

HOUSE FINANCE COMMITTEE
FOURTH SPECIAL SESSION
May 27, 2016
3:12 p.m.

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CALL TO ORDER

Co-Chair Thompson called the House Finance Committee meeting to order at 3:12 p.m.

MEMBERS PRESENT

Representative Mark Neuman, Co-Chair
Representative Steve Thompson, Co-Chair
Representative Dan Saddler, Vice-Chair
Representative Bryce Edgmon
Representative Les Gara
Representative Lynn Gattis
Representative David Guttenberg
Representative Scott Kawasaki
Representative Cathy Munoz
Representative Lance Pruitt
Representative Tammie Wilson

MEMBERS ABSENT

None

ALSO PRESENT

Jerry Burnett, Deputy Commissioner, Treasury Division, Department of Revenue; Fred Parady, Deputy Commissioner, Department of Commerce, Community, and Economic Development; Forrest Bowers, Deputy Director, Division of Commercial Fisheries, Department of Fish and Game; Representative Liz Vasquez; Representative Lora Reinbold.

PRESENT VIA TELECONFERENCE

John Binder, Deputy Commissioner, Department of Transportation and Public Facilities; Brandon S. Spanos, Deputy Director, Tax Division, Department of Revenue; Brent Goodrum, Director, Division of Mining, Land and Water, Department of Natural Resources.

SUMMARY

HB 4003 MOTOR FUEL TAX

HB 4003 was HEARD and HELD in committee for further consideration.

HB 4005 MINING: LICENSE, TAX, FEES; EXPLOR. CREDIT

HB 4005 was HEARD and HELD in committee for further consideration.

HB 4006 FISHERIES: TAXES; PERMITS

HB 4006 was HEARD and HELD in committee for further consideration.

Co-Chair Thompson addressed the meeting agenda.

#hb4003

HOUSE BILL NO. 4003

"An Act relating to the motor fuel tax; and providing for an effective date."

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JERRY BURNETT, DEPUTY COMMISSIONER, TREASURY DIVISION, DEPARTMENT OF REVENUE, explained that the provisions in HB 4003 were identical to provisions in HB 4001 pertaining to motor fuel tax. He relayed the bill would increase current tax rates for highway fuel from 8 cents to 16 cents; for marine fuel from 5 cents to 10 cents; for aviation gas from 4.7 cents to 7 cents; and for jet fuel 3.2 cents to 6.5 cents. He reviewed the sectional analysis (copy on file):

- Section 1: Amends AS 43.40.010(a) Changing the tax rate from eight cents to 16 cents per gallon for highway fuel, from four and seven tenths cents per gallon to seven cents per gallon for aviation gasoline, from five cents to 10 cents per gallon for fuel used in watercraft, and from three and two-tenths cents per gallon to six and one-half cents per gallon for aviation fuel other than gasoline.
- Section 2: Amends AS 43.40.010(b) to conform with changes made in Section 1.

- Section 3: Increases the credit against the motor fuel tax from six cents to 12 cents for fuel used for non-highway uses.
- Section 4: Makes the change in sections 1, 2, and 3 applicable to fuel sold after the effective date of those section.
- Section 5: Allows the Department of Revenue to adopt regulations to implement the provisions of this Act.
- Section 6: Is an immediate effective date for Section 5.
- Section 7: Provides for a July 1 effective date for the changes to the motor fuel tax.

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Representative Wilson asked how the bill would impact the mining and fishing industries. She spoke to jet fuel and relayed the international airports currently took over \$32 million in excess, which would not be used in Anchorage or Fairbanks and went to smaller airports. She asked if there had been any determination on why "this is better than landing fees on those small airports" versus increasing the jet fuel tax.

Mr. Burnett responded that the aviation advisory committee had recommended (after the Department of Transportation and Public Facilities' (DOT) recommendation to implement landing fees in airports other than Anchorage and Fairbanks) an increase in the aviation fuel tax rather than landing fees.

Co-Chair Thompson relayed that there were testifiers available from DOT.

Representative Wilson noted that a group had gotten together and had decided they still did not want landing fees; therefore, they recommended increasing jet fuel. She explained increasing jet fuel [tax] increased cost at the two airports that already had landing fees [Anchorage and Fairbanks]. She wondered how it was fair to put more stress on the international airports that were self-sustainable versus implementing landing fees at smaller airports or exempting the international airports.

JOHN BINDER, DEPUTY COMMISSIONER, DEPARTMENT OF TRANSPORTATION AND PUBLIC FACILITIES (via teleconference), clarified his understanding that the question was about why DOT preferred a fuel tax over a landing tax.

Representative Wilson asked if the department supported the legislation.

Mr. Binder answered that the governor had tasked DOT with investigating ways to reduce the amount of General Fund (GF) subsidies to the rural airport system. He detailed that the rural airport system cost about \$39 million to operate annually and brought in \$5 million in revenue. The conversation had begun approximately 1.5 years ago when the legislature had asked DOT to subsidize or fund personnel increases (at the time operations had been increasing - significant overtime had been occurring and carriers had been requesting extended hours at the airports, which required personnel) with landing fees. He furthered that the aviation advisory board had asked the governor to engage with DOT on other available options for generating revenue. He detailed the conversation had built over the past year about what options were available and what made sense. He continued that board members had raised concerns about equitability and fairness across the state rather than at a specific airport. The board felt that due to the impact on the state, since aviation fuel taxes were already in place and were some of the lowest in the country, the board believed it would be the best way to generate additional revenue on the rural system to close the subsidy gap. The board recommended an increase up to 7 cents [note: some audio indecipherable], which was the foundation for the governor's inclusion of the tax increase in the current bill.

Co-Chair Thompson shared that about 2.5 years back he had chaired the finance transportation subcommittee and had requested the department come back with some way to help cover the exorbitant cost of keeping 249 airports open without any money to offset.

Representative Wilson relayed she had found it upsetting when she had called DOT to try to determine how much general funds were used at every airport - she had been unable to get an answer. For example, she had been told that a lump sum of money was sent to the northern region and there was no way of tracking what went to the highway

and the airports. She opined that it was pretty scary if that was the way the state handled business. She asked if the department would be in favor of excluding the international airports from the tax, given they were already self-sufficient. She did not have a problem with the option for other airports. She was concerned that the bill would put more stress on the larger airports to subsidize the smaller airports.

Mr. Binder responded that domestic traffic would be impacted by the aviation fuel tax since the international traffic was exempt already - it was about three-fourths of the total figure and impacted the amount of revenue generated [note: poor audio quality, some testimony indecipherable]. He pointed out that the international airports were directly benefiting from rural Alaska. He stated that while the fuel tax was being collected in Anchorage and Fairbanks and then flowing back to the rural system, the international airports were directly benefitting from the operations even if they did not actually weigh in.

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Representative Wilson was concerned about actually looking at the users being able to support the industry. She clarified she was not speaking to the benefit. She noted she would offer an amendment to exempt the international airports from the tax. She furthered that the landing fee paid for capital projects at present on the two international airports (the airports also operated domestic flights). She asked if the department had modeling to show how the proposed increases would affect the average person in the mining, fishing, and other related industries throughout the state.

Mr. Burnett responded that the modeling primarily looked at the amount of revenue each of the particular tax increases would raise (on the existing taxes). He explained that the subject matter experts and economists in DOR and other departments believed the increases would have minimal impact on the business.

Co-Chair Thompson remarked that some modeling had been done pertaining to a commuter driving into Anchorage from the valley. The scenario had assumed a certain gas mileage and a five-day per week commute. He did not remember the

precise numbers, but it had determined the motor fuel tax increase would cost someone about \$48 per year.

Representative Wilson stated that it was not just about the tax. She stated the committee had heard how low its taxes were, but that Alaska paid some of the highest gas prices. She continued there were impacts to everyone and as investors she believed they should know how the increases would impact individuals. She stated the addition may be minimal, but it was necessary to factor in the cost of gas, the income people brought in, and what else would be utilized.

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Representative Gara referred to the committee's recent debate about whether there should be a big bill that included numerous taxes or separate bills for each of the taxes. He remarked that the administration had tried to submit individual bills [during regular session], which had not worked. Subsequently, the administration had introduced a large bill that included all of the taxes. He believed the administration was just trying to get something done. He apologized to Commissioner Hoffbeck that he had become animated in the previous discussion. He emphasized he merely wanted to see a bill move forward. He addressed the fuel tax and relayed the committee had been told that with the increase in the legislation the state's fuel tax would still be the lowest in the nation. He asked if the same was true for aviation fuel.

Mr. Binder responded in the affirmative.

Representative Gara remarked that the high price of fuel in Alaska had more to do with refineries; however, he acknowledged it was not the appropriate time to address that issue. He added that he and others had introduced a bill that would have dealt with refinery charges. He asked for verification that the aviation fuel tax increase would apply equally to all domestic flights including small plane flights in rural Alaska or flights at larger airports.

Mr. Binder replied in the affirmative. He detailed that most of the [air] traffic in Alaska used jet fuel [note: poor audio quality, some testimony indecipherable]. As written, the bill would apply to everyone in the state

except for international traffic originating or ultimately landing in a foreign country.

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Representative Gara remarked that whether or not people wanted to agree, the state needed to raise revenue. He stated the question was about how to raise the revenue and about how fair it was to everyone. He was leaning in favor of the legislation. He was concerned that a significant portion of the burden was falling on individuals with little money. He wanted to see wealthier individuals contribute in a commensurate way. Overall he wanted to see a package that was fair to everyone and more balanced.

Co-Chair Thompson referred to a prior presentation on HB 4001, which had demonstrated how the proposed motor fuel tax increase would impact Alaskans. For example, a typical person driving 12,000 miles per year in a vehicle getting roughly 20 miles per gallon, would pay an additional \$48 per year in taxes.

Representative Gara referred to a fiscal policy caucus that had existed before he had served as a legislator. At the time he had recommended that at high prices when there was less of a need for money and the price of gas was much more expensive, the gas tax would roll back. He noted a former version of the bill had rolled back the gas tax. He wanted the committee to spend some time considering whether the approach was fair.

Co-Chair Thompson noted the committee would consider the bill the following day as well.

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Representative Guttenberg acknowledged the state's budget crisis and noted that the price of motor and aviation fuel was fairly low. He recognized the bill's goal of increasing revenue. He mentioned the estimated \$48 per driver in additional taxes per year for motor fuel. He spoke to a time when the price of gas increased to over \$4.00 per gallon and was concerned the impacts on individuals would be significantly higher, but the state's needs for raising revenue would be greatly diminished. He asked if the administration had considered rolling back taxes at different stages if the oil price increased to \$80, \$90, or

\$110. He had heard questions about how the state would account for the price difference between Southcentral and Northern Alaska regions. He contended it was not difficult to draw a line around Paxson or Trapper Creek and Cantwell. He detailed rural Alaska would be paying the same hit two or three times the amount impacting the road system.

Mr. Burnett answered that the House and Senate Transportation Committees had both included a price trigger in the legislation; however, the governor's legislation had never included a price trigger. He detailed that in 2008 when the price of oil hit its record high, the legislature acted to suspend the gas tax for one year, which was always an option in periods of excess prices. He relayed the issue was not a concern included in DOR's 10-year revenue forecast.

Representative Guttenberg thought the best time to do something was when there was no pressure on it. He would look at bringing some of the things back.

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Representative Wilson asked how the increase would impact the trucking industry in Alaska. She remarked that most of the goods were trucked into Fairbanks.

Mr. Burnett responded that he did not have any estimates on hand related to shipping rates. The department had looked at how much fuel someone may use and what that would affect. He detailed the change in taxes was less than the change in the last month in fuel prices in most of the state's communities. He remarked there were not changes in shipping rates every time gasoline or diesel increased or decreased 8 cents. He stated it was very difficult to tell what the impact would be over time. He continued it was possible to identify the costs to a specific company, but it was not possible to know how it would impact prices.

Representative Wilson hoped to hear about the impact from the trucking industry, which had pulled its support from the bill. She believed the administration was asking the legislature to make a decision without all of the information. She wanted to know how the motor fuel, jet, and other taxes would impact her constituents. She remarked that many goods were either flown or trucked in from Anchorage. She opined the impact would be very different in

communities across the state. She believed the answers should be known.

Representative Edgmon spoke to the art of raising taxes. He wondered if there was any way to quantify the cause and effect of raising taxes on industry, private sector, and consumer behavior. He assumed the answer was "no." He surmised there were ways for industry representatives to provide numbers about what increases to their costs mean in terms of their economic behavior (their ability to invest and to go forward to private sector entities). He was frustrated that levying taxes was inevitable. Additionally, he was frustrated that the cause and effect relationship was indeterminate and that the legislature had to rely on others to tell them. He furthered that even DOR, with its best quantitative tools, could only give some kind of extrapolation or estimate about what the tax increases would mean. He asked if the department had been able to do the analysis. Alternatively, he wondered if the legislature would have to rely on others to come forward to specify what the increases would truly mean.

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Mr. Burnett replied that DOR could determine what the cost would be to an individual or company for any of the taxes. However, DOR could not determine how people would behave or change their behavior as a result of the tax. He shared that he had been a university business instructor in the past. He relayed there were numerous academic studies on the topic, but they were not conclusive and would not provide an answer about what would occur when taxes were raised.

Representative Gattis referred to the study of Mat-Su commuters driving an average of 12,000 per year who would pay an average of \$48 more per year [under the proposed motor fuel tax increase]. She shared that she lived in downtown Wasilla, which was 55 miles from Anchorage. She rounded the distance to 50 miles and stressed that a commute to Anchorage five days per week was more than 12,000. She stated the actual mileage would range between 27,000 and 30,000 not counting any other travel. She emphasized that the increase would have a bigger impact on Mat-Su than \$48 per year.

Co-Chair Thompson clarified that he had received a sheet from a former presentation showing that a car driving 12,000 miles per year at 20 miles per gallon, would pay an additional \$48. He explained 12,000 per year was considered to be the national average for miles put on a vehicle. He shared that his vehicle was a 2001 and it only had 92,000.

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Representative Gattis replied that she had a 2003 vehicle with over 150,000 miles. She stressed that most of the miles were not commuter miles. She detailed Mat-Su residents spent a significant amount of time traveling back and forth to Anchorage; therefore, there would be a big impact.

Representative Guttenberg referred to his personal vehicles. He believed the appropriate term was "elasticity." He relayed he had recently read an article on the elasticity in the economy on men's underwear. He provided further detail about the article. He remarked that elasticity was a common economic concept. He did not believe there was no way of measuring the impact of the proposed tax increases on Alaska. He surmised it was possible to Google the question and come up with a multitude of papers. He asked about the effect of the taxes on the economy. He surmised that at present the impact would probably be minimal, but if the price ever went to \$100, he believed it would be severe. He stated it was not rocket science. He underscored that the committee was asking questions, but was not getting the answers. He was disinclined to support the bill and had never been inclined to support it.

Mr. Burnett responded that the elasticity of demand for motor fuels was very, very low within any relevant range. The change from 8 cents to 16 cents was unlikely to make any reasonable change in people's behavior. The price change from \$2.00 to \$4.00 was a separate question entirely. He emphasized the price change as a result of the legislation would be very low.

Representative Guttenberg responded that he "certainly recognized that, but you get to a dollar a lot faster and that's the impact." He furthered that when the price went to \$1.00 because of the increase in the legislation, it would impact "it faster than it would otherwise." He stated

it made a difference when fuel would be \$4.00 or \$5.00 per gallon. He believed the increase in the bill would get to the higher price faster.

Co-Chair Thompson summarized that the bill would increase motor fuel tax from 8 cents to 16 cents and the state would still have the second lowest gas tax in the nation. He shared he had recently been in California, which had a 52 cent tax; gas in California had been \$3.15 per gallon when it had been \$2.30 per gallon in Fairbanks.

HB 4003 was HEARD and HELD in committee for further consideration.

#hb4005

HOUSE BILL NO. 4005

"An Act relating to the mining license tax; relating to the exploration incentive credit; relating to mining license application, renewal, and fees; and providing for an effective date."

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Mr. Burnett explained HB 4005 was an increase in the mining license tax rate. The bill would increase the top tax rate on net profits greater than \$100,000 per year from 7 percent to 9 percent. Additionally, the bill would reduce the tax holiday for new mines from 3.5 years to 2 years, prevent the mining exploration incentive credits from being used to reduce royalties (limiting them to the tax), and added a \$50 annual license fee. He noted the license fee was reasonable because miners were exempted from the business license fee. He read the sectional analysis (copy on file):

- Section 1: Eliminates the ability to take the mining exploration tax credit against royalty payments
- Section 2: Removes references to royalties in the mining exploration tax credit provisions in AS 27.30.030(a)
- Section 3: Removes references to royalties in the mining exploration tax credit provisions in AS 27.30.040
- Section 4: Removes references to royalties in the mining exploration tax credit provisions in AS 27.30.050.

- Section 5: Changes the existing tax holiday for new mining operations from three and one-half years to 2 years.
- Section 6: Changes the tax rate on mining income in excess of \$100,000 from 7 percent to 9 percent.
- Section 7: Provides for a \$50 annual mining license fee.
- Section 8: Provides that changes to the exploration tax credit are applicable to royalty payments after the effective date of section 1. Provides that the two year tax holiday applies to mining operations that begin production after the effective date of section 6. Provides that the new tax rate begins the first tax year after the effective date of section 6.
- Section 9: Provides the exploration tax credit accounting in current law applies to a mining operation which began mining production prior to the effective date of this act.
- Section 10: Allows for the Department of Revenue to adopt regulations to administer this act.
- Section 11: Provides for an immediate effective date for section 10.
- Section 12: Provides that the rest of the bill is effective July 1, 2016.

Mr. Burnett elaborated that the new tax would go into effect in January 1, 2017.

Representative Gara noted the bill had briefly been in front of the committee several weeks earlier. He had been surprised to learn that a company would continue to receive a tax holiday if they were making profits (for 3.5 years under current law and 2 years under the legislation). He understood the justification of not having a profits based tax if a company was not making profits; however, he wondered about the justification for giving a company a tax holiday when it was making profits.

Mr. Burnett responded that mining operations tended to have very large capital costs prior to the start of operations and the tax holiday allowed a company to recover some of those capital costs at the very beginning of production. He detailed there was no cash out to the companies as a result of the tax holiday. He furthered that companies tended to not be as profitable in the first two years of production as they became once production reached full swing.

Co-Chair Thompson referred to the International Tower Hill Mines Livengood project that had 300 people working on it two years back. He detailed the mine was still in the permitting process and it had tremendous upfront costs already. He reasoned the tax holiday would allow the mine to recover some of the startup costs - it would take several years before the company would actually begin mining.

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Representative Gara conjectured that two-year holiday made more sense under some circumstances. He provided a hypothetical scenario where a company invested \$10 million to prepare a mine for operation and became profitable in year one. He asked if the company would deduct part of the \$10 million from year one so they were truly profitable. Alternatively, he wondered if a company was not allowed to deduct the prior costs from the first year of profits.

Mr. Burnett responded that a company was not allowed to directly deduct prior cost. There was an exploration tax credit a company may be able to take part of. Additionally, there was a depletion allowance, which allowed a company to take a certain percentage of a prior cost. He explained a company did not take a deduction for prior cost in one lump like with a cash flow tax (oil and gas was a cash flow tax rather than a profits tax) where capital costs were taken when they were spent and credits were taken.

Co-Chair Thompson informed the committee that Brandon Spanos the deputy director of the DOR Tax Division was on the line for additional questions.

Representative Gara had heard companies were allowed to deduct a certain percentage of pre-operations costs. He referred to the carried forward tax credit and a portion of costs a company could deduct in the first year. He asked what portion could be deducted once a company became profitable.

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BRANDON S. SPANOS, DEPUTY DIRECTOR, TAX DIVISION, DEPARTMENT OF REVENUE (via teleconference), asked for clarification.

Representative Gara referred to a company's development costs and asked for an estimate of what portion the company was allowed to deduct once they became profitable. He referenced the concept that once a company became profitable they would still not pay a tax for a few years.

Mr. Spanos replied [note: audio cut out during the response].

Representative Gara referred to the depletion allowance and asked for verification a company was allowed to deduct development costs on a depreciation schedule (similar to federal law pertaining to federal taxes). He asked for verification that a company received the money back (the deductions) over a period of time.

Mr. Spanos replied in the affirmative. He detailed there was a cost or percentage depletion allowance similar to federal depreciation or depletion.

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Representative Gara asked if the allowance pertained to all of a company's development costs.

Mr. Spanos responded it pertained to a company's own capitalized development costs.

Representative Gara asked for verification the allowance pertained to capital costs but not operations costs.

Mr. Spanos replied no, if there had been an expense in a given year that would be capitalized. He detailed if a company had a loss in the year a corporation may be able to use it against other income. However, in general development costs were capitalized.

Representative Gara relayed he was getting tripped up on capitalized versus capital costs. He explained he was used to oil production taxes and the terms capital costs versus operations costs. He asked for a definition of capitalized costs.

Mr. Spanos replied a capitalized cost was an expense that was not expensed in the current year. He furthered that it

became part of the capital and was expensed through a schedule over the life of the mine.

Representative Gara asked for verification that a capitalized development cost could include operations and capital costs. Mr. Spanos asked Representative Gara to repeat the question.

Representative Gara complied. He surmised capitalized development costs could include operations costs (e.g. labor) and capital costs (e.g. equipment). Mr. Spanos agreed. He expounded that the labor would be capitalized if it was part of the development of a mine.

Representative Wilson asked how the mining and fuel tax bills would economically impact the mining industry.

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FRED PARADY, DEPUTY COMMISSIONER, DEPARTMENT OF COMMERCE, COMMUNITY, AND ECONOMIC DEVELOPMENT (DCCED), responded that the mining tax itself was a net income tax, which was somewhat unusual in his experience related to mining. He shared he had spent 30 years in mining in Wyoming. The taxes he was most familiar with in Wyoming were severance-based, not net income-based. The net income tax would not occur unless a property had a net income. He stated "you can debate the amount of the haircut, but at the end of the day you're still growing hair, you weren't bald." He noted he would leave the specifics of the fuel tax to DOR, but he believed there was an off-road tax credit against that because it's a fuel tax.

Representative Wilson indicated that she had spoken with Fort Knox and she believed even with a credit the fuel tax would be a huge amount of money (excluding the mining portion). She thought it was DCCED's responsibility to consider how taxes would impact business in Alaska. She added if it was not the department's responsibility, she wanted to know why.

Mr. Parady that the task had not been given to DCCED in the current timeframe. He suggested that as everyone looked at the holistic picture of the situation Alaska found itself in, of course there were economic consequences to a \$400,000 per hour deficit.

Representative Wilson stressed that HB 4005 was not her legislation; however, if it was her bill she would come up with the information [she was currently asking for from DCCED]. She did not understand why anyone would have to ask the administration to bring certain things up. She reasoned there were departments for specific reasons. She redirected her question to the Department of Natural Resources (DNR). She asked DNR if it had done any analysis on how the mining and fuel taxes would impact the mining industry. She wondered how much money they were talking about, especially related to mines making over \$100,000.

BRENT GOODRUM, DIRECTOR, DIVISION OF MINING, LAND AND WATER, DEPARTMENT OF NATURAL RESOURCES (via teleconference), replied that the department had not been able to conduct an economic analysis at the present time regarding the bill proposals.

Co-Chair Thompson asked how many mines in Alaska made over \$100,000 per year in taxable profits.

Mr. Goodrum responded that about six mines fell into the category [note: due to poor audio quality some testimony indecipherable].

Representative Wilson stated she was not asking trick questions. She reasoned the administration was asking the legislature to increase taxes on industry as well as on individuals without the information she believed should be required. She wanted to know the overall impact of the proposed taxes on each industry. She noted the bills would add an incredible cost to Fort Knox (the estimate did not include property taxes, which Pogo Mine did not have). She stated each mine was different and although there were not a significant number, certain boroughs had different responsibilities and costs. She thought the information should have been available either from DOR or DCCED.

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Co-Chair Neuman asked if there was a methodology that could predict the economic impacts of an increased tax.

Mr. Parady replied that in a mine management scenario with an investment property such as Fort Knox (i.e. an operating mine) at the time of determining the capital investment a company would have run best, worst, and probable scenarios;

the internal rate of return; and hurdle rate related to the range of risk for the investment. He stated the factors came from all directions including permitting timeline, scale of investment, rate of return, commodity price volatility, and other. Across the range of factors a company was reaching an investment decision. He acknowledged that uncertainty was the enemy of investment, which was the reason the tax holiday (at the time the investment was made) was a fairly significant benefit because it occurred right at the point where cash was flowing out the door, but not in. The bill would shorten, but not eliminate the window. He continued that once a company began operation, its cost structure was predicated on all of the variable costs (i.e. labor contracts, fuel, and other) and commodity price variability. He explained that mines were driven by economies of scale. He detailed a company could respond to market volatility by running its equipment around the clock, year round to spread out fixed cost and lower per unit cost.

Mr. Parady addressed the particular tax and its impact on an operating environment. He agreed the change from 7 to 9 percent was not a 2 percent change, it was a two-sevenths change or 28 percent, which constituted a substantive tax change. However, it was a tax change occurring on net income; at that point, it may lessen a mine's ability to reinvest or hire additional workforce, but it was not shifting from a profitable to a non-profitable enterprise on the basis of the tax. He did not have the ability to model Fort Knox's cost structure; each of the existing mines knew exactly where their cost structure was against the current price of gold. He agreed the tax increase would have an impact, but because it was a net income, it would tighten their operating margins, but would not position the mines for failure.

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Co-Chair Neuman knew that different mines had internal information that he surmised the department did not have access to. He thought the state would have a \$3 billion deficit for some time; he did not anticipate the price of oil to increase any time soon. He wondered how to measure that against trying to cover the state's debt. He questioned whether the money should be taken from the state's dividend. He was trying to think of some way the

department could model the economic impacts of all the various information.

Mr. Burnett responded that it was not a simple model. He specified that each of the mines were different. He clarified that DOR did receive the mines' cost information. The largest taxpayers in the group had about \$451 million in profits in 2014 and the tax would take an additional \$7 million in taxes per year out of that type of profit structure. He corrected that prices would be lower based on commodity prices - the profit was in the hundreds of millions and the state would take a few million. He elaborated that the state's tax would reduce the federal tax. He continued it was not a deduction from the state income tax, but it was a deduction from the federal income tax, which was a 35 percent tax. The impact on the companies was not as great as the dollar amount in the fiscal note. The 4 cents in additional fuel tax the mines would pay (he clarified the number was determined by subtracting 12 cents from 16 cents) was lost in the volatility of fuel prices. He acknowledged the dollar amount was significant, but commodity prices also tended to move together in many cases. He continued that oil prices and gold prices could move in the opposite directions, but it was only possible to make predictions or guesses. He underscored the increase would mean a small dollar impact relative to the total investment. The bill would not mean the state would take money before it became profit; the bill would only take profits with the mining tax.

Co-Chair Neuman requested a comparison of the mining, gas, motor fuel, and fisheries taxes compared to the taxes in other states.

Mr. Burnett replied that the department had previously provided the information to the committee. He noted the department could locate the information.

Vice-Chair Saddler echoed the comments by Representative Wilson. He expressed embarrassment on behalf of the administration that the taxes had been considered for five or six months, but he did not see any analysis or consideration of the potential impact of the taxes. He understood the tax would only be on the profit, but he wondered if the profit margin could be reduced to a point where it was not sufficiently profitable. He wondered about the potential impact on employment, exploration, and future

investments. He assumed there must be a general model that applied. He believed the administration had been given sufficient time to come up with some specifics. He was concerned the administration appeared not to have considered the impact of the bills.

Mr. Parady assured the committee the administration had not approached the tax bills with a cavalier attitude. He explained that mining was a cyclical business. In the past several years the price of gold had varied between \$950 or \$1,000 to \$1,400 or \$1,500. He detailed the specific commodity price spread far exceeded any impact in the suggested tax rate. He agreed that taxes had an effect on the bottom line of a business and a company would deal with the bottom line the same way the state was approaching the current deficit - a business could freeze travel, overtime, and hiring, and could layoff contractors. He acknowledged there was an impact when money was pulled out of a business. However, he spoke to the perspective of the scale of a change from 7 to 9 percent, which was only on a net income basis. He underscored the increase was not on a cost basis. He explained the effect was difficult to quantify and was less than the effect of the cost variability in the commodities cycle.

Mr. Parady continued that in his knowledge of taxes in general, Alaska's mining tax structure, which dated to the 1950s and was based on net income was different than in other major mining states; the most direct comparison to Alaska was probably Nevada because it was a hard rock gold mining state, whereas Wyoming was primarily a coal, uranium, and trona mining state (albeit trona mining occurred underground and there were some similarities). He elucidated that most tax structures were typically based on a percentage of cost, in Wyoming it was a severance tax basis. The fact that Alaska's tax structure was on a net income basis moderated some of the effect. He believed DCCED had a state-by-state comparison and he would provide it to the committee.

Co-Chair Thompson noted the committee had received the comparison in the past.

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Representative Gattis discussed that she could not compare her farms to those in the Lower 48. She detailed that the

cost of fuel and fertilizer was significantly higher. Additionally, she had to haul in all of her equipment from the Lower 48. She reminded committee members and others that Alaska was unlike other states as it related to logistics. She did not believe it was possible to compare apples-to-apples.

Representative Gara thought additional discussion was necessary. He recalled oil tax debates in the past when there had been a gross tax. He asked whether in low profits years a mining company would prefer a profits based tax or a gross tax (like in Wyoming).

Mr. Parady clarified the Wyoming tax was severance tax based. He detailed the tax was based on the value of the mineral at the time it was severed from the ground. He explained it was not a gross on the cost as the value of the cycle was completed when fed to a refinery or power plant. He believed a mining company would want the lowest tax possible at any given point in time.

Representative Gara thought there had to be an answer to his question. He wondered if a company would prefer a severance based tax or a tax based on profits during a time when profits were low or a company was losing money.

Mr. Parady commented on the complexity of the question. He explained when Russia imploded and Russian yellowcake flooded the world market and depressed uranium pricing, "we went to a graduated severance tax." He detailed the tax was zero percent at \$12 per pound of yellowcake and down (1 percent to \$14, 2 percent to \$16, and back to the original rate of 4 percent at \$18). The point was an effort to salvage the industry through the low spot caused by the spike. There had been zero taxes at the low end and an increase back to the normal taxing rate as the market returned. He concluded "there's a lot of ways to skin this cat."

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Mr. Burnett responded to Representative Gara's question and explained that a net income based tax at a zero profit would be a zero tax; therefore, anytime a company was losing money or profits were low, the tax would be lower - unless it was structured as Mr. Parady had discussed.

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Representative Gara had been surprised to learn that the state's royalty was profits based as opposed to based on the value of the commodity. He asked what the royalty was on mining.

Mr. Burnett deferred the question to Mr. Goodrum. He agreed it was a net tax based on the same calculations as the net mining license tax. He did not have the rate on hand.

Mr. Goodrum answered the rate was 3 percent net profit.

Representative Gara was not interested in raising the tax on struggling mines (companies that were not making money or were making very little money). He pointed out that the bill applied to mining companies making over \$100,000 in profit. He was curious what the fiscal impact would be if there were a slightly higher tax for companies making \$250,000 per year in profits. He asked about the fiscal impact of an 11 percent tax on those companies.

Mr. Burnett replied he had answered the question in a previous committee. Generally speaking, nearly all of the income above \$100,000 was income above \$250,000. He clarified it was nearly all above \$1 million. The impact of 2 additional percent on mines earning over \$250,000 would mean a doubling of the fiscal note at about \$14 million per year as opposed to the \$7 million.

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Representative Kawasaki asked for verification that gas prices and motor fuel would be rolled into the net income tax. He surmised companies would have the ability to write the increase off. Mr. Burnett responded that any expenditure for operating the mine could be taken as a tax deduction against profits.

Representative Kawasaki recalled a previous discussion related to when mining taxes had last been changed (in 1955). He asked if the brackets in Section 6 had been set at the time. He outlined the brackets as \$40,000 to \$50,000 at 3 percent, \$50,000 to \$100,000 was 5 percent, plus \$1,500.

Mr. Burnett replied that the brackets had been set in 1955. He reminded the committee that there had been no large mines operating in Alaska at the time. There were numerous large operating mines in Alaska prior to WWII and nearly all of the current operating mines had been started in the 1980s, 1990s, and 2000s.

Representative Kawasaki requested additional information on why the discussions about the brackets had not been changed. He referred to a Fairbanks resident working in the summer as a placer miner who made \$40,000 to \$50,000 per year and paid 3 percent of net. He continued that the largest scale mines paid 7 percent (or 9 percent under the proposed legislation). He thought the "mom and pop" mines were getting hit disproportionately compared to the larger mines.

Co-Chair Thompson relayed that in a prior presentation for HB 4001, a statement had been made that the tax increase would not impact mom and pop miners at all other than the \$50 annual license fee. He asked if the same applied to the current legislation.

Mr. Burnett replied in the affirmative; the increase in the legislation only applied to mines making over \$100,000; therefore, mom and pop organizations would not be impacted. He addressed Representative Kawasaki's question and relayed it had been discussed in the House Resources Committee. He elaborated there had been discussions about expanding the brackets, which would have very little impact in terms of how much money the state received. He continued it would be a policy decision to opt not to tax people at lower levels. The primary income to the state from the miners was from the 14 to 20 taxpayers making more than \$100,000 in profits on an annual basis (primarily from the 6 large mines). He referred to a spreadsheet the department had created for Representative Kawasaki, which had been shared with the committee in 2014. He detailed the net profits of the taxpayers making under \$100,000 totaled approximately \$1 million.

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Representative Kawasaki referred to the discussion about whether it was possible to make an apples-to-apples comparison of the mining industry in Alaska and other states. He believed it was fair to ask the questions. He

wondered if any analysis had been done on what other countries did. He reasoned Alaska was an international mining destination and was ranked number 6 worldwide for investment attractiveness (just behind Western Australia, Saskatchewan, Nevada, Ireland, and Finland) in a Frasier report. He noted the committee was familiar with Frasier pertaining to oil and gas. He continued that Frasier listed Alaska as number 2 worldwide for best practices, number 11 worldwide for best mineral extraction potential, and other. He asked if the administration had considered the report when analyzing the mining license tax.

Mr. Burnett replied that the issues were considered by DOR, DNR, and probably by DCCED. He affirmed the administration had looked at taxes in other jurisdictions besides the United States.

Vice-Chair Saddler commented that the most recent large mine to open in Alaska had taken a significant amount of time and had required a Supreme Court decision. He questioned how many new mines were opening in Alaska. He referred to page 3 of the bill and asked for verification the mining tax was on net income, not net profits.

Mr. Burnett replied that net income and profit were generally considered the same thing.

Vice-Chair Saddler asked for verification the current mining royalty was 3 percent of net profit. Mr. Burnett answered in the affirmative.

Vice-Chair Saddler had heard in previous presentations that the \$50 mining tax was in lieu of a royalty. He referred to the 3 percent net profit royalty and a mining tax royalty.

Mr. Burnett responded that the \$50 mining license fee was a recognition that all other businesses in Alaska paid for a business license. He continued that companies with a mining license were exempt from regular business licensing requirements.

HB 4005 was HEARD and HELD in committee for further consideration.

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#hb4006

HOUSE BILL NO. 4006

"An Act relating to the fisheries business tax and fishery resource landing tax; removing the minimum and maximum restrictions on the annual base fee for the reissuance or renewal of an entry permit or an interim-use permit; relating to refunds of the fisheries business tax and the fishery resource landing tax to local governments; and providing for an effective date."

Mr. Burnett detailed the bill would increase the tax rates by 1 percentage point. The entire tax increase was exempted from municipal revenue sharing. He explained the current tax was still shared 50/50 between the state and local governments. The bill would remove the \$3,000 cap on annual Commercial Fisheries Entry Commission (CFEC) entry permit fees and would exempt developing fisheries from the increase. He clarified that developing fisheries taxes would not change under the legislation. He read the sectional analysis (copy on file):

- Section 1: Eliminates the cap of \$3,000 on the base fee for Commercial Fisheries Limited Entry Permits and Interim permits.
- Section 2: Changes the tax rates for the fisheries business tax from four and one-half to five percent for salmon canned in a shore based business, from three to four percent for other fish processed in a shore based business and from five percent to six percent for fish processed by a floating business.
- Section 3: Changes the tax on fish for a direct marketing business from three to four percent.
- Section 4: Is a technical change eliminating the requirement to submit tax returns to Juneau.
- Section 5: Provides that one percent of the value of each fishery under the fisheries business tax will be deposited in the general fund and not be subject to sharing with local governments.
- Section 6: Changes the landing tax from three to four percent.
- Section 7: Provides that one percent of the value of each fishery under the fisheries landing tax will be deposited in the general fund and not be subject to sharing with local governments.

- Section 8: Provides that one percent of the value of each fishery under the fisheries tax will be deposited in the general fund and not be subject to sharing with local governments.
- Section 9: Provides that the tax changes in sections 2, 3 and 6 are applicable after the effective dates of those sections.
- Section 10: Allows for the Department of Revenue to adopt regulations to administer this act.
- Section 11: Provides for an effective date for section 1 (CFEC) of January 1, 2017.
- Section 12: Provides and immediate effective date for section 10.
- Section 13: Provides that the rest of the bill is effective July 1, 2016.

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Co-Chair Neuman was unfamiliar with the governor's version of the bill. He requested a sectional analysis showing the changes from the governor's original bill, the House Resources Committee version, and the current version of the bill.

Mr. Burnett was happy to provide the document and offered to speak to the changes. He explained that Section 1, which eliminated the cap on CFEC permits had been added in the current bill.

Co-Chair Neuman asked for an estimate on the economic impact. He wondered if there was an economic impact of \$2 million plus or minus state revenue.

Mr. Burnett answered the projection related to the change in Section 1 of the legislation was plus or minus \$2 million. The remaining tax changes in the bill equated to about \$18 million. He addressed the other change from the original bill and explained the original bill had increased the rate for one of the developing fisheries from 3 percent to 4 percent; however, the current bill did not make any changes to the tax rate for developing fisheries. He added that the previous year the total tax on developing fisheries had brought in less than \$50,000. He estimated the amount may have been around \$17,000. He concluded the dollar amount was not huge; therefore, the change made very little difference to the bill. He summarized that the

changes to the bill were the additional \$2 million and a few thousand in taxes related to a developing fishery.

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Representative Edgmon asked how DOR would characterize the fishery taxes. He referred to previous discussion about mining taxes and net income based.

Mr. Burnett responded that the fisheries business and landing taxes were both gross taxes on the value of the fishery. He detailed the taxes were modeled after a severance-type tax where people were taxed based on a common property resource owned by the people of the State of Alaska, which could be harvested by a few people. The individuals were paying something to Alaska residents for the privilege of harvesting the fish and to represent a value for the fish that were being harvested. He reiterated the tax was based on the value of the fish and not the profitability of the industry.

Representative Edgmon asked how much of the annual \$18 million in revenue generated by the taxes came from shore-side activities.

FORREST BOWERS, DEPUTY DIRECTOR, DIVISION OF COMMERCIAL FISHERIES, DEPARTMENT OF FISH AND GAME (DFG), replied the \$18 million was the increase in tax revenue that would result from the legislation. He believed the shore-side component of the current tax revenue was roughly 75 percent.

Co-Chair Thompson requested the information from DFG for the following day. Mr. Bowers answered in the affirmative.

Representative Edgmon commented that the issue demonstrated the "throwing of the dart process we're engaged in with these taxes." He clarified he did not intend his remarks to be disparaging towards the efforts of the departments and administration for bringing the bill forward. He could not recall when the fisheries tax had last been analyzed or revised (he mentioned the 1960s as a potential timeframe), but he surmised it had been a long time. He asked if the taxes had been revisited in the 1960s or 1970s.

Mr. Burnett answered he did not recall the last time the fisheries tax changed, but it had been a number of years

back. He noted there had been some changes to the methodology of sharing taxes and developing fisheries taxes over time. He clarified he was not referring to changes to the tax amounts.

Representative Edgmon relayed many smaller fisheries (e.g. salmon fisheries in Bristol Bay) received bonuses in a good year. He furthered in a perfect world the bonuses were distributed amongst the owners, skippers, crew members, and everyone who took part in operations. He asked if any of the proposed taxes would reduce some of those extra earnings.

Mr. Burnett responded that to the extent the fish were taxed by the legislation, if payment was due to the value of the fish, it should be taxed. He detailed it was not unusual for fish to be purchased at a specific price during season and for a price adjustment to be made later. The price adjustment was subject to the tax just the same as the original price paid.

Co-Chair Thompson asked if that meant up and down. Mr. Burnett answered in the affirmative.

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Representative Edgmon asked for verification DOR's annual assessment period occurred in the spring. He surmised the spring of 2015 reached back into calendar year 2014. Mr. Burnett responded in the affirmative.

Representative Wilson asked whether the bill addressed bycatch. She remarked on bigger boats taking in a significant amount of fish.

Mr. Burnett answered in the negative. To the extent that the fish were sold, they were taxed; if they were not sold there was nothing to tax.

Mr. Bowers added there were certain bycatch species that may be legally retained and sold, which had a value and were taxed. There were other bycatch species discarded at sea, which were not taxed because there was no associated value.

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Representative Wilson disputed the statement that discarded bycatch had no value. She reasoned that just because the fish went back overboard did mean the fish had no value. She understood that the industry also gave a significant amount to Seattle, Washington. She detailed that something had also been worked out with the Food Bank in Fairbanks. However, a large portion of the bycatch was thrown away. She stressed it was a resource that was being discarded. She referred to the legislation and believed the opportunity should be taken to penalize the boats. She understood there were ways to substantially reduce bycatch. She conceded it was more expensive for the boats, but she wondered why the legislation would not deal with the overall issue.

Mr. Bowers responded that many of the fisheries Representative Wilson was referring to occurred in federal waters and were federally managed. He was unsure what authority the legislature would have to regulate the activities in federal waters.

Representative Wilson asked for verification that none of the bycatch was caught in state waters and that everything caught in state waters were counted and brought in money.

Mr. Bowers responded in the negative. He elaborated that bycatch was brought in by fisheries in state waters. The tax was assessed when the fish were caught or brought into state waters. He believed many of the larger fisheries mentioned by Representative Wilson occurred in federal waters. He elucidated that the legislature could implement something related to bycatch caught by small boat fisheries in state waters. However, he did not know what could be done for larger offshore vessels fishing in federal waters.

Representative Wilson remarked that Alaska fishermen made sure to operate cleanly. She stated there were people doing the right thing and people doing the wrong thing. She stressed the fish were an Alaskan resource. She did not understand why the administration and legislature would not take the opportunity to stop some of the bycatch problem, whether it was related to bigger or smaller boats. She underscored the resources were all valuable. She hoped the department could provide an estimate related to the value the discarded fish.

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Representative Gara shared Representative Wilson's concerns. He discussed fish caught inside and outside of state waters. He noted there were fish caught outside state waters that were processed in the state. He asked how to divide between the fish the state was allowed to tax and those it was not allowed to tax.

Mr. Bowers replied the tax was assessed when the fish were brought into state waters. There was a commercial operators' annual report that every licensed processor had to complete. He detailed the annual report described a processor's production and purchasing history, which was the basis for calculating the price used to determine the value of the fish. He believed the processors indicated on their tax forms where the fish were purchased.

Mr. Burnett elaborated there was one exception. He detailed that under the Magnuson Stevens Act, the state was allowed to tax pollock, which was landed outside state waters.

Mr. Bowers corrected it was the American Fisheries Act.

Mr. Burnett agreed. He expounded the state was allowed to tax pollock that landed in Seattle, but it was not able to tax other fish that were not either caught, processed in, or brought into state waters.

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Co-Chair Neuman referred to floating processors that operated outside Alaska's waters. He believed Mr. Bowers had testified that the state did not tax fisheries until they reached Alaskan waters. He asked about floating processors.

Mr. Bowers replied that if the processors brought processed fish into Alaska (e.g. to offload the fish for transshipment, which was common practice) they were responsible for the tax at that point.

Co-Chair Neuman asked for verification that floating pollock processors operating outside of state waters and selling the fish in Seattle, were not included in the state's fish processing tax.

Mr. Bowers answered the American Fisheries Act regulated the pollock fishery in the Bering Sea. He detailed that because the state's late U.S. Senator Ted Stevens was aware of the potential, he had included a provision in the act requiring any pollock caught between 3 and 200 miles offshore was subject to the state's taxes.

Co-Chair Neuman concluded there was a tax. Mr. Burnett replied in the affirmative.

Representative Gara spoke about king salmon bycatch and explained that many of the fish were not worth very much because they were one to two-year-old fish that got crushed and pulverized in the nets. He asked for the accuracy of his statement.

Mr. Bowers responded that salmon were deemed prohibited species on groundfish vessels; therefore, when they were caught as bycatch they could not be legally sold. He explained the fish were not retained for use as a food product and were not handled the same as fish bound to become food products.

Representative Gara remarked he had heard reports that when some of the younger fish ended up in the huge nets were pulverized by the time someone reached them. He noted the issue was for another day. He asked which of the taxes effected factory trawlers.

Mr. Burnett replied the landing tax [applied to factory trawlers].

Representative Gara asked what type of operations were subject to the landing tax (e.g. factory trawlers).

Mr. Burnett replied the tax applied to any fish that were landed regardless of the type of fishing operation. He deferred to Mr. Bowers for further detail.

Mr. Bowers expounded the tax applied to any fish processed three miles offshore. He detailed it could include factory trawlers, loading processors taking deliveries from catcher vessels, freezer longliners (a number of large longliners operated in the Gulf of Alaska and Bering Sea that catch and process onboard), scallop catcher/processors, crab catcher/processors, and any other vessel processing in waters greater than three miles offshore.

Representative Gara surmised the vessels were large. Mr. Bowers responded the smallest vessel in the category would be around 58 feet. He expounded on his earlier answer and relayed there were some salmon trollers that catch and process. He detailed some of those boats were under 58 feet, but most of the boats impacted by the tax were larger vessels due to space requirements for the processing equipment, freezers, and crew size.

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Representative Gara asked why the state was allowed to tax vessels if they processed their catch beyond the three-mile offshore boundary. Mr. Bowers explained that the vessels became subject to the tax when they moved into state waters to offload fish. He detailed it was a common practice for the vessels to offload fish to freighters or cold storage facilities onshore because the boats were limited in their freezer size.

Representative Gara asked about the current cost of running the Division of Commercial Fisheries. He believed the cost was between \$25 million to \$35 million. Additionally, he asked for the current revenue and the bill's projected revenue to the state for the combined fisheries taxes. He was interested in revenue brought in compared to the cost required to operate the Division of Commercial Fisheries.

Mr. Bowers responded that the current General Fund budget for the Division of Commercial Fisheries was about \$35 million to \$36 million.

Mr. Burnett expounded that taxes generated by the legislation would be fairly close to that amount [\$35 million to \$36 million] and potentially slightly higher. He noted the revenue depended on the price of fish in the current year and other things. The revenue coming to the state was currently less than the amount required to operate the division.

Co-Chair Thompson mentioned he had chaired the House Fisheries Committee in previous years. He recalled that vessels in the Bering Sea had to pay for observers to be onboard the vessels. He detailed the vessels had been allowed a certain amount of bycatch; once the vessels

reached the limit they were required to quit fishing. He asked for comment.

Mr. Bowers agreed that most fisheries in Alaska had bycatch caps. The most common tool to assess those caps, especially for vessels processing at sea, were onboard observers. He detailed observer costs were \$300 to \$400 per day, which were typically borne by the vessels.

Vice-Chair Saddler encouraged committee members to give some deference to the House Fisheries Committee, which had some special expertise. He recommended against using the bill as a way to fix any issues regarding allocation, bycatch, or international issues. He reasoned the House Finance Committee's responsibility was net profits and not longline nets.

HB 4006 was HEARD and HELD in committee for further consideration.

Co-Chair Thompson relayed the agenda for the following meeting. He recessed the meeting to a call of the chair [note: the meeting never reconvened].

#

ADJOURNMENT

[4:53:53 PM](#)

The meeting was adjourned at 4:53 p.m.