

HOUSE FINANCE COMMITTEE

April 7, 2013

1:34 p.m.

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CALL TO ORDER

Co-Chair Stoltze called the House Finance Committee meeting to order at 1:34 p.m.

MEMBERS PRESENT

Representative Alan Austerman, Co-Chair
Representative Bill Stoltze, Co-Chair
Representative Mark Neuman, Vice-Chair
Representative Mia Costello
Representative Bryce Edgmon
Representative Les Gara
Representative Lindsey Holmes
Representative Scott Kawasaki, Alternate
Representative Cathy Munoz
Representative Steve Thompson
Representative Tammie Wilson

MEMBERS ABSENT

Representative David Guttenberg

ALSO PRESENT

Michael Pawlowski, Advisor, Petroleum Fiscal Systems, Department of Revenue; Dan Stickel, Assistant Chief Economist, Department of Revenue; Bruce Tangeman, Deputy Commissioner, Tax Division, Department of Revenue; Representative Lance Pruitt, Sponsor; Johanna Bales, Deputy Director, Tax Division, Department of Revenue; Daniel Moore, City Treasurer, Municipality of Anchorage; Diane Blumer, Commissioner, Department of Labor and Workforce Development; Paul Dick, Director, Division of Employment Security, Department of Labor and Workforce Development; Cathie Roemmich, CEO, Juneau Chamber of Commerce; Barbara Huff Tuckness, Director, Legislative and Governmental Affairs, Teamsters Local 959; Paul Grossi, Alaska Pipe Trades and Iron Workers of Alaska, Juneau; Dennis Dewitt, National Federation of Independent Businesses, Juneau; Don

Etheridge, Alaska AFL-CIO, Juneau; Joe Balash, Deputy Commissioner, Department of Natural Resources.

PRESENT VIA TELECONFERENCE

Andy Rogers, Self, Anchorage; Rachel Petro, CEO, Alaska State Chamber of Commerce.

SUMMARY

HB 76 UNEMPLOYMENT; ELEC. FILING OF LABOR INFO

HB 76 was HEARD and HELD in committee for further consideration.

HB 129 OIL & GAS EXPLORATION/DEVELOPMENT AREAS

CSHB 129(FIN) was REPORTED out of committee with a "do pass" recommendation and with one new fiscal impact note from the Department of Natural Resources.

HB 193 MUNICIPAL TAXATION OF TOBACCO PRODUCTS

CSHB 193(FIN) was REPORTED out of committee with a "do pass" recommendation and with one new fiscal impact note from Department of Revenue and one previously published zero note: FN1 (CED).

CSSB 18(FIN) am
BUDGET: CAPITAL

CSSB 18(FIN) am was SCHEDULED but not HEARD.

CSSB 21(FIN) am(efd fld)
OIL AND GAS PRODUCTION TAX

CSSB 21(FIN) am(efd fld) was HEARD and HELD in committee for further consideration.

#sb21

CS FOR SENATE BILL NO. 21(FIN) am(efd fld)

"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; providing a tax credit against the corporation income

tax for qualified oil and gas service industry expenditures; relating to the oil and gas production tax rate; relating to gas used in the state; relating to monthly installment payments of the oil and gas production tax; relating to oil and gas production tax credits for certain losses and expenditures; relating to oil and gas production tax credit certificates; relating to nontransferable tax credits based on production; relating to the oil and gas tax credit fund; relating to annual statements by producers and explorers; establishing the Oil and Gas Competitiveness Review Board; and making conforming amendments."

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Co-Chair Stoltze discussed the meeting agenda.

MICHAEL PAWLOWSKI, ADVISOR, PETROLEUM FISCAL SYSTEMS, DEPARTMENT OF REVENUE, presented the PowerPoint presentation: "Fiscal Impact HCS CSSB 21(RES)." He noted that the analysis focused on a long-term policy goal to increase oil production in Alaska in the near-term and into the future.

DAN STICKEL, ASSISTANT CHIEF ECONOMIST, DEPARTMENT OF REVENUE, communicated that the department had identified 15 areas included in its fiscal analysis. The department would provide information about each of the areas and would conclude with a summary table showing the total fiscal impact of the bill over the upcoming 6 years compared to the fall 2012 forecast. He added that the fiscal note did not consider potential additional production that could be incentivized by the legislation. The presentation would also look at revenue sensitivity under Alaska's Clear and Equitable Share (ACES) and various versions of SB 21 specifically for FY 15.

Mr. Stickel pointed to slide 3: "1. Repeals Progressive Surcharge." Under the current ACES system the surcharge was the additional tax that applied when the production tax value was in excess of \$30 per barrel. The fiscal impact of the repeal ranged up to \$1.8 billion per year.

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Co-Chair Stoltze asked what the price of oil had been when ACES was implemented. Mr. Stickel believed the price had been in the \$60 range.

Representative Gara asked Mr. Stickel to repeat his comments about the impact of the elimination of progressivity. Mr. Stickel replied that the repeal of progressivity would have an impact of up to \$1.8 billion per year.

Mr. Stickel moved to slide 4: "Impact of Progressive Surcharge." The slide showed revenues from the ACES 25 percent base tax and on the progressive tax portion from FY 08 to FY 19. He pointed out that going forward the progressivity revenue was in the \$1.8 billion to \$1.5 billion range between FY 13 and FY 19. He noted that under the current rates the department forecasted larger revenues from the base tax than from the progressive tax.

Mr. Stickel turned slide 5: "Increases Base Production Tax Rate." He explained that under the legislation the base rate would increase from 25 percent to 33 percent (a decrease from 35 percent was included in the prior bill version CSSB 21). He elaborated that the change would bring a revenue increase to the state of up to \$875 million per year. He noted that the difference between the 33 percent and 35 percent base rates would be between \$200 million to \$250 million annually.

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Vice-Chair Neuman wondered how the elimination of progressivity would mean that oil and gas would be taxed separately. He had been told that removing a BTU equivalency section of the current law and eliminating progressivity would have a decoupling effect. He stated that progressivity was a multiplication function on the tax and the BTU equivalency functioned to ensure that a tax rate was followed for the producer's average monthly production tax.

Mr. Stickel responded that under the ACES system the progressivity surcharge factored in oil and gas and was brought down by the lower gas value. He expounded that when a producer had different commodity values there were varying impacts on the surcharge. He explained that by eliminating progressivity and taxing at a flat rate, gas

production would no longer change the tax rate. Under HCS CSSB 21(RES) the base production tax would be 33 percent for gas and 33 percent for oil.

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Vice-Chair Neuman stated that under ACES there was a standard allowable deduction on capital and operating expenses at the wellhead value. He clarified that the flat rate under the legislation would include the same components. Mr. Stickel agreed and stated that the underlying calculation of the production tax value was not changed in the legislation.

Co-Chair Austerman asked the department to review the material as clearly and simply as possible for the benefit of the committee and the public. He pointed to the information on slide 3 stating that the fiscal impact would be up to \$1.8 billion. He asked what the fiscal impact pertained to.

Co-Chair Stoltze requested simplicity and asked for other department staff to augment with detail on slides as well.

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Mr. Pawlowski explained that the progressivity surcharge was a tax that was added to the 25 percent base tax rate; its elimination would have a revenue impact on the state. The department endeavored to look at each revenue piece separately given that some provisions had fiscal impact to the state whereas others did not. He referenced slide 4 and stated that while progressivity was a large piece of revenue generated under ACES, the base tax rate also generated significant revenue. For example, under the FY 14 forecast the base tax rate was estimated to generate \$2.775 billion and progressivity was estimated at \$1.55 billion. He clarified that the slide showed the impact of revenue raised prior to the application of credits.

Representative Wilson asked whether \$1.8 billion would be subtracted [potential loss related to the elimination of progressivity] and \$875 million would be added as a result of the base tax rate increase from 25 percent up to 33 percent (slide 5).

Mr. Pawlowski answered in the affirmative.

Mr. Stickel expounded that the presentation included a summary table showing the collective fiscal impact of the provisions.

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Representative Gara looked at high revenues earned under ACES in FY 08 and FY 12 (slide 4). He wondered if FY 12 was the year that oil reached \$140 per barrel and if retroactive taxes had caused the high number in FY 08.

Mr. Stickel replied that oil prices had reached \$140 per barrel in FY 08. He detailed that the state had taken in close to \$1 billion in a specific month in FY 08.

Co-Chair Stoltze believed the retroactive provision had expired after two or three years.

Representative Gara asked if the high revenue in FY 12 was a result of high oil prices as well. Mr. Stickel replied in the affirmative; prices had consistently been above \$100 per barrel throughout FY 12.

Co-Chair Austerman pointed to slide 5 and asked for verification that the state's revenue would increase up to \$875 million annually [due to an increase in the production tax rate].

Mr. Stickel responded that the \$875 million revenue growth referred to an increase in the base production tax (based on the fall 2012 forecast), which would vary by year. He elaborated that the \$875 million reflected a change in the FY 16 forecast due to an increase in the base tax from 25 percent up to 33 percent.

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Mr. Pawlowski moved forward to slide 21: "Provisions in HCS CSSB 21(RES) and Their Estimated Fiscal Impact as Compared to Fall 2012 Forecast (\$millions)." He noted that the slide showed revenue impacts without a change in production. Provisions in HCS CSSB 21(RES) were numbered on the left of the slide. He believed it was pertinent to focus on FY 15 as it would be the first full fiscal year impacted by the legislation.

Co-Chair Austerman noted that slide 21 showed a reduction in \$875 million; whereas slide 5 showed an increase in \$875 million. He assumed the numbers were not the same.

Mr. Pawlowski replied that the number on slide 5 was related to the upper maximum in the table on slide 21. He elaborated that the elimination of progressivity would mean a maximum loss in revenue per year of \$1.8 billion (shown in the FY 17 forecast); the revenue increase of \$875 million was shown on line 2 in FY 16 (slide 21).

Co-Chair Austerman asked for clarification on the \$1.8 billion impact shown on slide 3. He wondered if the impact was a gain or loss in revenue to the state. He reiterated his earlier comment about providing clarity for the public.

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Mr. Pawlowski answered that the overall fiscal impact would be best described by the FY 15 analysis (tax was determined in a calendar year). He pointed to slide 21, line 1 showing that the elimination of progressivity would result in a loss of \$1.5 billion in FY 15 based on the fall 2012 forecast. Line 2 showed that an increase in the base tax rate to 33 percent would increase income by \$850 million in FY 15. Line 3 included an increase of \$700 million in revenue as a result of the limitation on credits for qualified capital expenditures for the North Slope (20 percent spending credit). He noted that line 3 only pertained to taxpayers who directly took credits to offset their production tax liability. Line 4 showed a minimal revenue impact for the net operating loss (NOL) credit increase from 25 percent to 33 percent. He detailed that the NOL credit was available to small explorers who were spending more than they were earning through production; the change would impact the operating budget where credits would go through the credit fund.

Mr. Pawlowski moved to line 5 that showed a \$25 million decrease in FY 15 revenue related to the gross revenue exclusion for oil production in new units and new or expanded participating areas. The provision eliminating the requirement for credits to be taken over two years would only have a fiscal impact in FY 14, which was projected at an increased \$250 million (reflecting credits that would have normally been taken in FY 15). He explained that the fiscal impact was limited to FY 14 because the obligations

created by companies spending in calendar year 2013 were an obligation to the state. He furthered that when a company made a qualified capital expenditure it earned a credit based on 20 percent of the expenditure; under current law the company had to divide the credit over a two-year period. He expounded that the intent of the legislation was to close out the fiscal obligation to the state.

Mr. Pawlowski continued on slide 21, line 7 showing no fiscal impact of an amendment to the community revenue sharing fund. He detailed that the item was linked to the corporate income tax receipts under the legislation, but it did not change the functioning of the program or the legislature's authority to appropriate. Line 8 pertained to a \$5 per taxable barrel sliding scale credit, which was based on the price of oil. The change would result in a reduction in state revenue of up to \$825 million in FY 15 based on the forecast production. He noted that if production was higher the credit rate would increase. Line 9 showed the qualified oil and gas industry expenditure credit, which was a corporate income tax credit for manufacturing or modification of tangible personal property (e.g. modules, truck and pipe improvements, and other). The impact of the credit was indeterminate, but had an upper range of \$25 million per year in decreased revenue. He detailed that the credit was limited to a company that paid tax and could only be used to reduce the company's individual tax liability.

Mr. Pawlowski addressed slide 21, line 10 pertaining to the reduced interest rate for late payments and assessments on most taxes; it showed an indeterminate fiscal impact with a possible \$25 million loss in revenue per year. Line 11 showed zero fiscal impact resulting from the removal of the 3-mile requirement for the Frontier Basin tax credit (the change had been made in the House Resources Committee). He communicated that the change showed no fiscal impact because the Middle Earth [Interior Alaska] exploration credit was included in the department's current production forecast. Line 12 addressed the extension of the fixed \$12 million small producer credit to 2022; the credit applied to companies producing less than 100,000 barrels BTU equivalent per day. He noted that there was no fiscal impact in the near-term; in FY 17 through FY 19 there was a loss in revenue projected as a result of new production from new qualifying entities. Line 13 referred to the 2016 required report to the legislature from the department. He

remarked that the report requirement was in lieu of the competitive review board. The report requirement cost would be absorbed by the department and would generate zero additional cost to the state.

Mr. Pawlowski moved to line 14 related to a requirement to consider joint interest billings in the audit process. The fiscal impact of the requirement was indeterminate; it was challenging for the department to determine how the requirement worked through the current audit process. Line 15 showed zero fiscal impact for Alaska Industrial Development and Export Authority (AIDEA) bonding authority to finance oil and gas processing facilities. He communicated that the total revenue impact to the state including all 15 items was projected at a loss of \$800 million to \$850 million per year.

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Representative Costello referred to prior testimony that a tremendous amount of revenue was brought in through the progressivity feature under ACES and that a significant portion of the revenue was distributed in capital credits. She had been told the number was approximately \$850 million. She wondered where the amount was reflected on slide 21 and noted the numbers seemed lower on the slide.

Mr. Pawlowski replied that there were two tiers in relation to companies eligible for the qualified capital expenditure credit. One tier included companies with a tax liability that used the credit to reduce their liability. The other tier included companies without a tax liability that were issued a credit; the credit came through the state's operating budget via the oil and gas credit fund. The impact on the operating budget was \$150 million in FY 15; whereas the combination of the two tiers equaled the \$850 million.

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Representative Gara stated that the base tax rate of 33 percent was misleading. He pointed to lines 2 and 8 and surmised that a 33 percent tax rate would generate \$450 million more than a 25 percent tax rate, but with the \$5 sliding deduction \$425 million out of the \$450 million was lost.

Mr. Pawlowski pointed out that the state would also gain \$300 million from the capital credit elimination. He noted the numbers pertained to FY 14 (slide 21). He detailed that when comparing the progressivity between the two, the number would be a negative \$525 million.

Representative Gara asked if the department could provide different variations of the data on slide 21 assuming various oil prices. Mr. Pawlowski directed attention to a chart on slide 30: "Production Tax Revenue, Less North Slope Refunded and Carried-Forward Credits." The data pertained to FY 15 only, given that it would be the first full year the legislation would impact. The impact was shown across a range of prices (\$50 to \$150) and for various versions of the legislation (from left to right: ACES was shown in blue, SB 21 was shown in red, CSSB 21(FIN) was shown in yellow, and HCS CSSB 21(RES) was shown in purple).

Representative Gara spoke to a ConocoPhillips projected production decline of 3 percent for legacy fields beginning in FY 17. He stated that the DOR forecast used a steeper rate of decline and requested data using a 3 percent decline from FY 17 going forward. Mr. Pawlowski was happy to work with the committee on forecasted decline. He noted that Conoco's 3 percent decline rate was limited to legacy fields under its operation (the Colville River and Kuparuk River units).

Representative Gara responded that an article using the 3 percent decline beginning in FY 17 included all of the legacy fields operated by Conoco, BP, and Exxon. He noted that Conoco estimated that its decline rate would be less than 3 percent beginning in FY 17 given its other oil fields.

Co-Chair Stoltze relayed that ConocoPhillips would have a chance to present to the committee in the future.

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Co-Chair Austerman looked at slide 21, line 2, which showed the 33 percent base tax. He pointed to FY 15 and asked if the \$850 million was representative of the 33 percent tax and what the number would be under the current 25 percent rate.

Mr. Pawlowski replied that the \$850 million was the difference between a 25 percent and 33 percent base tax rates.

Representative Munoz followed up on a question by Representative Costello related to how companies received the capital expenditure credit. She wondered why the entire amount was not reflected on slide 21.

Mr. Pawlowski replied that only looking at revenues brought in by tax payers would have ignored the obligation created by credits paid through the operating budget; therefore the items had been broken out to clarify the expenditure by the state. The total revenue impact (only factoring in revenue) would be underestimating the bill's fiscal impact by \$150 million. He remarked that it was difficult to represent the two items in the fiscal note.

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Representative Munoz asked for verification that there was an additional \$400 million or \$450 million not reflected in bill's bottom line impact to the state. Mr. Pawlowski replied that the total revenue impact was shown below line 15 on slide 21. The impact on the operating budget was shown below and included in the bottom line total fiscal impact on slide 21.

Representative Gara pointed to slide 21, line 8 and observed that the tax rate would not reach 33 percent until oil reached a price of \$150 to \$160 per barrel. Mr. Pawlowski agreed that the impact on line 8 did reflect an offset against the increase.

Vice-Chair Neuman asked what the cost of the gross revenue exclusion (GRE) would be to the state. He wondered what the cost to the state would be under the current standard allowable deduction system.

Mr. Pawlowski replied that the GRE impact was represented on slide 21, line 5. The estimated impact in FY 15 was approximately \$25 million. He noted that qualifying production had been strictly limited to new oil that had not been forecasted at present.

Representative Costello observed that the fiscal impact of the GRE was projected at \$50 million, but that it was also

listed as indeterminate. She wondered how the department had approached the estimate and the unknown factors involved. She assumed the worst case scenario had been used in the assumption.

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Mr. Stickel replied that the GRE took the forecasted production from the barrels and fields that would qualify for the new unit and expanded participating areas. He believed the number was 2 percent to 3 percent of the total production for FY 15. The department also looked at the forecasted production tax revenue with and without the GRE applied to the barrels for the qualifying fields, which was how the \$25 million cost had been determined for FY 15. He believed \$25 million for the HCS CSSB 21(RES) version of the bill was a good estimate; there was little uncertainty about which barrels would qualify. He noted that the prior version had included a more liberal definition about what qualified as new oil. The uncertainty had been higher under the prior version and the department had provided a range of revenue estimate.

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Representative Edgmon pointed to slide 21, line 7 and surmised that it was unlikely the community revenue sharing fund would exceed \$60 million given its tie to corporate income tax unless a large uptick in activity occurred.

Mr. Stickel replied that the total corporate income tax collections from oil, gas, and other corporations had been over \$500 million in each of the past eight years and collections were continued to be forecasted at over \$500 million per year for the length of the fiscal note. He added that the \$60 million threshold would easily be reached.

Representative Edgmon questioned whether there would be a decrease to the current \$60 million. He believed an additional \$20 million to \$25 million added to the revenue sharing program in the last couple of years. He was interested in the impact of tying revenue sharing to the corporate income tax provision of the bill.

Mr. Pawlowski believed it was illustrative to look at the progressivity piece (slide 4) because that was where

community revenue sharing dollars were softly dedicated to the revenue sharing fund. He discussed language that was up to 20 percent of the progressive portion or \$60 million to \$180 million. He furthered that given the \$500 million annual corporate income tax revenue the department was comfortable that plenty of revenue would be available for the revenue sharing program. He stressed that the legislation did not attempt to change how much would be appropriated to the fund. The intent was to locate a revenue stream that would meet the \$60 million to \$180 million to meet the obligation under the statute.

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Representative Edgmon relayed that an interactive presentation demonstrating how changing numbers around would impact the data. He wanted to be prepared for unexpected events such as decreases or increases in various areas. He referred to the importance of stress testing.

Co-Chair Austerman referred to his earlier question related to \$850 million. He clarified that the spring revenue forecast was based on the ACES 25 percent production tax. Mr. Stickel replied in the affirmative. He detailed that the spring forecast was based entirely on the current ACES production tax. He noted that slide 21 was based on the fall forecast.

Co-Chair Stoltze made a remark about tying government growth to production.

Mr. Pawlowski relayed that slide 21 was included on page 4 of a department fiscal note [FN10 (DOR), 4/8/13]. The department felt the slide integrated the bill's provisions without factoring in any changes to production or price. He referred to a presentation by Econ One from the previous day and to the importance of long-term decisions beyond the timeline shown on the fiscal note.

Co-Chair Austerman asked whether the fiscal note reflected the fall 2012 or spring 2013 revenue forecast. Mr. Pawlowski replied that the note reflected fall data; the department was currently working to update it for the spring forecast.

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Representative Edgmon referred to a news article discussing that the reduction of oil taxes should be thought of as an investment to increase production. He wondered if a projection of the potential increase in production resulting from the legislation would be provided to the committee. Mr. Pawlowski pointed to slide 22: "Production Scenarios." He cautioned that any methodology looking at increased production had flaws. The department had attempted to provide a scenario method that examined different production increase profiles.

Scenario A:

- New 50 Million barrel field developed by small producer without tax liability
- Peak production = 10 thousand bbls/day
- Development costs = \$500,000,000
- Qualified for GRE and NOL

Mr. Pawlowski relayed that ACES and the legislation used a net tax. He expounded that it was important to also consider the cost of reaching the production, which would have a fiscal impact. Scenario A represented the addition of one new 50 million barrel field.

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Mr. Pawlowski discussed Scenario B on slide 23: "Production Scenarios." He communicated that the scenario provided the most reasonable expectation for the near-term. He emphasized that the scenarios were not meant to be predictive.

Scenario B:

- Operators of existing units add 4 drill rigs to current plans
- Each rig adds 4,000 bbls/day in new production each year
 - Which each then decline at 15% per year
- Does not qualify for GRE

Mr. Pawlowski elaborated that it was important to factor in a decline rate when looking at oil production. He looked at Scenario C on slide 24: "Production Scenarios."

Scenario C:

- Operator of existing legacy unit builds new drill pad
- Development cost = \$5 billion
- Adds 15,000 bbls/day in 2014 increasing to peak rate of 90,000 bbls/day in 2018
- Does not qualify for GRE

Representative Holmes wondered about development costs associated with Scenario B. Mr. Pawlowski pointed to page 5 of the fiscal note [FN10 (DOR), 4/8/13] and relayed that the development cost for each well was estimated at \$20 million. The figure was on the high side of current cost on the North Slope, but he believed it was indicative of future development costs.

Representative Gara expressed a concern related to Scenario A (slide 22). He agreed that incentivizing new field production was necessary. He asked for verification that the GRE or the reduction in tax for a new field was 20 percent. Mr. Pawlowski replied in the affirmative.

Representative Gara asked whether the 20 percent GRE would reduce the base tax rate by more than 20 percent. Mr. Stickel replied that the 20 percent GRE was based on the gross oil value and was subtracted from the net value. He agreed that the impact of subtracting 20 percent of gross would be a reduction of greater than 20 percent of net. He explained that the exact percentage would depend on the price of oil.

Representative Gara addressed tax rates of future new fields. He stated that at \$110 per barrel oil companies would not pay a 33 percent tax due to the \$5 sliding scale [slide 21, provision 8]. He asked for a rough tax rate estimate for FY 15 before the GRE.

Mr. Pawlowski asked for clarification on which presentation Representative Gara was referencing.

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Representative Gara pointed to slide 21 of the DOR presentation. He noted that line 2 assumed a 33 percent tax rate, but the \$5 per taxable barrel credit meant that companies would pay less than 33 percent. He stated that

based on the chart the \$5 credit would mean a reduction of \$825 million from the \$850 million in gained revenue resulting from the base tax rate increase to 33 percent. He assumed that the actual tax rate on companies was closer to 26 percent or 27 percent with the inclusion of the \$5 per barrel credit. He wondered if the assumption was fair.

Mr. Stickel replied that at the forecast price the base tax increase from 25 percent to 33 percent was roughly offset by the per taxable barrel credit. He stated that the effective tax rate factoring in only the two provisions would be approximately 25 percent. He offered that the department could provide more specific calculations that encompassed all of the components.

Representative Gara pointed to the GRE, which subtracted roughly 35 percent from the 25 percent tax rate. He surmised that the tax rate would be approximately 17 percent when factoring in the GRE. Mr. Stickel answered that the amount was roughly in the ball park.

Representative Gara understood that companies needed to make up for sunk costs in the development of new fields, but he wondered if the department had thought about a time limit for the GRE. He did not know what the state would be able to fund if it had to live off of a 17 percent tax rate.

Mr. Pawlowski responded that a time limit on the GRE had been discussed in multiple committees; the department was concerned that it could create distorting effects on behavior. Specifically, how investment behavior would change if taxes were increased at the end or partway through the useful life of a well. The department was more comfortable with the more narrowly defined definition of new oil in the current bill. He elaborated that DOR did not see all of the new oil in the foreseeable future coming from GRE eligible barrels because it did not apply to the basic legacy production. He relayed that Mr. Stickel would speak to the forecast related to non-GRE eligible production.

Representative Gara understood that the GRE did not apply to everything. He discussed areas that would qualify for the GRE including new geological units in legacy fields, Umiat, Nakiachuk, Ooguruk, CD5, and other oil. He stressed that the provision would apply to a significant amount of

oil. He wondered if the state could fiscally sustain a 17 percent tax rate on the oil that would be included.

Mr. Pawlowski replied that the department had looked at what the state could afford to offer in credits particularly when it would not receive equal royalty into the future. He believed CD5 was largely on non-state land; the state paid through the credits and the deduction in ACES. He furthered that the state invested, but did not have the other components to provide the revenue to pay back. The department was concerned about the state not receiving the full royalty from the production and paying for it upfront. The administration was more comfortable with inspiring increased production in a way that did not have the state as invested in the upfront development, particularly when there was not the full balance of the royalty to support the state.

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Representative Gara believed that the ACES tax system would be eliminated in the near future. He asked about the pros and cons of a significant amount of new oil being taxed at a rate of approximately 17 percent and approximately 25 percent. He wondered why a 7-year to 10-year time limit on the lower tax should not be imposed.

Mr. Pawlowski answered that when incentives changed behavior also changed. He stated that the concern was related to how tax increases would impact declining production; costs would rise and increased taxes may cause incentive to shut in the production. The fear was that the change would discourage production in the future.

Representative Kawasaki asked if the production scenarios provided were likely and how they were developed (slides 22 through 24).

Mr. Pawlowski replied that the scenarios had initially been developed based on how something works without trying to be predictive. He stated that predicting the magnitude of the change was very difficult. He furthered that each scenario was a realistic concept, but they were intended to be illustrative. He pointed to Scenario B and relayed that [operators of existing units] adding 4 new drill rigs was not necessarily realistic. The department wanted to avoid doing a direct correlation between increases in spending

and a direct percentage increase in production. He remarked that it cost money to develop oil, production happened, and then production declined; the items needed to be built into a model given a net system in order to provide a realistic picture for policy makers.

Representative Kawasaki believed there would be more value to the scenarios if they were in a current development plan under the Division of Oil and Gas.

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Mr. Pawlowski replied that the department had worked with its economic research group to go through current DOR data to get ideas on cost, development, and projects and had built the data into the models. He relayed that the models were not based on any individual opportunities.

Representative Kawasaki wanted to ensure that the public understood that the scenarios were illustrative in nature.

Mr. Pawlowski stressed that DOR had attempted to move away from anything that was not indicative of what actual developments and projects would look like. The intent was to produce something reasonable to show the public related to the types of production.

Representative Holmes referred to the CD5 oil field. She pointed to the department's concern that under ACES the state may not collect royalties on developments off of state land; therefore, production tax would make up the entire revenue for the state on those areas. She furthered that in the existing system there was interplay of the state paying credits and the way the tax ran; she noted the state could end up under water. She asked how the situation would look under the proposed legislation and whether the state would be on safer ground.

Mr. Pawlowski replied that the removal of the buy-down effect had the largest impact. He elaborated that under the net system the state support for company spending was at the 25 percent rate plus the buy-down effect. He remarked that PFC Energy and Econ One had talked about state support for a project in the 80 percent range. The spending was different under the current system because it was limited to the basic tax rate (33 percent in the current bill); for an existing company developing a field, the state supported

at 33 percent. The state would take a production tax equivalent to the tax rate minus the GRE effect and the per barrel future credit. He furthered that the scenario was different than the buy-down effect and the capital credits that came out up front in the current tax system. He stated that there would be less potential for the state to go negative in the situation than there was under ACES. He referred to the decoupling effect and a previous PFC Energy presentation. He detailed that the impact to the state could be negative if a high value resource such as conventional oil was combined with a low value resource like viscous or high cost oil; the proposed system would not create the same effect, but it was primarily linked to the buy-down effect and not the credit structure. Under the current system moving into the field, a company would have the ability to write off expenditures against its taxes and to receive 33 percent support. The company would receive a per barrel production credit and the GRE for new fields. The department saw the royalty system being dramatically different in comparison to the current system.

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Representative Wilson asked if the state could continue to fund its budget with oil as the main resource. She observed that oil is not a renewable resource and believed a change needed to be made to stretch its production lifespan out in Alaska.

Mr. Pawlowski focused on the power of production. He referred to various presentations by departments showing that Alaska was resource rich; approximately 3.5 billion barrels of oil remained in the legacy fields and an additional 3 billion barrels were waiting to be discovered. He explained that roughly 10 percent of the resource needed to be developed to continue to drive the revenues seen under ACES with forecasted declines. He stated that in the long-term the issue was about production being able to sustain vital revenues to the state. He noted the importance of discussing the relationship of state revenues and the value being created. He pointed out that the state received revenues in multiple ways in addition to the production tax. The scenarios provided in the presentation looked at production compared to the current system. He suggested looking at the scenarios as underestimates. He wanted to focus on what the production could do to drive

the long-term sustainability of Alaska as opposed to looking at other revenue sources.

Representative Wilson understood that Alberta had recently changed its tax structure. She wondered if the change had made a difference. Mr. Pawlowski replied that DOR would provide the committee with benchmarking data from prior presentations that showed a dramatic increase in investment and production in Alberta. He noted that Alberta was currently experiencing some significant challenges due to low oil prices caused by stranded production.

Representative Wilson remarked that Alaska could look to other locations that had experienced similar issues to gain information about outcomes.

[2:51:54 PM](#)

Representative Gara referred to the possibility that the Alberta tax cut had raised the value to equalize the offset. He relayed that the province was facing \$2 billion to \$3 billion budget deficits. He stated that when too much was spent on tax breaks it was possible to lose money.

Mr. Pawlowski referred to a Wall Street Journal article from the past December that indicated there was oil at \$50 per barrel if tankers were available to transport it. He stated that there was a significant amount of oil produced in Alberta with very little infrastructure to transport it. He discussed various pipeline proposals. He understood that the increased production was largely due to the decline in price. He agreed that Alberta was facing a fiscal deficit.

Mr. Pawlowski continued to discuss Scenario C on slide 24: "Production Scenarios." The scenario included a large drill pad development with multiple wells, increased production, and billions of dollars in spending. He furthered that the scenario was an aggregate of the small field, the rigs, and the addition of the large pad. He moved to slide 25: "Production Profiles of Production Scenarios." The slide illustrated production numbers associated with Scenarios A through C. He pointed to FY 14 and noted that the blue bar to the left represented forecasted production; Scenario A did not add new oil, Scenario B increased production from 539 to 555 thousand BoPD, Scenario C increased production to 570 thousand BoPD. The chart provided data for FY 14

through FY 19 including decline curves with production layered on top.

Representative Gara asked whether actual projects had been identified under Scenario C that would go online as a result of the bill. Mr. Pawlowski answered that the scenarios were hypothetical based on the department's understanding of the type of spending that would occur. The information was intended to be illustrative of realistic elements that could occur.

[2:55:46 PM](#)

Mr. Pawlowski discussed slide 26: "Projected Revenues under Production Scenarios at \$90/Barrel ANS." The slide showed rounded unrestricted general fund revenue at various prices for the different production scenarios. The goal was to present the sensitivity level of a new revenue system on production. The chart provided a time limited (FY 14 through FY 19) illustrative scenario based on production figures shown on slide 25.

Mr. Pawlowski turned to slide 27: "Projected Revenues under Production Scenarios - at \$100/Barrel ANS." The bar in black on the far right showed ACES at the forecast production (other scenarios were shown for comparison). He pointed to Scenario B in FY 16, which showed that \$5 billion would be raised under the proposal and \$5.2 billion would be raised under ACES.

Representative Gara recalled testimony that it would take roughly seven years from the start to bring new production online. He wondered why the chart showed new production coming online within three and four years.

Mr. Pawlowski replied that adding a new rig to the legacy fields could offer near-term opportunity and provide a quick turnaround in production. He reiterated that the slides were illustrative. He furthered that adding a new rig could be done quickly; therefore, it was not GRE eligible under the analysis.

Representative Gara asked for verification that there were no commitments from any company that developments would occur as a result of the bill. Mr. Pawlowski responded that the oil industry was better equipped to answer the question.

[2:58:43 PM](#)

Representative Costello observed that Scenario C preformed the best. She asked the department to carry the analysis beyond FY 19. She stated that the bill had a short-term cost with the hope of a long-term gain. Mr. Pawlowski replied that there were various requests that the department could work with committee members on in order to provide the desired information.

Mr. Pawlowski moved to slide 29: "Projected Revenues under Production Scenarios - at Forecast ANS Price." The slide showed how sensitive the scenarios were to moderations of the decline curve to potentially create revenues that could offset the revenue reduction under ACES.

Representative Edgmon discussed department comments that U.S. oil production was at historic high levels. He noted that production was increasing globally as well. He wondered if a lack of infrastructure would provide a limitation on the production scenarios.

Mr. Pawlowski replied with a reference to work done by Econ One related to how much resource needed to be developed over the long-term. Econ One had looked at what would happen if Alaska trended along with its peer group following 2006; it had examined what spending would be like at present and how much resource there would be. Econ One had also looked at the relationship between government take and potential drilling and how many wells would need to be developed over what period of time. He stated that when considering the longer-term, it was necessary to look at the opportunity to exceed the break even. He furthered that the availability of capital as opposed to infrastructure was the bigger question; whether companies had the capital to reallocate quickly to develop resources in Alaska. He encouraged members to ask the industry questions about its ability to reallocate capital. He expounded that the change would not happen immediately, but the attractiveness of the tax system would make companies decide to reallocate capital to Alaska to be competitive.

[3:04:17 PM](#)

Representative Holmes discussed slide 21 and the difference between an impact on revenue and on the operating budget.

She pointed to slides 26 through 29 that showed projected revenues under various scenarios. She asked whether the slides also considered the impact of credits paid out under the existing system on the state's operating budget.

Mr. Pawlowski believed the revenue projections factored in the credits that would be paid out.

Representative Gara queried what 5.5 stood for in FY 19 (slide 29). Mr. Pawlowski answered that the figure was \$5.5 billion in GFUR [General Fund Unrestricted Revenue]; the bars represented revenue forecasts under the various scenarios.

Representative Gara referred to testimony by the major oil companies that technology was preventing the production of massive amounts of heavy oil in Alaska. He recalled a BP testifier who had said that the issue was technological and not fiscal. He stated that Conoco had said it planned to increase production, which would decrease its rate of decline to approximately 3 percent. He was concerned that the department was applying a 17 percent tax rate to new oil, which was likely to be produced under the current ACES system anyway. He was worried the state would unnecessarily incentivize some items.

[3:07:16 PM](#)

Mr. Pawlowski replied that it was related to what the state assumed would happen. He agreed that Conoco had made comments about its specific production and decline rate. He addressed the question about new oil and what would happen and looked at projects that were on the horizon, but did not happen (e.g. Liberty). He surmised that the root question was about relying on the revenue forecast to determine what would actually happen in the future and using that to define new versus old oil. The department was concerned that much of what was projected to occur under ACES would not occur. He pointed to testimony from Ken Thompson (of Brooks Range Petroleum) that the company had been to over 200 potential investors to pitch its 40 million barrel project under the current system; it had been unsuccessful and had asked the state to finance the project.

BRUCE TANGEMAN, DEPUTY COMMISSIONER, TAX DIVISION, DEPARTMENT OF REVENUE, relayed that the department had

incorporated information it learned from producers about expected decline rates into its fall revenue forecast (2012 Fall Revenue Forecast, page 43).

Co-Chair Stoltze referred to a phrase "we're not fine with decline."

Mr. Pawlowski agreed. He could provide committee members with a transcript of the Conoco analyst presentation. He added that the company had included that it saw an opportunity to reverse the decline if tax reform occurred. He pointed to the opportunity of production to provide a long-term sustainable base for the state.

[3:10:29 PM](#)

Vice-Chair Neuman referred to slide 29 and the committee's discussion the prior day on well amortization running at about five years. He wondered whether the value resulting from the potential addition of four wells per year was included in FY 19.

Mr. Pawlowski replied in the affirmative. The rig drilling under Scenario B would cost \$20 million per year; the money would be spent up front and the production would come on and decline within the model. He added that 1,000 barrels per day had been used based on the current average productivity of a well in the Prudhoe Bay unit.

Mr. Pawlowski pointed to slide 30: "Production Tax Revenue, Less North Slope Refunded and Carried-Forward Credits." The slide showed the fiscal impact of ACES and various versions of the legislation on production revenue for FY 15.

Mr. Stickel explained that slide 30 illustrated the total impact of ACES and various versions of the legislation on production revenue for FY 15 including credits paid out. The amount of expected credit refund payments for the North Slope under each of the tax systems had been subtracted from the total production tax number. There were carry-forward credits at \$50 per barrel in excess of the tax liability for major producers. He noted that the slide only looked at major provisions of the bill; an assumption for the corporate income tax and the reduced interest rate for late payments or assessments had not been included, which represented an impact ranging from \$0.00 to \$50 million.

3:13:46 PM

Representative Gara asked which fiscal year slide 30 pertained to. Mr. Stickel responded that the chart pertained to FY 15.

Mr. Pawlowski moved to slide 31: "General Fund Unrestricted Revenue, Less North Slope Refunded and Carried-Forward Credits." The slide related to FY 15 and attempted to incorporate other sources of state revenue outside of the production tax including royalty, property tax, and corporate income tax; it included the impact on revenue at oil prices ranging from \$50 to \$150 per barrel.

3:15:16 PM

Representative Gara hoped to see the state to receive a more substantial share of the revenue when oil prices were high and oil companies were making record profits. He did not believe the state would have sufficient revenues to fund schools and other projects over the next 10 years. He wondered about an option that would allow the state share in the benefits when oil prices were high. He asked if DOR had modeled a scenario that would provide the state with a more substantial share as oil prices increased. He suggested an increase in revenue to the state when companies made \$50-plus per barrel profit. He referred to a proposal the prior year to include a stair-stepped progressivity feature and wondered if the administration had considered it as a possibility.

Mr. Pawlowski replied that under the legislation the effective tax rate and government take increased as prices rose. He stated that whether the bill increased the government take to levels preferred by committee members was a policy call the administration was willing to work on with the legislature. He furthered that the state's share increased with higher prices without the problems associated with the progressivity mechanism.

Mr. Tangeman stated that if the current decline path continued the state would be limited in its ability to fund basic services 5 to 10 years in the future. He pointed to page 43 of the 2012 Fall Revenue Source Book, which projected production of 250,000 barrels per day in 2022. He stressed that it was critical to show an upside and potential in the state in order to layer on new oil to the

legacy fields. The department believed it was critical to turn the decline rate around in order to fund basic services in 10 years.

3:20:06 PM

Representative Gara communicated that every committee member wished to reverse the decline rate; he noted that there were varying views on how to meet the goal. He understood the department wanted to move away from the current progressivity mechanism. He stated that the bill would reduce tax rates down between 17 percent and 25 percent and would cap out at 33 percent even if prices reached \$200 per barrel. He wondered if there were proposals that would allow the state to share in the profits in a way that would not damage oil production. He believed a 17 percent tax on new oil was low.

Mr. Pawlowski believed the administration had been open to all input from each committee throughout the process. He agreed that government take was an important concept; at what point production and economics would not be hurt was taken into account. He stated that the administration was willing to work with the committee and its members.

Representative Gara replied that he would schedule a meeting with the department.

Representative Costello commented that she received emails from constituents who did not want changes made to ACES. She believed there was a compelling reason and need to explain what would happen if nothing was done [to decrease the current decline rate]. She appreciated the department's offer to work with committee members on the bill.

Co-Chair Austerman pointed to slide 21. He discussed that a prior version of the bill passed by the Senate had included a 35 percent tax rate. He wondered if the department's model could insert the 35 percent tax to show what it would look like. He requested a breakout between the flat \$5 per barrel and the sliding scale based on the department's projections related to volume and dollar value.

Mr. Pawlowski agreed. He noted that Mr. Stickel could provide a verbal answer related to the difference between the 33 percent and 35 percent tax rates.

Co-Chair Austerman requested the information in writing for all committee members.

[3:24:21 PM](#)

Representative Gara pointed to a provision added in the prior committee [House Resources Committee] that would mean the state would rely on company and joint billing statements in auditing companies. He recalled that in the past most Democrats had wanted a gross tax because it was relatively straight forward. He pointed to concern that under the profits tax some companies could overstate their costs, understate revenue, or qualify something for a tax credit that should not qualify. He wanted DOR to have the most power possible to ensure that the state was receiving its intended return under the legislation. He wondered whether the department was more comfortable with the current auditing system than it was with the proposed auditing provision.

Mr. Tangeman replied that the department had access to and used the joint interest billings; many other "tools" were also available to the department. He furthered that from an audit perspective it was necessary to rely on all available tools in order to get a job done.

Representative Gara asked whether Mr. Tangeman would prefer the current auditing system or the one included under the legislation that was limiting. Mr. Tangeman answered that the provision had not been in the governor's original bill and had been added by the previous committee.

[3:27:49 PM](#)

Vice-Chair Neuman looked at a provision related to lease expenditures and a change on pages 26 through 28. He discussed past concern related to "gold plating" and items allowable under lease expenditures. He observed that there were considerable changes in the legislation and asked for an analysis from the department.

Mr. Tangeman replied that joint interest billings could be very lengthy and were shared between two companies. He expounded that the department did have access to the billings, but they were not used by all companies. He asked for clarification on the request.

Vice-Chair Neuman referred to a subsection (B)(3) in the legislation, which stated that costs must be direct costs for exploring, developing, and producing. He stated that each producer was different; current statute included direct cost per individual for standard allowable deductions for production value. He stated that a new section included an arms-length clause that made it possible to be owner of the pipeline. He wondered about the best way to get the actual cost to the state. He understood the department had become fairly comfortable with the current system; he wondered how all of the changes would impact the department.

Mr. Tangeman answered that it was the state's responsibility to have a relationship with every tax payer; any insights provided through the documents helped the department do its job. He relayed that relying exclusively on a document between two companies limited the department's insight into the information needed. He stressed the importance of the one-to-one relationship between the state and individual tax payers.

[3:31:54 PM](#)

Vice-Chair Neuman surmised that Mr. Tangeman preferred the existing system. Mr. Tangeman answered that the department had developed the existing system over years and was comfortable where it was and where it was going under the net tax system.

Co-Chair Stoltze remarked that the related thought process and conversation would be ongoing.

Representative Edgmon looked at slide 21 and asked for a ballpark sketch on how a base tax increase from 33 percent to 35 percent would impact the data. Mr. Stickel replied that once the tax was put in place the difference would be in the \$200 million to \$250 million per year range.

Representative Edgmon noted he had misunderstood earlier comments and had thought the difference in the base rate from 25 percent to 33 percent was \$200 million to \$250 million.

Co-Chair Stoltze asked the department to clarify the information. Mr. Stickel answered that line 2 of slide 21 showed the increase in revenue to the state from the base

tax. He detailed that moving from a base rate of 25 percent up to 33 percent would increase revenue in FY 15 by \$850 million. He furthered that moving from a rate of 33 percent up to 35 percent would increase revenue by approximately \$200 million to \$250 million on top of the \$850 million. The impact of moving from a base rate of 25 percent up to 33 percent would be slightly over \$1 billion in increased revenue.

Representative Munoz understood that a close relationship existed between changes to the base rate tax and the \$5 to \$8 per barrel credit. She asked for the per barrel credit impact to be included in the department's modeling of the change between a 33 percent and 35 percent base rate.

SB 21 was HEARD and HELD in committee for further consideration.

[3:35:41 PM](#)

RECESSED

[4:08:05 PM](#)

RECONVENED

#hb193

HOUSE BILL NO. 193

"An Act relating to the joint administration of tobacco taxes by the state and a municipality."

[4:09:50 PM](#)

Representative Costello MOVED to ADOPT the proposed committee substitute for HB 193, Work Draft 28-LS0714\U (Bullock, 4/5/13).

Co-Chair Stoltze OBJECTED for discussion.

REPRESENTATIVE LANCE PRUITT, SPONSOR, shared that the bill had come to him at the request of the municipality of Anchorage. He clarified that the bill did not increase taxes; it was about communication and potentially lowering property taxes. He stated that the legislation would allow communication between municipalities and the state regarding tax returns, audits, etc. He detailed that currently the state could share the information with the federal government, other states, and the Canadian

government, but not with municipalities within the state. He noted that the City of Anchorage treasurer [Daniel Moore] was available via teleconference to discuss the issue.

Representative Pruitt relayed that the second piece of the legislation allowed the Department of Revenue (DOR) to partner with cities to create a stamp tax on tobacco. He explained that currently the state received tobacco tax from wholesalers and cities received the tax from retailers. The bill would enable the city to partner with the state and the tax would be administered at the wholesale level, which would eliminate the potential for tax evasion at the retail level. The bill's language assured that the money would be provided by a municipality to cover the costs. He shared that if 5 percent of tax evasion could be recovered it would equal approximately \$1 million for the City of Anchorage.

[4:13:37 PM](#)

Co-Chair Stoltze WITHDREW his OBJECTION. There being NO further OBJECTION, Work Draft 28-LS0714\U was ADOPTED.

Representative Wilson asked whether people could buy cigarettes online to avoid the tax. Representative Pruitt deferred the question to DOR.

JOHANNA BALES, DEPUTY DIRECTOR, TAX DIVISION, DEPARTMENT OF REVENUE, replied that the state currently had a cigarette tax stamp that was purchased by distributors. She detailed that individuals who purchased cigarettes online were required to pay tax to the department; individuals had the same tax liability as distributors.

Co-Chair Stoltze noted that DOR had provided testimony related to the tracking of cigarette taxes in the past. He asked how the department tracked the tax and about measures it had used. Ms. Bales relayed that federal law required internet sellers to provide the department with information when individuals purchased cigarettes online. She stated that over 2,000 Alaskans had purchased cigarettes online; the department had sent the individuals tax bills that they were required to pay.

Co-Chair Stoltze asked whether the process had been under an amnesty program. Ms. Bales replied that the department had waived all penalties and had generous payment plans.

DANIEL MOORE, CITY TREASURER, MUNICIPALITY OF ANCHORAGE, spoke in support of the legislation. He relayed that the city's tobacco tax was currently collected without a tax stamp. He stated that in the future the city may want a tobacco tax stamp. The city was aware the state already had a tobacco stamp. The private tobacco distribution industry had strongly recommended that if Anchorage had a tobacco stamp that it should be a joint single combination stamp that would require the city to work through the state to distribute and sell the stamps to distributors.

[4:18:43 PM](#)

Representative Munoz asked for an explanation about the meaning of stamp relating to cigarettes.

Co-Chair Stoltze asked Representative Thompson to provide an example. Representative Thompson read a tax stamp on pack of cigarettes to the committee.

Representative Thompson asked whether the bill would change the City of Anchorage's retail tax system to a wholesale level. Mr. Moore replied that currently the tax was done at a wholesale level; it was an excise tax applied to any volume of cigarette product that came into Anchorage for sale. He stated that the retailers were at the other end of the distribution chain; Anchorage did not directly tax retailers. The tobacco stamp would create a more identifiable trail showing that the tax had been paid; the stamp would eliminate situations where an entity bought a product in Anchorage, claimed it would be sold outside of the city, and then brought the product back into the city for sale to retailers. The goal was to discourage the potential for tax evasion.

Representative Thompson had been concerned about the possibility of sales outside of Anchorage. He appreciated Mr. Moore's explanation.

[4:21:15 PM](#)

Representative Kawasaki wondered about examples of similar tax collections that involved municipal and state tax

collections. Ms. Bales answered that the department did not currently collect taxes for other localities. She explained that taxes were collected through revenue sharing. She pointed to fish tax as an example; a portion of the tax was shared with the location where the fish was caught. She stated that the form of taxation was utilized in other states, specifically for sales tax.

Representative Kawasaki asked whether the bill would impact revenue sharing or caps on local tax or revenue. Ms. Bales replied that cigarette tax was not included in revenue sharing. The Municipality of Anchorage and seven other localities within the state had their own cigarette taxes. She did not believe the cigarette tax would work into the tax cap for Anchorage. She deferred the question to Mr. Moore for additional detail.

Co-Chair Stoltze clarified that the bill related to the broader category of tobacco taxes and was not limited to cigarette taxes. He detailed that cigarette taxes provided \$31.4 million in unrestricted general fund (UGF) revenue; whereas non-cigarette tobacco taxes provided \$14.4 million. He noted that the taxes brought in more UGF revenue than the commercial fishing industry.

Mr. Moore relayed that tobacco tax fell under the tax cap in Anchorage. He stated that any type of additional revenue received as a result of tightening enforcement would be a dollar for dollar tradeoff with property taxes; a dollar more in tobacco tax would mean a dollar less in property tax.

Representative Holmes asked for clarification on the fiscal note from DOR. She pointed to the total cost of \$135,100 coming from statutory designated funds. She observed that because the state could be reimbursed by municipalities the total cost to the state would be \$0.00. She asked for verification that the funds would be reimbursed to the state.

Representative Pruitt replied that the CS would have a new fiscal note showing program receipts.

Representative Holmes asked for confirmation that there would be no fiscal impact to the state. Ms. Bales replied that the forthcoming fiscal note would show that revenue would come from program receipts. The fiscal note would

show an increase related to the creation of one new position, but the total state expenditure would be zero; the additional fees would be collected from participating municipalities.

[4:27:35 PM](#)

Co-Chair Austerman asked whether the \$135,000 would cover all municipalities with a cigarette sales tax that wanted to participate. Ms. Bales answered that the state would continue to issue same number of cigarette tax stamps as it did currently; there would be additional fees and new designs if all municipalities chose to participate. She furthered that most of the costs would be associated with a position tasked with tracking all of the cigarette tax stamps. The goal was to have a limit of one tax stamp per pack of cigarettes to prevent additional costs incurred by distributors. The department expected that the total cost would not exceed \$135,000.

Co-Chair Austerman asked for verification that there would be one state/municipal stamp given to each of the participating communities. Ms. Bales replied in the affirmative.

Co-Chair Austerman asked for confirmation that DOR would collect the fees and distribute them back to municipalities. Ms. Bales answered in the affirmative. She elaborated that revenue was collected when stamps were sold to distributors; there would be different inventories of stamps for sale and DOR would track which portion of the sale was for either state or municipal revenue.

Co-Chair Austerman looked at page 2 of the CS and observed that the bill indicated that the department "may" collect funds from municipalities; there was nothing in the bill that required the department to collect funds. He assumed the intent was for DOR to collect the funds.

Representative Pruitt replied that he had worked with the department on the bill language and it was the intent for the state to have no financial burden.

Co-Chair Austerman asked whether the sponsor would object if the word "may" was changed to "shall." Representative Pruitt was agreeable to the change if no unintended consequences were identified by DOR.

Co-Chair Stoltze did not see a problem with the current language. He furthered that participation would be initiated by municipalities and it would be in their best interest to work with the state. He wondered if changing the language to "shall" would create a burden. He was more comfortable with the word "may."

[4:31:58 PM](#)

Representative Pruitt asked the department to weigh in on the issue. Ms. Bales replied that the department would have no problem with the change to shall and saw no unintended consequences that would result from the change. The department would ensure that costs to municipalities would be predicated on the number of stamps sold in the area.

Co-Chair Stoltze asked whether the change would force a municipality into a relationship with the state.

Co-Chair Austerman looked at line 4 on page 2 of the bill, which included language related to the agreement between DOR and a municipality. He was more concerned about line 12 related to reimbursement. He did not have a problem with "may" in line 4.

Representative Pruitt confirmed that the intent was to ensure that a municipality willingly and knowingly took on the cost burden.

Co-Chair Stoltze communicated that the amendment would be offered at a later portion of the meeting.

Representative Kawasaki referred to testimony from the city and municipality [of Anchorage] about lost revenue due to tax evasion. He asked about the department's record related to tax collection. Ms. Bales answered that the state did not have a tax stamp until 2004. She shared that there had been a 24 percent increase in cigarette tax revenue in the first full year after the stamp's enactment. She referred to discussions with the Municipality of Anchorage related to dealing with tax evasion; following the trail of cigarette tax sales through invoices had been unsuccessful. She relayed that the tax stamp had allowed for successful enforcement.

[4:35:01 PM](#)

Representative Wilson asked what would happen if Anchorage was the only municipality interested in participating. Ms. Bales replied that the department would continue to issue a state-only cigarette tax stamp for cigarettes sold outside of the municipality and would have a joint stamp for cigarettes sold within the municipality. She added that there would be no problem if a municipality did or did not want to have the tax stamp.

Representative Wilson wanted to make sure the state would not need to hire a position if only one community decided to participate.

Co-Chair Stoltze asked Mr. Moore about conversations with other jurisdictions. He noted that Mat-Su had a cigarette/tobacco tax. Mr. Moore replied that he had not had recent conversations with other jurisdictions on the subject; conversations had been primarily with private sector wholesalers. He surmised that if Anchorage was the only entity in the state pursuing a joint tobacco tax stamp it would receive a disproportionate share of the costs. He furthered that the municipality would work with the state to determine whether a full-time or part-time person would be needed. He continued that there would be a joint agreement between the state and the municipality to determine the terms. He elaborated that the state was in the driver's seat and would tell the jurisdiction what the cost would be; the municipality would then decide whether it agreed to the terms. The municipality would look at the cost and potential revenue that would be generated from the stamps prior to a decision.

Co-Chair Stoltze commented that Anchorage should hope that other cities would choose to participate because DOR would hire a person if authorized by the legislature.

Representative Thompson discussed that Fairbanks had a former similar tax; there had been no tax charged on cigarettes shipped out of the city. He wondered if a municipal stamp would be required on the packets sold in stores such as Costco. He thought the issue could become confusing.

Mr. Moore answered that the municipality had asked major tobacco distributors including Sam's Club, Costco, Northern Sales, and others about how the change would impact the

stores. The entities had responded that a joint stamp would be necessary. He furthered that some of the member wholesalers (e.g. Costco) would need to have two separately managed secured inventories for the state-only stamp and the joint state/city stamp.

4:39:20 PM

Representative Kawasaki stated that there were currently six municipalities that taxed tobacco. He wondered if the bill would encourage other municipalities to tax tobacco, given that the state would take on the most expensive aspect of administering the tax.

Representative Pruitt replied that some municipalities may make the decision to begin taxing tobacco. He noted that in Anchorage there was currently substantial revenue set in place that was not obtained, which meant others throughout the city had to pick up the costs through property tax or other methods. He acknowledged that the bill may make it easier for other municipalities to tax tobacco and recognized that many people would benefit in communities currently levying tobacco tax as well.

Representative Thompson could see where the change would work for Anchorage, but he did not know if it would work in Fairbanks. He explained that the Fairbanks North Star Borough had a cigarette tax, within city limits there was a separate sales tax, and there was also a state tax.

Ms. Bales commented on the concerns. She stated that there was nothing currently that would preclude a municipality from enacting a cigarette tax or from having a cigarette tax stamp. She pointed to the concern that without a cooperative agreement with the state every municipality could enact its own stamp, which would put a requirement on distributors. The bill would provide a mechanism to make it easier (particularly for distributors) if more municipalities decided to tax tobacco.

4:42:20 PM

Co-Chair Stoltze CLOSED the public testimony.

Co-Chair Austerman MOVED to ADOPT a conceptual amendment on page 2, line 12 that would change the word "may" to "shall." There being NO OBJECTION, it was so ordered.

Representative Costello requested to amend the replacement fiscal note. She discussed that page 2 of the DOR fiscal note specified that \$50,000 would be used annually to purchase cigarette stamps. She pointed to a services line of \$54,700 and believed that \$50,000 of the amount should be moved to the commodities section of the note.

Co-Chair Stoltze clarified that general fund program receipts should be changed to statutory designated receipts.

Representative Costello responded that the updated note did reflect the change to statutory program receipts. She discussed the zero note from the Department of Commerce, Community and Economic Development and the Department of Revenue replacement note [FN3], which showed \$135,100 for FY 14 through FY 19 in statutorily designated funds.

Representative Costello MOVED to REPORT CSHB 193(FIN) as amended out of committee with individual recommendations and the accompanying fiscal notes. There being NO OBJECTION, it was so ordered.

CSHB 193(FIN) was REPORTED out of committee with a "do pass" recommendation and with one new fiscal impact note from Department of Revenue and one previously published zero note: FN1 (CED).

[4:46:25 PM](#)

AT EASE

[5:03:54 PM](#)

RECONVENED

#hb76

HOUSE BILL NO. 76

"An Act relating to electronic filing of certain information with the Department of Labor and Workforce Development; relating to surcharges, rate increase reduction, prohibition on the relief of certain charges, the unemployment trust fund account, and the offset of certain unemployment compensation debt under the Alaska Employment Security Act; relating to the definition of 'covered unemployment compensation debt'

in the Alaska Employment Security Act; and providing for an effective date."

DIANE BLUMER, COMMISSIONER, DEPARTMENT OF LABOR AND WORKFORCE DEVELOPMENT (DLWD), introduced department staff. She explained that the bill did four things: (1) allowed for electronic filing of reports and documents, (2) improved the ability to recoup fraudulent unemployment insurance (UI) payments, (3) adopted minor changes bringing the department into compliance with federal law governing the UI program, and (4) changed how UI tax rates were set in order to keep more money in the hands of Alaskan employers and employees. The bill would keep more money circulating in the state's economy while protecting the integrity of the trust fund.

PAUL DICK, DIRECTOR, DIVISION OF EMPLOYMENT SECURITY, DEPARTMENT OF LABOR AND WORKFORCE DEVELOPMENT, provided a sectional analysis of the bill.

Section 1 adds a new section, AS 23.05.055, authorizing the commissioner to allow the use of electronic filing methods in place of paper filing.

Section 2 adds a new section, AS 23.20.021, authorizing the legislature to appropriate money into the unemployment trust fund account.

Section 3 adds a new section, AS 23.20.279, to bring the state into conformity with federal law, Public Law 112-40, by prohibiting the relief of charges to employers when an erroneous payment of unemployment insurance benefits is made due to an established pattern of the employer, or an agent of the employer, for failing to respond timely or adequately to a documented request for information relating to a claim for unemployment compensation. This section defines "erroneous payment" as a payment made that would not have otherwise been paid, but was due to the failure of the employer to respond timely or adequately. This section also defines "pattern of failing" as two or more times or 2% or more of all requests, whichever is greater, during the prior year.

Section 4 amends AS 23.20.290(c) by adding the word "surcharge" following the words "fund solvency adjustment".

Section 5 repeals and reenacts AS 23.20.290(f), replacing a table method for determining fund solvency adjustment surcharges with a more precise calculation method. It also eliminates the 0.3 limitation on fund solvency adjustment surcharge decreases in a single year.

Section 6 adds a new section, AS 23.20.291, authorizing the commissioner to suspend, in whole or in part, increases in unemployment tax rates when the "average high cost multiple," a measure of solvency calculated by the U.S. Department of Labor, Employment and Training Administration, is 0.8 or greater and after consultation with the department's actuary.

Section 7 amends AS 23.20.390(f) to bring the state into conformity with federal law, Public Law 112-40, by removing the department's authority to waive the collection of a penalty established due to misrepresentation and requires that a minimum of 30% of the unemployment insurance penalties collected due to misrepresentation be deposited into the state's unemployment trust fund account.

Section 8 adds new section, AS 23.20.486 to authorize the department to offset unemployment compensation debt against a claimant's federal income tax refund. This section would allow the state to participate in the federal treasury offset program.

Mr. Dick elaborated on Section 7 and relayed that currently the department was required to put 100 percent of the penalty collections into the unemployment trust fund account (the figure would be changed to 30 percent under the legislation). He pointed to Section 8 and shared that there were 19 other states currently participating in the federal treasury offset program; the program would enable the department to collect \$500,000 per year and to allocate more money to the trust fund.

[5:09:14 PM](#)

Mr. Dick continued with the sectional analysis:

Section 9 amends AS 23.20.520, by adding a new paragraph to define "covered unemployment compensation

debt" in accordance with the federal statutory definition.

Section 10 effective July 1, 2018 repeals AS 23.20.291, added by section 6 of this bill.

Section 11 amends state uncodified law by specifying that AS 23.20.279, added by section 3 of this bill, applies to overpaid benefits established after October 21, 2013.

Section 12 specifies that the department will adopt necessary regulations to implement changes. Regulations will not be effective prior to July 1, 2013.

Section 13 establishes that section 12 takes effect immediately.

Section 14 establishes the effective date for the remaining sections of this Act as July 1, 2013.

[5:10:08 PM](#)

CATHIE ROEMMICH, CEO, JUNEAU CHAMBER OF COMMERCE, spoke in support of the legislation. She read from a statement:

Thank you for all of your efforts to keep our state strong by working for small business growth. It's not often these days we find ways to lower the cost on anything, so we applaud the governor for bringing forward the solvency of Alaska's Unemployment Trust Fund Account. The Juneau Chamber of Commerce represents nearly 400 business members and their employees. It is our job to promote and support a positive business climate, not only in Juneau, but throughout the state. Our members support legislation that updates and clarifies laws as they relate to doing business in an effort to improve Alaska's business environment. Therefore, we would like to add our support to House Bill 76. We are pleased that this legislation will ensure that business owners as well as Alaskan workers are not paying more to state government in unemployment insurance taxes than necessary. The Juneau Chamber also understands the importance of compliance with the federal unemployment insurance laws. Maintaining a significant federal

Unemployment Tax Act credit that our employers currently receive is another critical piece of responsible taxation. The federal compliance components of House Bill 76 ensure that Alaskan businesses will not be sending any more money to Washington D.C. than necessary for the unemployment insurance program. We are also supportive of the greater efficiencies that the Department of Labor will be able to provide by allowing electronic filing of our unemployment claims. Thank you all for the work you do on behalf of Alaskans.

5:11:56 PM

BARBARA HUFF TUCKNESS, DIRECTOR, LEGISLATIVE and GOVERNMENTAL AFFIARS, TEAMSTERS LOCAL 959, discussed the organization's membership. She referred to an opposition letter from the Fairbanks Chamber of Commerce (copy on file). She relayed that the organization had paid approximately \$36,000 in unemployment taxes in 2012; employees had paid slightly over \$8,000. She shared that Alaska was one of three states where employee and employer contributions went into the fund. She communicated that the organization had concern related to Section 6 of the House Labor and Commerce Committee CS. She detailed that the concern with Section 6 related to the amount of money employers and employees would pay into the fund. She had sent DLWD questions related to how the rate was calculated and how the change would impact employers and employees. She read a specific question that had been raised followed by a response from DLWD:

Q: If the rate increases are suspended as referenced in Section 5 [Section 6 in the current CS] of the bill and the average high cost multiple falls below the trigger, won't employers and employees subsequently be required to pay more than what they would have had the earlier rate increase not been suspended.

A: If rate increases are suspended employers and employees would be required to pay slightly more in subsequent years than they would have if the increases had not been suspended in the earlier years. Over the long-term, the amount paid by employers and employees would be about the same or slightly less if increases were never suspended. Any suspension would have the

effect of deferring suspended taxes that would be absorbed over a multiple of years following.

Ms. Huff Tuckness was not concerned with any other sections of the bill.

[5:16:21 PM](#)

Ms. Huff Tuckness stressed that the current formula had worked well since the 1980s. The concern related to a potential impact on a fund that was currently running well. She encouraged the committee's consideration related to Section 6.

Representative Holmes asked what the organization's preference was related to Section 6. Ms. Huff Tuckness replied that the organization would prefer that the section was removed from the legislation. She noted that the removal of the section would mean there would not be any suspensions of what employers or employees would pay.

Representative Gara asked whether Section 6 could be rewritten so that the regular rate would go back into effect when the fund's surplus dissipated. Ms. Huff Tuckness felt that she was not the appropriate person to respond to the question. She referred to a question by the organization about how a surplus in the fund would be defined. She believed the questions fell under the purview of the department or the creator of the original formula. She added that the UI fund paid for some great educational programs throughout the state and made contributions to unemployed individuals.

Representative Gara wanted to ensure the fund was able to continue paying for items it funded. He asked if Ms. Huff-Tuckness disagreed that the fund currently had a surplus.

[5:20:02 PM](#)

Ms. Huff Tuckness did not agree that there was a surplus. She elaborated that fund contributions were based on a formula that had been established in the 1980s that had successfully ensured adequate contributions when economic times in the state were bad or good. She discussed rates over the past 10 or 20 years and referred to a chart showing slight increases and decreases over the years. She noted that the current formula ran smoothly.

Vice-Chair Neuman asked whether the issue had been addressed in the House Labor and Commerce Committee and if so, why the committee had decided to keep the section. Ms. Huff Tuckness replied that she had brought the concern to the prior committee. She believed a sunset provision amendment passed by the prior committee was a way to address any negative issues should they occur. She surmised that if the bill passed with the provision intact and none of the concerns came to fruition there may be an effort to either extend or remove the repeal.

Representative Costello requested that the bill be held after public testimony for further review. She offered her time to help resolve the issue.

[5:23:26 PM](#)

PAUL GROSSI, ALASKA PIPE TRADES AND IRON WORKERS OF ALASKA, JUNEAU, followed up on testimony provided by Ms. Huff Tuckness related to Section 6 and stated that there may be a surplus in the fund currently, but there was no way for him to know. He surmised that the Legislative Finance Division director was probably the expert. He stated that there may be a way of tweaking the formula if the fund was over funded in order to give employers a break; the fund had been in effect for over 30 years and had worked close to perfectly. He cautioned to be careful with changing the formula because if there was a relief of an increase and a downturn in the economy caused the fund to become insolvent the employers would be on the hook. He explained that the federal government would have to pay the benefits and would require reimbursement with interest and the fund would need to be made solvent again. He did not believe the sky was falling, but the current system had worked for a long-time. He suggested that the committee look further into the issue.

[5:26:42 PM](#)

Representative Wilson observed that Section 6 appeared to have checks and balances. She furthered that if the formula were to be changed it would be looked at again in the first year and subsequent years to ensure it was running smoothly.

Mr. Grossi agreed that there were checks included the Section. He communicated that when the formula had gone into effect in 1979 or 1980 there had been significantly fewer employers and employees. He stated that it may be possible to tweak the formula to give employers a break for a long period of time. He noted that the financial analysts would be better equipped to provide that information.

[5:28:45 PM](#)

DENNIS DEWITT, NATIONAL FEDERATION OF INDEPENDENT BUSINESSES, JUNEAU, shared information about the organization. He spoke in strong support of the legislation including Section 6. He shared that the organization's national consultant had looked at the section and was comfortable that the slight formula tweak would not cause any trouble for employers. He detailed if no employer were able to pay any UI taxes the fund would still have the ability to pay out funds equal to those paid in the last year for another 1.75 years. The organization believed the amount was sufficient for a trust fund. Additionally, the organization believed that continuing to increase the trust fund assessment was taking money out of employers' and employees' pockets and putting it into a state savings account at an inappropriate and unneeded level.

Representative Gara pointed to Section 6, page 4, line 26. He believed the bill's provision requiring a reduction to last for a one-year period in the event of a surplus was inflexible. He wondered whether the section could be modified to allow for a lower rate on a month to month basis.

Mr. Dewitt replied that continued changes of tax rates created problems for employers related to payroll. Changing the rate on a monthly basis would require computer systems to be reprogrammed on a monthly basis, which would become expensive. He stated that Public Employees' Retirement System (PERS) was concerned about when retirees were elderly; however, the UI fund was concerned about setting rates for the present and three years out. The organization believed an annual setting was sufficient and the likelihood of the fund being expended during that time period was very unlikely.

Representative Gara assumed that the rate would not need to be looked at every month. He believed that if a surplus was

identified the rate could be reduced and once there was no longer a surplus it could be dropped the following month.

[5:33:30 PM](#)

DON ETHERIDGE, ALASKA AFL-CIO, JUNEAU, supported the majority of the legislation but had concerns about Section 6. He shared that declining revenues was the primary reason for concern.

[5:34:29 PM](#)

ANDY ROGERS, SELF, ANCHORAGE (via teleconference), spoke in support of the legislation. He spoke from the perspective of an employer and did not see the bill as a game changer. He was encouraged by the state's work to conduct business efficiently. He looked at Section 6 and opined that the ability for the commissioner to give employers a break when the fund did well was a good way for the state to help employers. He did not believe a break on a potential increase would save the solvency of the fund in a major economic downturn.

Co-Chair Stoltze asked if Mr. Rogers was a small business owner. Mr. Rogers replied in the affirmative. He and his wife owned a physical therapy clinic with multiple locations.

[5:36:54 PM](#)

RACHEL PETRO, PRESIDENT and CEO, ALASKA STATE CHAMBER OF COMMERCE (via teleconference), spoke in support of the legislation. She stated that most of the provisions were straight forward. She asked for the system to remain compliant, efficient, and fair. She relayed that the chamber did support Section 6 of the legislation.

Co-Chair Stoltze CLOSED the public testimony.

HB 76 was HEARD and HELD in committee for further consideration.

AT EASE

[5:39:06 PM](#)

RECONVENED

[5:42:48 PM](#)

#hb193

HOUSE BILL NO. 193

"An Act relating to the joint administration of tobacco taxes by the state and a municipality."

5:43:10 PM

Co-Chair Stoltze brought previously reported out CSHB 193(FIN) back before the committee upon advice from legal counsel related to an amendment.

Representative Costello MOVED that the committee RESCIND its action to report CSHB 193(FIN) out of committee. There being NO OBJECTION, it was so ordered.

Co-Chair Austerman MOVED to RECIND action on amending CSHB 193(FIN). There being NO OBJECTION, it was so ordered.

Co-Chair Austerman pointed to page 2, line 12, and MOVED Amendment 2 that would replace the word "may" with "must."

Co-Chair Stoltze OBJECTED for discussion.

Co-Chair Austerman explained that Legislative Legal Services had communicated that the proper replacement of the word "may" was "must" (instead of "shall") in order to accomplish the amendment's intent.

Co-Chair Stoltze WITHDREW his OBJECTION. There being NO further OBJECTION, Amendment 2 was ADOPTED.

Representative Costello MOVED to REPORT CSHB 193(FIN) out of committee with individual recommendations and the accompanying fiscal notes.

CSHB 193(FIN) was REPORTED out of committee with a "do pass" recommendation and with one new zero impact note from Department of Commerce, Community and Economic Development and one new fiscal impact note from Department of Revenue.

5:45:51 PM

AT EASE

5:46:30 PM

RECONVENED

#hb129

HOUSE BILL NO. 129

"An Act relating to approval for oil and gas or gas only exploration and development in a geographical area; and providing for an effective date."

Representative Costello MOVED to ADOPT the proposed committee substitute for HB 129, Work Draft 28-GH1970\U (Bullock, 4/5/13). There being NO OBJECTION, it was so ordered.

[5:47:12 PM](#)

JOE BALASH, DEPUTY COMMISSIONER, DEPARTMENT OF NATURAL RESOURCES (DNR), relayed that the department had worked on changes to the substantive portion of the bill in Section 2. He noted that Section 1 included a lengthy set of findings and determinations in response to a recent Alaska Supreme Court decision [Sullivan v. Resisting Environmental Destruction on Indigenous Lands]; the language directed DNR to follow the existing statutory guidance in AS 38.05.180(a) in order to adopt regulations to implement the court's finding in terms of the state's interests (public and otherwise) for the advancement of exploration and development.

Mr. Balash pointed to Section 2 and relayed that Legislative Legal Services had recommended a couple of clarifying changes. The department had no concerns with the changes.

Co-Chair Stoltze noted that the bill was heard previously and that public testimony had been closed.

Mr. Balash added that DNR staff was available online for technical questions.

[5:49:12 PM](#)

Representative Costello pointed to the findings section and wondered if it was common for the legislative branch to mention a decision made by another branch of government.

Mr. Balash believed the language was appropriate. He communicated that the agency was addressing a decision by

the Supreme Court, which determined that it was the legislature's prerogative related to how DNR would implement the aspect of the case requiring that DNR take a continuing hard look at decisions beyond the leasing phase. The language was modeled on language that had been adopted by the legislature approximately 12 years earlier.

Co-Chair Stoltze agreed that the language was not unique. He recalled fighting a past effort by the Alaska Railroad to overturn an Alaska Supreme Court decision related to a Native village in his district.

[5:51:41 PM](#)

Representative Gara wanted to ensure that the bill would not extend the amount of time a company with an oil and gas lease would have to develop the land. He stated that currently companies were provided a specific amount of time under a lease to develop; if the lease was not acted upon the state had the right to lease the area to another party.

Mr. Balash replied a lease could be held no more than 10 years unless the terms specified a shorter period. The only way for a party to continue to hold the lease was through production, a certified well, or unitization. The legislation would not impact the existing requirements; the language related to the decisions made by DNR when granting permission to explore or develop the lease.

Representative Gara asked for verification that current law provided three public comment periods (when the lease came out, when the development plan was released, and in one other circumstance), but the legislation reduced the number down to one.

Mr. Balash replied that after the leasing phase there would be an opportunity for public notice and comment for exploration and another opportunity for comment on the area in question for development. He stated that under current practice there may be multiple public notices/comments for each one of the phases; the change to one public comment period per phase would provide more efficiency in considering decisions. He furthered that DNR wanted to hold public comment on the frontend in order to have a more meaningful decision making process.

Representative Gara asked for verification that the bill would maintain the two levels of public comment, but a broader combination of leases would be combined into one public comment period.

Mr. Balash responded in the affirmative. He explained that the intent was to enable a given decision to affect more than one lease, rather than having lease-by-lease decisions. He detailed that the number of leases included in a decision would be dependent on the circumstances; some leasing areas lent themselves to larger geographic scopes. For example, DNR would be more discerning related to public comment on the east side of Cook Inlet, which was more populated than the west side.

[5:56:21 PM](#)

Representative Gara noted that he tended to want to speed up development on most of the leases rather than letting them lag. He understood that residents in some communities wanted to proceed with caution. He stated that when the system was lease by lease the development plan would be known; however, if many leases were combined it would be harder to meaningfully comment on leases that may be at different stages. He wondered how the department would deal with the potential issue.

Mr. Balash pointed to a distinction between exploration and development. He explained that the exploration activity was likely to be on a broader scope than the development decision; exploration and development would have separate decisions associated with various phases of development. He shared that currently leases were sold to companies coming to the state for exploration. Under the bill there would be a public notice and decision document affecting leases; once a resource was located there would be a separate decision that would likely narrow the scope from the larger body of leases to those under which the resource had been found. He furthered that the details on the implementation of decisions would be determined under DNR regulations.

[5:59:08 PM](#)

Co-Chair Stoltze handed the gavel to Co-Chair Austerman.

Co-Chair Austerman pointed to legislative findings in Section 3 and asked if the direction to continue analyzing

the cumulative impact of a project was already addressed within current DNR regulations.

Mr. Balash replied that the examination of multiple factors beyond the cumulative impacts was undertaken in the department's 10-year best interest finding conducted for the leasing phase. He expounded that each year DNR conducted a call for additional information, which allowed the public and communities to bring items to the department's attention; other departments frequently brought new reports, studies, and findings to DNR. The items were all taken into account before the department moved forward with annual lease sales. He relayed that the Supreme Court decision mandated that DNR could not stop considering the impacts.

Co-Chair Austerman asked whether the cumulative effect was included. Mr. Balash replied in the affirmative.

Co-Chair Austerman asked whether the cumulative effect was included in new regulation. Mr. Balash replied that DNR considered cumulative effects as part of the best interest finding in the leasing stage; the department continued to look at the information as time went by as the face and speed of development changed in a given area. He furthered that DNR was considering the items, but the regulations would direct it to specify when or where the consideration took place.

Representative Kawasaki asked for the impact of each of court's legislative findings under the legislation. Mr. Balash asked for a specific example.

Representative Kawasaki pointed to Section 5 related to consideration and analysis by the department, Section 7 related the department's continued look at new information and changing circumstances, and Section 8 related to meaningful public notice by the department. He believed the items were subjective and asked for comment.

Mr. Balash replied that Sections 5 and 7 fell under the prior topic discussed with Co-Chair Austerman. He elaborated that the best interest finding was done on a 10-year cycle for each sale area; the document was comprehensive and considered a multitude of items specified in statute. He stated that 10 years was a long time between findings; therefore, DNR did a call for information each

year in order to make sure findings remained relevant. He elaborated that the call was publicly noticed and provided an opportunity for other agencies and the public to comment. He explained that Section 7 related to the annual call and Section 5 acknowledged that the department's current process made the creation of an entirely new finding for decisions unnecessary.

[6:04:51 PM](#)

Representative Kawasaki asked for an explanation of the changes included in Section 2 and about their necessity. Mr. Balash answered that the changes made had not been due to the Supreme Court case. He relayed that the changes helped bring clarity to the meaning of the substantive section. He pointed to a write up of specific changes included in member's packets (copy on file), which referenced the page and line numbers from the original bill. He detailed that the words "without regard to individual lease boundaries" had been deleted because the topic was related to area-wide decisions. He communicated that DNR had no problem with the change. He furthered that per a recommendation by Legislative Legal Services the sentence had been revised to read "an approval applies to an exploration or development commencing during a period for up to 10 years. The language created an upper limit and pertained to decisions that were made in an exploration or development context; the decision would define the length of time.

Mr. Balash continued to explain the changes in Section 2. He addressed a clarifying change from the language "specified period" to "a period specified under the approval." The length of time would not automatically be 10 years and would be determined in the decision made. He relayed that the department had no problem with any of the changes. The fourth change added the language "or group of leases" to follow the word "leases" in the bill. He noted that the word "area" was mistakenly used twice in a sentence and subsequently had been deleted.

Vice-Chair Neuman discussed a gas well that had been drilled in Big Lake. He explained that the company had drilled some monitoring wells in response to concern from locals; the lease had subsequently transferred to another company. He noted that commitments had been made to check for contaminates over time. He wondered who was responsible

for transfers and whether it was associated with the lease contract.

6:09:09 PM

Mr. Balash replied that each case was different; however, the obligations of the lease or any permits would change hands from lessee to lessee. He relayed that transfers of interest in a lease had to be approved by the Division of Oil and Gas. The department looked to see whether the company taking over a lease would take on the existing obligations (e.g. obligations on older properties with abandonment liabilities).

Vice-Chair Neuman cited language on page 3 of the legislation: "the director may approve exploration for development for all or part of an area previously approved for oil and gas leasing." He further discussed the drilled area at Big Lake and relayed that the cleanup had not been ideal. He pointed to the 10-year lease maximum under the legislation and wondered if a similar scenario could happen again; if so, he doubted it would be approved by DNR.

6:09:46 PM

Mr. Balash answered that the bill's language addressed the different phases regarding a previously approved leasing area. He discussed circumstances when DNR had determined it was in the state's best interest to dispose of property interest on a piece of land; the division would still need to make a decision for exploration and development phases, but in order for property to be disposed of DNR was required to do a best interest finding.

Vice-Chair Neuman continued to speak to the issue in Big Lake. He shared that the drilling had been approved by DNR on private property and the property owner had been concerned about the situation.

Mr. Balash answered that Alaska had a split estate where the mineral interest was reserved for the state and the surface area could be sold to private individuals in some cases. The state had the ability to make decisions that affected private owners, but DNR had regulations and processes that governed under the circumstances. He furthered that DNR would be required to provide public notice that a lease was in question if the lease was on

private land. He relayed that the department's decision would be subject to appeal and/or litigation if an individual was concerned about the area in question.

[6:14:46 PM](#)

Vice-Chair Neuman surmised that the Big Lake land owner had not wanted to go to the expense of suing the state.

Representative Munoz commented that the purpose was to look holistically at a geographical area to determine the parameters of development that would be allowed. She believed the goal was to provide the public with a better understanding of what types of activity would occur within a certain area.

Mr. Balash replied in the affirmative. He communicated that DNR wanted its process to be more meaningful and to engage the public in a way that would allow the department to guide its decisions on the front-end as opposed to a piece-meal process. He pointed out that the North Slope Borough had provided a letter of support for the legislation. The department believed that engaging the borough would be holistic and would help everyone involved to reach an affirmative decision in a better way.

Representative Costello discussed the fiscal impact note from Department of Natural Resources that included \$134,000 in FY 14 for one non-permanent position.

Representative Costello cited language from the fiscal note analysis section: "without regard to individual lease boundaries." She believed the language had been removed from the bill and wondered about the impact. Mr. Balash replied that there would not be a fiscal impact.

Representative Gara stated that the bill would result in fewer public hearings. He surmised that subsequently there would be less employees required. He remarked that the state was facing fiscal challenges and he was not convinced the fiscal note made sense.

Mr. Balash answered that the department was asking for a non-permanent employee to maintain current work done and to help compile regulations that would guide the new program. Once the transition was made, the division expected to be able to perform its job more efficiently. He could not

quantify the change, but the goal was for the department to make preparations to do more with less.

6:19:58 PM

Representative Gara noted that the division had existing staff to handle multiple hearings. He believed the development of regulations could be done with its current staff and with the help of the Department of Law (DOL). He did not believe a new position was necessary.

Mr. Balash answered that DNR would have to reimburse DOL for work done. He clarified that public notice and comment periods were held, but there were not a tremendous number of public hearings held on the decisions. He furthered that the department would continue to review plans once an exploration decision had been made. He explained that the public comment period would be truncated.

Representative Gara OBJECTED to the fiscal note. He MOVED to AMEND the fiscal note to zero. He stated that there were DOL attorneys who worked specifically on regulations. He believed the work could be done with existing employees with some potential overtime work.

A roll call vote was taken on the motion.

IN FAVOR: Gara, Kawasaki

OPPOSED: Munoz, Holmes, Neuman, Wilson, Costello, Thompson, Stoltze, Austerman

The MOTION FAILED (2/8).

Representative Costello MOVED to REPORT CSHB 129(FIN) out of committee with individual recommendations and the accompanying fiscal note. There being NO OBJECTION, it was so ordered.

CSHB 129(FIN) was REPORTED out of committee with a "do pass" recommendation and with one new fiscal impact note from the Department of Natural Resources.

#sb18

CS FOR SENATE BILL NO. 18(FIN) am

"An Act making, amending, and repealing appropriations, including capital appropriations,

supplemental appropriations, reappropriations, and other appropriations; making appropriations to capitalize funds; and providing for an effective date."

CSSB 18(FIN) am was SCHEDULED but not HEARD.

Co-Chair Stoltze discussed the schedule for the following day.

Representative Munoz asked which bills were scheduled for the following morning. Representative Costello replied that the bills on the schedule included SB 21, HB 63, HB 102, HB 134, and HB 195.

Co-Chair Stoltze noted that not all bills would be heard and that the schedule had been compiled to provide sufficient public notice.

#

ADJOURNMENT

[6:27:16 PM](#)

The meeting was adjourned at 6:27 p.m.