her she didn't want to do this. The teacher explained despite the urge to pull up that the very thing you have to do is point your nose down in order to regain control. To a certain extent the legislature is on a parallel track. They have seen production numbers decline and their instinct has been "to grab as much as we can." Consultants have also said this tax system is a harvest model.

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SENATOR WIELECHOWSKI agreed that members have deep philosophical differences on these issues. He opposed this amendment for a number of reasons, one is that it will cost the state billions of dollars per year. He said, "We're the board of directors of the State of Alaska. The Constitution says we're responsible for insuring we get maximum benefit for our resource..."

He explained that the state had 30 years of low taxation policy. It had a system called the economic limit factor (ELF) that allowed a 0 percent tax rate by 2006 on 15 out of 19 fields on the North Slope. The legacy fields paid a gross tax rate of around 12.5 percent. The philosophy for 30 years was low taxes will lead to more production.

SENATOR WIELECHOWSKI reasoned, "Well what happened to production during the 30 years of this low taxation policy we had? We went from 2 million barrels a day to 750,000 barrels a day. This was a failed policy. The policy simply didn't get us the results that we want." So, he strongly disagreed with going back to a policy that had been in place for 30 years and failed, and cost the state probably hundreds of billions of dollars.

SENATOR WIELECHOWSKI said during the period of 2000 to 2006 when ELF was in place (a 0 percent tax rate), production went down 8 percent per year; jobs and investment declined, too. Since passing ACES, jobs on the North Slope are at an all-time high and there aren't enough beds to accommodate all the employees that work up there (hot sheeting). They actually pay people \$125 per day so that someone else can sleep in their bed while they are out working. Unfortunately, a high percentage of workers are

not Alaskans. Investment is at an all-time high, both capital and operating. Every single year since passing ACES there have been all-time highs of investment.

He remarked that people say that everyone is going to North Dakota, but the number of companies on the North Slope has increased by 250 percent since passing ACES. More exploratory wells are scheduled this year than in decades on the North Slope. He hears that companies are doing terrible, that they can't make money on the North Slope any more. But look at the companies' income statements. They've had \$30 billion in profits on the North Slope in the four years since ACES has been passed. Senator Wielechowski said he is happy they are making record profits in Alaska, but as someone who is responsible for insuring that Alaska gets its fair share, they have a responsibility as well. He's thrilled that the companies made \$30 billion, but he can't see giving them billions more back.

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SENATOR WIELECHOWSKI said they hear people say Alaska is not a good place to do business. But when they modeled rates of return (IRR) under ACES they assumed that capital costs would go up 300 percent, but that didn't happen, and if you put your money in a bank today, you're lucky if you get 1 percent, but the IRR for infield drilling at Prudhoe Bay was 123 percent on \$80/barrel oil according to Gaffney and Kline, the company that was hired by the governor. He was happy they were making those high rates of return, but don't come back to Alaska and tell him that Alaska is not profitable and you can't make money here when all the numbers, all the objective evidence, show just the opposite.

The 2004 BP memo was shocking he said, saying Alaska's role in the company is to be a "cash cow." So they can make a lot of money here and spend it to grow their business elsewhere.

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SENATOR WIELECHOWSKI recalled that they just heard yesterday the \$5 billion in commitments is no commitment. They don't have all the agreements of all the parties for this \$5 billion. And breaking that down, the \$5 billion commitment, pledge, whatever - some of the projects have been in their plans of development for five years. He said he had asked the director of the Division of Oil and Gas to name a single project plan or development on the North Slope that is un-economic under ACES, and he couldn't name a single one. He has been asking for modeling for over a year, but he hasn't seen a single model of a field or a single development or a single exploration or

modeling of anything that has shown him there is a single un-economic project under ACES that would be made economic by HB 110 or a similar type of bill. He hasn't seen any data that shows it. He can't vote for a bill that gives back that amount of money when he hasn't seen modeling that does it.

Further, Senator Wielechowski said, the \$5 billion investment could be over a 6 to 10 year period; so that's really \$500 million a year. But the catch is that the state picks up 60 percent of the costs. So they are really getting \$200 million of investment and at the same time the state is giving back roughly \$18 billion (\$2 billion per year). "Is there a CEO in the world, is there a businessman in the world, a business woman in the world, that would accept that deal...? They'd get fired," he said.

CO-CHAIR WAGONER added that it's nice to have explorers on the North Slope and he is the one who did the legislation 10 or so years ago in SB 186 that brought a lot of them. At the same time he wasn't aware of what was really going on. It isn't the ability to drill and produce oil; it's that not one well that has been drilled this year or was drilled that year has put a drop of oil into the pipeline. We have zero increase in production in areas outside of the existing units and they aren't going to get any. Wells are being drilled and if hydrocarbons are found, they are trying to flip them and sell them to someone else and not produce them. The mistake was that the state wasn't requiring them to come to production. The exploration that is going on on the North Slope is to hold onto their leases, it's not about production.

[4:19:00 PM](#)

SENATOR STEDMAN commented that the amendment was well intended, but he opposed it mainly because it moves too much cash without further balancing the system out. The CS has a progressivity adjustment and it might need to be adjusted some more. They could tip it to the other direction at high oil prices, but the time is not ripe for this amendment.

SENATOR MCGUIRE said she appreciates their comments and reiterated that this amendment has two higher brackets (as opposed to the governor's bill) and it wouldn't take them back to ELF. It still ensures a higher state take than any other tax regime the state has had. But she agreed that more work needs to be done. She also commented that although it's true a lot of workers are on the North Slope, they are in exploratory wells

and maintenance operations, but the state wants people up there working on production.

CO-CHAIR PASKVAN maintained his objection and asked for a roll call vote. Senators McGuire and Wagoner voted yea; Senators Wielechowski, French, Stevens, Stedman and Paskvan voted nay; therefore the amendment failed.

[4:22:22 PM](#)

SENATOR MCGUIRE moved E.17 [old B.7]

27-LS1305\E.17  
Bullock

**A M E N D M E N T**

OFFERED IN THE SENATE

TO: CSSB 192(RES), Draft Version "E"

Page 2, line 1, following "tax":

Insert "**rate; relating to oil and gas production tax credits, including qualified credits for exploration, development and production**"

Page 4, line 29, through page 5, line 9:

Delete all material and insert:

"\* **Sec. 5.** AS 43.55.011(e) is repealed and reenacted to read:

(e) There is levied on the producer of oil or gas a tax for all oil and gas produced each calendar year from each lease or property in the state, less any oil and gas the ownership or right to which is exempt from taxation or constitutes a landowner's royalty interest. Except as otherwise provided under (f), (j), (k), and (o) of this section, the tax is equal to the sum of the annual production tax value of the taxable oil and gas

(1) produced from a lease or property not described in (2) of this subsection as calculated under AS 43.55.160(a)(1) multiplied by 25 percent, and the sum, over all months of the calendar year, of the tax amounts determined under (g)(1) and (p) of this section, as applicable; and

(2) produced during the first seven consecutive years after the start of sustained production or produced during the first seven years after the effective date of this subsection, whichever is later, from a lease or property containing land

that was not or previously had not been within a unit or in commercial production as of December 31, 2008, as calculated under AS 43.55.160(a)(1) multiplied by 15 percent, and the sum, over all months of the calendar year, of the tax amounts determined under (g)(2) and (p) of this section, as applicable; in this paragraph, "sustained production" has the meaning given in AS 43.55.025(1)."

Page 5, line 28, through page 7, line 5:

Delete all material and insert:

"\* **Sec. 7.** AS 43.55.011(g) is repealed and reenacted to read:

(g) For each month of the calendar year for which the producer's average monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) of a BTU equivalent barrel of taxable oil produced during the month, gas produced during the month from a lease or property in the Cook Inlet sedimentary basin, and gas produced during the month from a lease or property outside the Cook Inlet sedimentary basin and used in the state is more than \$30, the tax is calculated as follows:

(1) the amount of tax for purposes of (e)(1) of this section is determined by multiplying the value calculated under AS 43.55.160(a)(2)(A) - (E) by the tax rate calculated as follows:

(A) if the producer's average monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) of a BTU equivalent barrel of the taxable oil and gas for the month is not more than \$92.50, the tax rate is 0.4 percent multiplied by the number that represents the difference between that average monthly production tax value of a BTU equivalent barrel and \$30; or

(B) if the producer's average monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) of a BTU equivalent barrel of the taxable oil and gas for the month is more than \$92.50, the tax rate is the sum of 25 percent and the product of 0.1 percent multiplied by the number that represents the difference between the average monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) of a BTU equivalent barrel and \$92.50, except that the sum determined under this subparagraph may not exceed 50 percent;

(2) the amount of tax for purposes of (e)(2) of this section is determined by multiplying the monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) of the taxable oil and gas produced during the month by the following tax rates, as applicable:

(A) if the producer's average monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) of a BTU equivalent barrel of the taxable oil and gas for the month is not more than \$42.50, the tax rate is 2.5 percent of the difference between that average monthly production tax value of a BTU equivalent barrel and \$30;

(B) if the producer's average monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) of a BTU equivalent barrel of the taxable oil and gas for the month is more than \$42.50 but not more than \$55, the tax rates are

(i) 2.5 percent on the first \$12.50 of monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) for each BTU equivalent barrel that is greater than \$30; and

(ii) 7.5 percent of the monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) for each BTU equivalent barrel that is greater than \$42.50;

(C) if the producer's average monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) of a BTU equivalent barrel of the taxable oil and gas for the month is more than \$55 but not more than \$67.50, the tax rates are

(i) 2.5 percent on the first \$12.50 of monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) for each BTU equivalent barrel that is greater than \$30;

(ii) 7.5 percent of the next higher \$12.50 of monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) for each BTU equivalent barrel; and

(iii) 12.5 percent of the monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) for each BTU equivalent barrel that is greater than \$55;

(D) if the producer's average monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) of a BTU equivalent barrel

of the taxable oil and gas for the month is more than \$67.50 but not more than \$80, the tax rates are

(i) 2.5 percent on the first \$12.50 of monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) for each BTU equivalent barrel that is greater than \$30;

(ii) 7.5 percent of the next higher \$12.50 of monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) for each BTU equivalent barrel;

(iii) 12.5 percent of the next higher \$12.50 of monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) for each BTU equivalent barrel;

(iv) 17.5 percent of the monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) for each BTU equivalent barrel that is greater than \$67.50;

(E) if the producer's average monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) of a BTU equivalent barrel of the taxable oil and gas for the month is more than \$80 but not more than \$92.50, the tax rates are

(i) 2.5 percent on the first \$12.50 of monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) for each BTU equivalent barrel that is greater than \$30;

(ii) 7.5 percent of the next higher \$12.50 of monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) for each BTU equivalent barrel;

(iii) 12.5 percent of the next higher \$12.50 of monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) for each BTU equivalent barrel;

(iv) 17.5 percent of the next higher \$12.50 of monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) for each BTU equivalent barrel; and

(v) 22.5 percent of the monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) for each BTU equivalent barrel that is greater than \$80;

(F) if the producer's average monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) of a BTU equivalent barrel

of the taxable oil and gas for the month is more than \$92.50, the tax rates are

(i) 2.5 percent on the first \$12.50 of monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) for each BTU equivalent barrel that is greater than \$30;

(ii) 7.5 percent of the next higher \$12.50 of monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) for each BTU equivalent barrel;

(iii) 12.5 percent of the next higher \$12.50 of monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) for each BTU equivalent barrel;

(iv) 17.5 percent of the next higher \$12.50 of monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) for each BTU equivalent barrel;

(v) 22.5 percent of the next higher \$12.50 of monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) for each BTU equivalent barrel; and

(vi) 25 percent of the monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) for each BTU equivalent barrel that is greater than \$92.50;

(3) for purposes of this subsection, the average monthly production tax value calculated under AS 43.55.160(a)(2)(A) - (E) of a BTU equivalent barrel of taxable oil and gas is calculated by

(A) adding all of the monthly production tax values determined calculated under AS 43.55.160(a)(2)(A) - (E); and

(B) dividing the sum calculated under (A) of this paragraph by the total amount, in BTU equivalent barrels, of

(i) taxable oil produced by the producer during the month;

(ii) taxable gas produced by the producer during the month from a lease or property in the Cook Inlet sedimentary basin; and

(iii) taxable gas produced by the producer during the month from a lease or property outside the Cook Inlet sedimentary basin and used in the state."

Page 8, line 19, following "percent":

Insert ", or 15 percent, as applicable under AS 43.55.011(e),"

Page 8, line 20:

Delete "AS 43.55.011(g)"

Insert "AS 43.55.011(g)(1) or (2), as applicable"

Page 8, line 22, following "percent":

Insert ", or 15 percent, as applicable under AS 43.55.011(e),"

Page 9, line 1, following "percent":

Insert ", or 15 percent, as applicable under AS 43.55.011(e),"

Page 9, line 2:

Delete "AS 43.55.011(g)"

Insert "AS 43.55.011(g)(1) or (2), as applicable"

Page 9, line 4, following "percent":

Insert ", or 15 percent, as applicable under AS 43.55.011(e)"

Page 9, line 10:

Following "percent":

Insert ", or 15 percent, as applicable under AS 43.55.011(e),"

Delete "AS 43.55.011(g)"

Insert "AS 43.55.011(g)(1) or (2), as applicable"

CO-CHAIR PASKVAN objected for purposes of discussion.

[4:22:46 PM](#)

At ease from 4:22 to 4:24 p.m.

[4:24:13 PM](#)

SENATOR MCGUIRE explained that this is progressivity bracketed (without the two higher brackets) and it applies only to new fields. Existing production is expected to decline at 7 to 11 percent annually to just 336,000 barrels a day by FY2017. According to the fall 2012 revenue forecast Alaska would then need to bring on 200,000 barrels a day of new production just to maintain current production. She wanted them to remember that as they look at the system of incentives.

Amendment E.17 attacks this problem from a slightly different angle; it doesn't affect any current production. She doesn't see

it as a give back to corporations, but as a correction to something they over-reached on. It reduces the base tax rate to 15 for new fields outside existing units for seven years; it adopts a bracketed progressivity system similar to B.5 with a top bracket of 25 percent for the first seven years of sustained production and then those fields would revert to the regular ACES regime.

SENATOR MCGUIRE said she has heard from new explorers, in particular, who have explained how important changing ACES is for them. One company has secured a contract for development that would lead to 1,400 new Alaskan jobs that is specifically contingent on passage of ACES.

She was president of a group called the Pacific Northwest Economic Region during the same time [2007] that Alberta adopted a windfall profits tax. The net effect of that was that industry investment declined by 50 percent. Dr. van Meurs said the experience of Alberta which faces a declining conventional oil production like Alaska indicates that designing lower fiscal terms in the 50 to 60 percent range of government take for higher cost resources is a viable strategy to increase production. Once Alberta ratcheted back its tax regime they got back the business they had lost largely to places like Saskatchewan, which had taken advantage of the opportunity and incentivized its oil industry. Alberta came back after a competitiveness review and modified their system in 2009 to 2010; and the changes resulted in a rebound in investment from \$10.6 billion in 2008 to \$16 billion by 2011 and record land sales that surpassed previous records by over \$400 million.

SENATOR MCGUIRE said that Dr. van Meurs used Alberta as a model and went on to say the 60 to 65 percent government take for more costly new light oil resources as proposed in HB 110 and HB 117 is a reasonable level from an international perspective. Amendment E.17 adopts this level of government take for new undeveloped fields outside of existing units. To be fair, he said bracketed progressivity was a complicated approach and one in which they wouldn't know the full effects. He recommended other approaches which have been in amendments here and might be discussed in the Senate Finance Committee. She hadn't seen them modeled and hadn't heard commitments from industry, so she was going to rely on E.17 for now.

[4:29:30 PM](#)

SENATOR FRENCH asked why the amendment uses the date of 2008.

MIKE PAWLOWSKI, staff to Senator McGuire, explained that December 31, 2008 is the bright line that was drawn about commercial production not within an existing unit to distinguish between what the amendment is attempting to do, which is only to affect projects outside of the existing units.

SENATOR FRENCH asked if the amendment would apply to Prudhoe Bay, Kuparuk and Alpine.

MR. PAWLOWSKI answered no.

SENATOR FRENCH said he would be a no vote, but it comes closer than the previous one did. This is what they need to be focused on, but leaving out Prudhoe Bay is where a lot of oil can be moved. It's still one of the biggest reservoirs left in North America. A 1 or 2 percent production increase at Prudhoe Bay will swamp a lot of smaller new fields. He liked the idea because they must be focused on incentivizing new oil no matter where it comes from.

[4:31:42 PM](#)

SENATOR STEDMAN said he would oppose the amendment. It's on point in working on incremental production, but they need to be careful to not make the system too complex. The issue is still in the middle of the table.

CO-CHAIR PASKVAN maintained his objection and asked for a roll call vote. Senators McGuire and Wagoner voted yea; Senators Stevens, Stedman, Wielechowski, French, and Paskvan voted nay; so the amendment failed.

[4:33:17 PM](#)

SENATOR WIELECHOWSKI offered Amendment E.10.

27-LS1305\E.10  
Nauman/Bullock

**A M E N D M E N T**

OFFERED IN THE SENATE

TO: CSSB 192(RES), Draft Version "E"

Page 1, line 1, following "tax;":

Insert "relating to oil and gas or gas only leasing; requiring that a minimum work commitment be included in each oil and gas and gas only lease and that a proposed plan of development be included in an application for an oil and gas or gas only lease;"

Page 4, following line 28:

Insert new bill sections to read:

"\* **Sec. 5.** AS 38.05.180(h) is amended to read:

(h) The commissioner shall [MAY] include terms in a [ANY] lease that impose [IMPOSING] a minimum work commitment on the lessee to implement the plan of development submitted by the lessee with a bid for an oil and gas or gas only lease. The terms of the minimum work commitment must [. THESE TERMS SHALL BE MADE PUBLIC BEFORE THE SALE, AND MAY] include appropriate penalty provisions to take effect in the event the lessee does not fulfill the minimum work commitment. If it is demonstrated that a lease has been proven unproductive by actions of adjacent lease holders, the commissioner may set aside a work commitment. The commissioner may waive for a period not to exceed one two-year period any term of a minimum work commitment if the commissioner makes a written finding either that conditions preventing drilling or exploration were beyond the lessee's reasonable ability to foresee or control or that the lessee has demonstrated through good faith efforts an intent and ability to drill or develop the lease during the term of the waiver.

\* **Sec. 6.** AS 38.05.180(x) is amended to read:

(x) A lessee conducting or permitting any exploration for, or development or production of, oil or gas on state land shall provide the commissioner access to all noninterpretive data obtained from that lease; shall provide the commissioner access to all information necessary to perform an economic analysis under (ii)(2) of this section, including the capital, operating, production, and development costs and an estimate of total reserves; and shall provide copies of that data and information, as the commissioner may request. The confidentiality provisions of AS 38.05.035 apply to the information obtained under this subsection.

\* **Sec. 7.** AS 38.05.180 is amended by adding new subsections to read:

(hh) The commissioner shall require each bidder for an oil and gas lease or gas only lease and each lessee applying for an extension or renewal of an oil and gas lease or gas only lease to submit a plan of development for exploring, developing, and producing from the lease within the period of the lease or the

extension or renewal of the lease. The commissioner shall review each plan of development and determine if the proposed plan of development is reasonably expected to develop the lease in the best interest of the state. The plan of development shall be included in a lease along with penalties for failing to comply with the plan of development and other terms of the lease. A bidder may not be a "qualified bidder" for the purposes of (f)(1) of this section if the commissioner finds that the bidder has not submitted a proposed plan of development that is in the best interest of the state or that the person that submitted the plan of development is not reasonably capable of implementing the plan.

(ii) The commissioner shall

(1) review each oil and gas lease or gas only lease each year for the purpose of determining whether a lease is being developed in the best interest of the state, whether the lessee is complying with the plan of development applicable to the lease, and whether revision of a development plan, including the planned rate of development, would provide the maximum benefit to the people of the state;

(2) every five years, perform an economic analysis on each participating area and determine whether the participating area is capable of increased production in paying quantities over the current rate of production or plan of development;

(3) enforce the terms of each oil and gas lease or gas only lease, including imposing any applicable penalty or other remedy for noncompliance, within a reasonable time after finding that a lessee is out of compliance with the terms of the lease;

(4) submit a report to the legislature before the first day of each regular session that lists each oil and gas or gas only lessee that is found to be out of compliance and the action by the commissioner to bring the lessee back into compliance or to terminate the lease.

(jj) For the purposes of (hh) and (ii) of this section, a plan of development for a cooperative or unit under (p) of this section is the plan of development for a lease within the cooperative or unit, except where a different plan of development is established for a lease within the cooperative or unit.

(kk) For purposes of (ii) of this section,

(1) "participating area" means that part of an oil and gas lease unit area to which production is allocated in the manner described in a unit agreement;

(2) "production in paying quantities" means production in quantities sufficient to yield a return in excess of drilling, development, and operating costs."

Renumber the following bill sections accordingly.

Page 21, line 8, following "APPLICABILITY.":  
Insert "(a)"

Page 21, line 9:  
Delete "sec. 13"  
Insert "sec. 16"

Page 21, following line 12:  
Insert a new subsection to read:  
"(b) Section 5 of this Act and AS 38.085.180(hh), enacted by sec. 7 of this Act, apply to a proposed lease sale and the renewal or extension of a lease on or after the effective date of secs. 5 and 7 of this Act."

Page 21, line 13:  
Delete all material and insert:  
"**\* Sec. 21.** Sections 5 - 7 of this Act take effect July 1, 2013.  
**\* Sec. 22.** Except as provided in sec. 21 of this Act, this Act takes effect January 1, 2013."

CO-CHAIR PASKVAN objected for discussion purposes.

SENATOR WIELECHOWSKI said this is a pro development amendment and that he is in alignment with Senator Wagoner with the issue that one of the bigger problems on the North Slope is the leasing structure. This amendment requires companies before submitting leases to submit a minimum work plan. This avoids the situation where companies go out and bid on tracts of land with no intention or funding to actually ever go ahead and explore on it. Recently, a producer acquired 34 tracts of land on the North Slope and next week the Petroleum News reported they didn't have any plan to develop them; they wanted to see what would happen with the ACES tax structure. That is the wrong approach from his perspective.

When you bid on a lease in the State of Alaska you have a legal obligation to explore and if you find oil to develop it, Senator Wielechowski said. Unfortunately that is not the way the state's leases are being handled. They are being handled as options to explore and options to develop. They have learned through the short time of this amendment's existence that 25 percent of the state's leases, hundreds, having nothing going on with them. There have been no seismic studies, no permit applications nothing; they're idle.

[4:35:13 PM](#)

As the sovereign they can do a better job; this amendment requires minimum work commitments. It says if you want to acquire a lease in Alaska you have to have some minimum standards, some sort of a plan to come in and not simply use this as an option.

The second thing it does is require a review of existing leases and plans of developments. The goal is to see whether the lessees are complying with their current plans of developments and whether they should be revised. He said the Constitution says they have an obligation to get the maximum benefit for the resource and this would ensure that the state's land is being developed. It also requires the Department of Revenue and Department of Natural Resources to perform an economic analysis on each participating area to determine whether it is capable of increased production. Thirdly, it ensures the terms of existing leases are enforced. He thought this measure would get more oil in the pipeline with more exploration and drilling, and would better align the state with industry.

SENATOR WIELECHOWSKI said he recognized this amendment didn't have much vetting and needed more work and he was hopeful it would get a hearing. He withdrew the amendment.

[4:37:15 PM](#)

SENATOR STEVENS moved to report CSSB 192(RES), version E, from committee with individual recommendations and attached fiscal note(s) and forthcoming fiscal information.

CO-CHAIR WAGONER objected.

[4:38:08 PM](#)

SENATOR FRENCH said he wanted to speak to the objection. He said it's very difficult to move a bill like this through the committee. He congratulated the chair on doing that and

balancing the philosophical divisions and scheduling issues. He said the committee had put hundreds of hours of time into this both in the committee and in their offices.

He said this bill makes a significant concession to the oil industry in terms of progressivity and hundreds of millions of dollars. It hasn't meant with much "industry love," but that is a negotiating posture. "That is what the oil industry does." So, they are negotiating and the focus of this bill is about new oil and every person in this room is united around that concept. With that idea they can move forward.

4:40:29 PM

CO-CHAIR WAGONER stated that he talked to a lot of people about another amendment, but he decided not to offer it because he hadn't seen the modeling that goes with the bill. He expected that to be done in Finance, but he thought the tax holiday was the way to go. He said his staff worked many hours and days on the amendment, but without the modeling it's only half way there.

CO-CHAIR PASKVAN noted the objection and asked for a roll call vote. Senators McGuire and Wagoner voted nay and Senators Stevens, Wielechowski, French, Stedman and Paskvan voted yea; therefore, CSSB 192(RES), version E, moved from the Senate Resources Standing Committee.

4:42:40 PM

Finding no further business to come before the committee Co-Chair Paskvan adjourned the Senate Resources Standing Committee meeting at 4:42 p.m.