HOUSE FINANCE COMMITTEE
April 24, 2018
1:36 p.m.

1:36:24 PM

CALL TO ORDER

Co-Chair Foster called the House Finance Committee meeting to order at 1:36 p.m.

MEMBERS PRESENT

Representative Neal Foster, Co-Chair
Representative Paul Seaton, Co-Chair
Representative Les Gara, Vice-Chair
Representative Jason Grenn
Representative David Guttenberg
Representative Scott Kawasaki
Representative Dan Ortiz
Representative Lance Pruitt
Representative Steve Thompson
Representative Cathy Tilton
Representative Tammie Wilson

MEMBERS ABSENT

None

ALSO PRESENT

Jack McGee, Self/Attorney, Juneau; Joseph Geldhof, Self/Attorney, Juneau; Don Bullock, Self, Juneau; Barbara Huff-Tuckness, Director, Governmental and Legislative Affairs, Teamsters Local 959, Juneau; Sheldon Fisher, Commissioner, Department of Revenue; Ken Alper, Director, Tax Division, Department of Revenue; Representative Charisse Millett.

PRESENT VIA TELECONFERENCE

Chad Schaefer, Self, Soldotna; George Pierce, Self, Kasilof; Doug Smith, CEO, ASRC Energy Services, Anchorage; Cathy Duxbury, Self, Anchorage; James Squyers, Self, Rural Deltana; Kevin Durling, Self, Anchorage; Galen Nelson, Self, Anchorage; Vern Johnson, Self, Anchorage; Erin

Renfro, Self, Anchorage; Ben Anglen, Self, Anchorage; Melonnie Amundson, Self, Anchorage; Dale Hoffman, Self, Anchorage; Roger Demoss, Self, Prudhoe Bay; Jeanie Peirce, Self, Kasilof; Jim Beckham, Deputy Director, Division of Oil and Gas, Department of Natural Resources.

SUMMARY

HB 331 TAX CREDIT CERT. BOND CORP; ROYALTIES

HB 331 was HEARD and HELD in committee for further consideration.

Co-Chair Foster reviewed the agenda for the meeting.

#hb331
HOUSE BILL NO. 331

"An Act establishing the Alaska Tax Credit Certificate Bond Corporation; relating to purchases of tax credit certificates; relating to overriding royalty interest agreements; and providing for an effective date."

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^PUBLIC TESTIMONY

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Co-Chair Foster OPENED public testimony. He announced public testimony would be limited to three minutes per testifier.

JACK MCGEE, SELF/ATTORNEY, JUNEAU, spoke about the Carr Gottstein case, which was relevant to the question of whether HB 331 created a state debt. He read from prepared remarks:

The governor and the administration take the position that the language in Section 37.18.030(b) removes all doubt whether a bond issue issued by the corporation, creates a state debt. We're told that this language clearly means that it does not. I don't think that is accurate and it's not accurate because of the supreme court decision in Carr Gottstein. This case involves a lease purchase agreement and the court held it did not create a state debt. What's important is the reason it

> gave. The reason it gave was this, because the lease: 1) contains a non-appropriation clause; 2) it limits recourse to the leased property; and 3) it does not create a long-term obligation binding future generations or legislatures. In order to satisfy this ruling, absent such language in a bond offering or the bonds themselves, I think it will likely find the corporation created a state debt (an obligation) that has to be ratified by the majority of qualified voters.
>
> I don't think it's sufficient simply including language in the legislation such as that that's found in AS 37.18.030(b) unless the corporation is required by statue to include non-appropriation language in the bond offering and in the language itself. The issue comes down to full disclosure to potential bond purchasers.

Representative Ortiz asked Mr. McGee to elaborate further on the Carr Gottstein case that included a non-appropriation clause in the lease. He asked about the impact of the non-appropriation clause.

Mr. McGee referenced page 2, subsection (b) of the bill and read:

> The bonds do not constitute a general obligation of the state and are not state debt within the meaning of art. IX, sec. 8, Constitution of the State of Alaska. Authorization by the voters of the state or the legislature is not required.

Mr. McGee elaborated that "if that's all you have, and it's not in the bond offering or issue, you have a problem of full disclosure." He believed if the bill was contested, the court would find it created a state debt and a majority vote was needed.

Representative Ortiz asked if Mr. McGee believed HB 331 would need to include a non-appropriation clause in order to avoid non-disclosure.

Mr. McGee answered that the clause in the bill would not be sufficient to get past the Carr Gottstein ruling. He detailed it should be included in the document in order for

a party that was thinking of buying the bonds to go in with open eyes.

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Co-Chair Foster noted that Representative Pruitt had joined the meeting.

Representative Wilson asked for verification that the language would have to be on the bond in order for potential purchasers to know whether or not it would be coming back.

Mr. McGee answered in the affirmative. He added the issue documents should contain the information as well.

Vice-Chair Gara asked if including the language in the bond would resolve the constitutional issue. Mr. McGee replied that the language he had read could probably use a bit of clarity. He stressed the importance of clear language.

Vice-Chair Gara hoped the administration would take a look at Mr. McGee's suggestion.

Representative Guttenberg explained that the state's outside bond counsel had been online during the recent Saturday meeting. He recalled that the individual had disagreed with the legislature's attorneys regarding the constitutional issue. He recalled the counsel had been secure in his interpretation that the bill was constitutional as written. He wondered if Mr. McGee believed part of the counsel's interpretation was including or excluding the language.

Mr. McGee responded that if it was included it would be included in the bill section on bond terms; however, it was not included there. He believed the counsel was operating under the assumption that putting the detail in the legislation would be sufficient. He disagreed with that opinion.

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JOSEPH GELDHOF, SELF/ATTORNEY, JUNEAU, spoke against the bill. He provided detail about his professional career as an attorney. He asked if it really had come to not meeting the state's obligations and needing to borrow a substantial

sum of money to pay off tax credits. He discussed that for 30 years the state had been wrestling with tax policy and spending. He believed there were some huge issues remaining. He pointed out that the concept of borrowing to meet past obligations was a new discussion. He did not think there was any question they were talking about floating a debt instrument. He remarked it was possible to include language specifying the borrowing would not be debt, but he believed that was a conclusion that was not supported by critical analysis. He elaborated that the state's constitution required votes for general obligation debt instruments. He believed someone was desperately trying to find a workaround.

Mr. Geldhof remarked that there was frequent debate in the legislature that it was not possible to cut or tax the state's way into a sound fiscal situation. He underscored that it was not possible to borrow the state's way into a financial situation. He characterized the bill's proposal as a clever workaround. He wondered if the state was going to start borrowing finances like Illinois or treating its finances like Venezuela. He believed the bill measure was unconstitutional as proposed. He asked the committee to take its own attorneys into account. He believed the press release from the Office of the Attorney General was a "whistling past the graveyard opinion that says it's okay." He thought the bill would put the state's finances into deeper trouble.

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CHAD SCHAEFER, SELF, SOLDOTNA (via teleconference), spoke in support of the bill. He believed the bill would provide certainty for the state with payments that were not tied to oil price or production. He encouraged the committee to pass the bill to get more Alaskans working.

Representative Ortiz asked for Mr. Schaefer's affiliation. Mr. Schaefer replied he is an Alaska resident.

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GEORGE PIERCE, SELF, KASILOF (via teleconference), testified against the bill. He did not believe there was need for a bond debt on Alaskans. He stressed that the state was in deficit. He supported cuts to the budget. He stated that since the passage of SB 21 the oil industry had

received $1.6 billion in per barrel tax deductions. He believed Alaskans had been short-changed. He discussed that new oil discoveries not on the books meant nothing. The state had every right to pay the minimum credit obligation. He believed paying credits in-full with bonds would reward oil companies for not living up to their obligations to the state. He believed the real crime was the legislature's mismanagement of Alaska's finances. He stated that North Dakota and Texas did not have to sell bonds to pay for their debt. He believed those states taxed oil companies two to three times more than Alaska. He thought the bill represented major oil companies and not Alaskans. He stated that [as a resident] he owned the resources and there were no taxes on his resources. He believed a $1 billion bond should be voted on by Alaskans - the people who own the resources. He believed the legislature needed to quit catering to oil companies and begin working for Alaskans.

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DON BULLOCK, SELF, JUNEAU, shared that he had prior experience and contact with the laws underlying the bill. He detailed that he had heard the testimony from the Department of Law and by Legislative Legal Services. He believed that Emily Nauman's letter from Legislative Legal Services written to Co-Chair Seaton was much closer to the truth than information provided by the Department of Law (DOL). He referenced Article IX, Sections 8 and 11 of the state constitution and noted that general obligation debt had to be generally for capital projects and required a vote of the people. Section XI talked about revenue bonds. For example, if the Knik Arm bridge was built and bonded, there would be a revenue flow from the project - the tolls could be available for appropriation to pay for the bonds.

Mr. Bullock stated that the problem with the bill was that the repayment of the bonds was based on future appropriations. The only asset the corporation created by the bill would have was what was appropriated. He reasoned that in a way the state would not really gain anything because under AS 43.55.028, the statute creating the credit fund consisted of appropriations as well. Additionally, AS 43.55.028 clearly stated that the section did not create a dedicated fund. Almost every designated fund in the General Fund (GF) that was not dedicated would have that language. He believed the structure of the bonds was questionably constitutional.

Mr. Bullock spoke to an additional issue. He stated that under AS 43.55.028 the legislature appropriated the money - when the money was appropriated to buy the tax credit certificates it was an appropriation that was not dedicated (it may be designated) and as money became tighter and tighter in the GF those type of appropriations had to compete with other things like schools, the University, and public safety. As long as an appropriation was for a valid public purpose, appropriations from the GF were allowable. He addressed a scenario where the state sold a bond that it promised to pay back in the future with interest. In the future, the state would have a discretionary appropriation and the pressure of the bond contract. The contractual relationship with the bond holders would add additional pressure and possibly additional litigation between the bond holders and state.

Mr. Bullock noted that committee had recently been told the court system could order the legislature to appropriate the money to pay any kind of litigation like that. The state had a separation of powers - the legislature had the power to appropriate money (the court could not do it and the governor had to request the legislature to make an appropriation). He stated that the issue had been seen in the Kasayulie case pertaining to education funding in rural areas. He detailed that the legislature had basically been signaled to appropriate more money to bring some of the standards up. He cited another case involving overcrowding in prisons. The court had found that prisoners were overcrowded, and more money had to be appropriated to create more places to house prisoners. He reiterated that the court could not appropriate the money. The Kasayulie case had been settled when the former Parnell Administration agreed to put requests into the budget for additional school funding. In the case of general obligation bonds, which were not used in HB 331, there could perhaps be a court order to liquidate some assets because those type of bonds had the full faith in credit.

Mr. Bullock believed the best opinion the legislature had was the non-partial opinion by legislature's own attorneys. The question of constitutionality raised a possible challenge to the bill. He was also concerned about another sense of entitlement based on the contract against the GF.

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Mr. Bullock believed the foundation of the bill was built on sand. He stated that AS 43.55.023 and AS 43.55.025 create the opportunity for tax credits. Statutes directed companies to apply to the state to receive a tax credit. He stated there were three ways the tax credits could be used. He likened credits to an income tax return where credits could be taken to reduce tax liability dollar-for-dollar. He noted it was different than a deduction because it was an actual reduction in tax. The credits were issued in return for the desired activity or investment taking place - the person holding the credits could hold them until they could use them, they could sell them to another taxpayer, or they could be presented to the state for payment. There was no dedicated fund to pay those taxes. A source was identified; a certain percentage of the production taxes were received. He stated that when things were good there were higher production taxes whatever percentage went into the fund would be higher. At the same time, there were lean times - when production taxes went down there was less available from the identifiable fund source.

Mr. Bullock underscored there was no requirement for the taxes to be put into a credit fund - the funds were discretionary. The discretion to appropriate money would be the same as the discretion if the bill passed to fund the bonds. He thought the bill had been characterized as an obligation of the state to pay the bonds. He stressed that at best it was discretionary. He clarified he was not saying there were not any impacts or that people did not expect to be paid. He remarked that when the state had the money it bought everything on the shelf; in the past it had paid the full amount to companies. However, it did not amend the law that reasonable expectation would be that the state would always buy "them" because there was no dedicated fund or requirement.

Mr. Bullock continued that tax credit certificates were issued with a face value that did not gain interest or grow. He shared that he had a zero-interest loan on his car and had no incentive to prepay. The credits were a liability to the state, which was something necessary to consider - potentially every credit issued would reduce future tax payments to the state. He added that the credits did not expire. He equated it to the risk of a gift card - some people never used them and others did. He explained that credits could be sold to a company that could use

them. For example, a company could discount the sale of credits to a taxpayer - there were limitations on how the credits could be applied - and there would be a future reduction in tax. He continued that if the state had the money and could negotiate the outstanding credits, perhaps it could bid against the other taxpayers. For example, if another buyer was going to offer less for the credits, the state would be ahead if it could offer 80 percent of the value of the credit because the treasury would not lose the money. The trouble was, if the state did not have the money, it would have to wait. He did not believe the bill was the way to go. The liability for payment on the bonds and future appropriations was worse than looking at the credits owed now.

2:04:51 PM

Representative Wilson asked if the bill would be constitutional if it included putting language on the bonds that read "good luck, we hope you get paid."

Mr. Bullock did not believe putting the language on the bonds mattered. He elaborated that the laws would still be on the books if the language was not on the bonds. The current law had discretionary language and did not always allow bills to include the terms "must" and "shall" instead of "may." Part of the problem with the credits was they had been assigned with the expectation the legislature would appropriate the assignments, which was where the concern of financial lenders resided. He stated that whether the credits would be purchased was based on the state's ability to purchase the credits.

Representative Wilson spoke to a proposal that in order for the state to pay the credits there would be some sort of requirement for increased development. She asked Mr. Bullock whether he did not believe it was a good tradeoff to potentially help the state's economy versus less development.

Mr. Bullock answered that any kind of state money into the economy was always beneficial; however, the law did not allow for that. The law provided the credit and perhaps a purchase by the state based on available money. He stated it was always good to spread the money, which was part of the issue of the Permanent Fund Dividend where state money went out to help the economy. The state's major industry

was in oil and gas - the state took a balanced approach between what it gave up and what it could expect in the future. He had testified in the past that when the state decided to an act of deduction or credit it was effectively making an investment of state money. He recommended identifying what the state expected in conjunction with the credit and whether it was a good outlay. Especially a targeted credit going towards incentivizing production. He added that some of the credits were received for dry holes, but at least that meant companies were out exploring.

Representative Wilson asked if there would be legality issues attaching certain work being done on money being paid to companies, especially when they had completed projects.

Mr. Bullock answered that the expectation of qualifying for the credit was to receive a credit. There was nothing binding saying they would be paid, which would be dedicating future revenue at some point to buy the credit.

Representative Wilson clarified that she was speaking about a proposal to require companies to reinvest in order to get the larger amount of money for the credits.

Mr. Bullock believed it would be acceptable because it would be like settling it. The state did not have the money to appropriate to buy the credit, but it would offer a company a discount. The credit would be discounted in a smaller way if the company made a commitment to keep working. He stated it was like getting another credit or another deduction; it was an incentive to go forward. He liked the idea of the overriding royalty - another thing that would contribute to the government part of the state.

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Representative Guttenberg thanked Mr. Bullock for all of his work for the legislature in the past. He stated that the state's current relationship with the credits was as a sovereign and a taxpayer. He believed the bill would change the structure to a commercial relationship between two parties. He asked if the state lost anything if the relationship changed.

Mr. Bullock asked for clarity on the two parties.

Representative Guttenberg explained he was referring to the state entering into a contractual relationship with the industry.

Mr. Bullock replied that he did not believe so. He detailed the state wore two hats - it was the resource owner (it received royalty payments) and it was the tax collector. Those things would not change. He continued that if the state got into the overriding royalty situation, it would have an additional interest in production. He clarified it was not the same as the royalty the state generally received, which came off the top as payment for something. He provided an example. He did not believe it changed the relationship with the state - it would continue to be a resource owner and tax entity.

Co-Chair Foster recognized Representative Charisse Millett in the audience.

Vice-Chair Gara thanked Mr. Bullock for all of his years of service. He appreciated the testimony.

2:12:05 PM

Co-Chair Seaton asked if the major problem with the bill would be solved if there was a revenue stream associated with the bond.

Mr. Bullock answered in the affirmative. The idea of revenue bonds was there was an identifiable source. Conceivably if there was an overriding royalty as part of the deal, it could be a revenue source. He speculated anything could be bonded for a price - as the risk increased, the interest in buying the bonds would be less, but the interest the state would have to pay to sell the bonds would be higher. An identifiable revenue source provided some comfort to the bond buyers - a buyer could reason that it was a good contract with overriding royalties on known fields that would continue to produce. He stated that revenue bonds were authorized under Article IX, Section 11 of the state constitution; the bond buyer could look at the source. He detailed that the state did everything it could to meet its legal obligations. He mentioned constraints like the dedicated fund. Under the bill, a bond buyer would have to speculate about whether there would be money for future appropriations. Depending

on the extent of the revenue shortage, the buyers may not get paid.

Co-Chair Seaton asked an overriding royalty would have to be designated to the [AS 43.55] .028 fund. He wondered if it would present dedication problems. He wondered whether revenue would have to generate to the corporation or GF as long as revenue was being generated.

Mr. Bullock affirmed that it would raise dedication problems. He elaborated that the state's revenue was sacred apart from for specific exceptions in Article IX, Section 7 regarding dedicated funds. There were several cases about limitations and dedication including the recent Permanent Fund Dividend case and the University lands case. He highly recommended reading the latter case summary regarding anti-dedication clause rules. He spoke to the importance of caution. He discussed that the constitution had been written in the 1950s when the state's population had been much smaller. He continued that the state had known its government would have to survive somehow. He shared that Alaska and Georgia were the only states with anti-dedication provisions, which gave the legislature maximum flexibility. Some states were handicapped by dedication after dedication.

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Co-Chair Seaton provided a scenario where the overriding royalty was perceived as a revenue stream to the GF. He asked if the language specifying the revenue may be appropriated to the [AS 43.55] .028 fund satisfied the appropriation power and produced a revenue stream.

Mr. Bullock could not comment on the question. He stated it was a nontraditional revenue stream. He reported the case closest to the dedicated fund issue was Meyers v. Alaska Housing Finance Corporation. He detailed the case was related to a tobacco settlement. Effectively the state sold an asset (the right to future income that would be paid by the tobacco companies) and the legislature appropriated the money from the sale. He detailed that because the money was to be received over time, it raised the dedicated fund issue; however, because it was the sale of an asset followed by an appropriation, the court allowed it. He noted it had been a close case; he did not know if the same outcome would occur if the issue arose again.

Representative Pruitt asked if it was possible for the state to sell a share of future royalties to a corporation.

Mr. Bullock answered that the Permanent Fund had been created with a dedication of royalties that could not have been done without a constitutional amendment. He detailed that because royalties were a cash flow based on the state's ownership, it would violate the dedicated fund prohibition.

2:18:40 PM

BARBARA HUFF-TUCKNESS, DIRECTOR, GOVERNMENTAL AND LEGISLATIVE AFFAIRS, TEAMSTERS LOCAL 959, JUNEAU, spoke in support of the bill. She spoke to the amount work the small independent contractors had done over the past couple of years during a time of reduced work opportunity and the backing off of the credits reimbursement. The organization believed there was a work opportunity here. She stressed the small independent contractors had done a good job working with Nanuq Inc. and AFC [Alaska Frontier Contractors]. The independents included ENI, Caelus, Armstrong, Repsol, and Brooks Range. Over the past couple of years, the companies had worked closely with Alaskan contractors; Teamsters members had enjoyed much of that work opportunity. She added there could be more work opportunity. Unfortunately, the opportunity to discuss local hire was not included in the bill, but the organization commended the administration for what it believed was an innovative way to allow for some of the tax credits through the bonding process. She underscored the importance of jobs to the Alaskan economy. She added that the industry jobs paid good money.

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DOUG SMITH, CEO, ASRC ENERGY SERVICES, ANCHORAGE (via teleconference), testified in support of the bill. He provided detail about the company that had 85 percent Alaska hire. He remarked on the confusing nature of the issue. He reported he had a large meeting that night with other Alaska businesses to discuss the issue and he needed clarification. He explained the company's understanding of the oil credit obligation by the state to oil companies. He wanted to know if he was obligated as a resident to pay the credits annually over time. If so, if the bond deal would

allow the state to pay the credits up front at a discount and not cost Alaskans any more in the long run than it would eventually pay and hopefully generate economic activity in the process, he needed to understand how it was not good for every Alaskan.

Mr. Smith clarified that most of the oil companies holding the tax credits were not large. One of the tax credit holders was the Arctic Slope Regional Corporation (ASRC). He provided detail about millions of dollars in investment. He stressed that equipment the company had spent millions on would be covered by the bill and reduced utility costs in Interior Alaska by 30 percent. The investors did not only include oil companies - he listed Ahtna as an example. He spoke to anchored high rates of Alaska hire and employing companies also experiencing the tax problem. He believed the resource belonged to Alaskans too, but in 1958 the state had $54 million in its Permanent Fund and as of Monday it contained $64 billion. He underscored that the state did not get there without co-investing and developing by oil companies. The bottom line was, the state had benefitted from development of its resources.

Mr. Smith stated that under Alaska's Clear and Equitable Share (ACES) the state had taken more money from industry and had implemented a credits system for balance. The state had enjoyed many years of extra money coming in. He referenced the past energy dividend to all Alaskans by former Governor Sarah Palin. He stated that the state had put its word behind the obligations. He stressed the state's word had to be worth something. The state needed to stand behind the credits and ensure it was getting value for the deal. He spoke to the need of getting people back to work. The organization's support for the bill was about Alaskans and Alaskan paychecks. He asked for clarification on whether the state would ever pay the debt with or without the bill.

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CATHY DUXBURY, SELF, ANCHORAGE (via teleconference), testified in support of the bill. She agreed with the prior testifier. She did not understand the testimony pertaining to constitutionality. She stressed that the bottom line was that the state owed the credits to oil companies. She believed the liability made Alaska look unstable. She did

not understand what made the legislature think it was okay to not pay the money back. She supported the bill.

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JAMES SQUYERS, SELF, RURAL DELTANA (via teleconference), spoke in opposition to the bill. He referenced all of the concern about statutory obligations regarding oil and gas credits; however, he saw no concern for the statutory obligation to recognize the unpaid Permanent Fund Dividend (PFD) in the past few years. He wondered where the discussion was to bond for the unpaid PFD obligation. He asked how oil and gas credits became a preferred creditor over the PFD debt. He wanted to hear whether the House's proposal for the statutory minimum on the credits could be supported at $49 million versus $184 million (the difference between the House and Senate amounts). He spoke about a cash flow triage where the state could not afford the statutory minimum. He recommended bonding for the agreed upon statutory minimum instead of binding the state to a more rigid payoff schedule. He stated that if the dog were wagging its tail, the legislature would be working towards a sustainable budget number, cutting and tucking as necessary. He believed the tail was wagging the dog in the legislature. He surmised that if the legislature decided to bond for the oil and gas credits, it should bond the same amount to pay off the statutory PFD obligation. He reasoned it would be immediately injected into the state's depressed economy with a multiplier of 1.4.

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KEVIN DURLING, SELF, ANCHORAGE (via teleconference), testified in support of the bill. He shared that he had made a living in the oil and gas industry. He stressed that the state had agreed to a financial commitment to oil companies. Subsequently, the companies had spent money in Alaska, hired Alaskans, developed resources, and located additional resources. Since the state had stopped meeting its commitment, the companies could not go out to bring more resources to market. He believed that getting the bonding done on the front end would result in $150 million in interest savings for the state. Companies that could raise funding were paying three times the market rate to get the funds. He believed if the same was true in the housing market it would dry up. He strongly supported the bill and meeting the state's obligations.

2:31:30 PM

GALEN NELSON, SELF, ANCHORAGE (via teleconference), spoke in favor of the bill. He shared that in the past few years he had seen countless friends and family members lose jobs or moving to other states for work. He spoke to constraints put on small companies that were in the state to do business and employ Alaskans. He had seen the amount of work that could be done with an influx in capital in the oil industry. He stated that when money was not paid it meant companies had to lay people off and shut down projects. He thought it was sad to think he may need to move from Alaska to support his family.

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VERN JOHNSON, SELF, ANCHORAGE (via teleconference), testified in support of the bill. He agreed with testimony given by Mr. Smith, Mr. Durling, and Mr. Nelson. He had moved to Alaska 18 years earlier to work in the oil industry. He had seen a dramatic shift over the past several years, especially when the state had pulled support for the small companies by shutting down tax credits. He supported turning the situation around, which would help investment and getting Alaskans back to work. He reported that the slowdown in payment had impacted him, his family, business associates, friends, and other. He had seen many friends get laid off or have to move to the Lower 48 to find work in the oil field.

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ERIN RENFRO, SELF, ANCHORAGE (via teleconference), spoke in support of the bill. She worked in the oil industry. She had seen many friends lose their jobs because of the downturn and because the state had pulled back its obligation to pay the credits. She believed the sooner the credits were paid, investment would begin again, and Alaskans could get back to work.

2:35:31 PM

BEN ANGLEN, SELF, ANCHORAGE (via teleconference), spoke in favor of the bill. He stressed that the state had made a commitment to pay the tax credits to oil companies that had made investments in Alaska. He elaborated that companies

could be cash-poor and in debt to large financial institutions. He thought it was unbelievable the state would not pay what it had committed to without any specified payment schedule going forward. The issue was hurting the state's reputation in the investment community. Paying the credits or providing a payment schedule would increase future investment by the oil industry and would increase jobs in the state.

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MELONNIE AMUNDSON, SELF, ANCHORAGE (via teleconference), testified in support of the bill. She worked for the oil industry. She had seen many negative impacts of not paying the tax credits including job loss and the postponement of projects. She believed the bill was a win-win for the state and Alaskans. She wanted to get Alaskans back to work.

2:38:15 PM

DALE HOFFMAN, SELF, ANCHORAGE (via teleconference), spoke in support of the bill. He shared that he worked for Caelus Energy Alaska. He had seen the impacts the situation had at Caelus - many people had lost their jobs and there were individuals eager to get back to work. He believed the bill would get oil investment back on track in Alaska.

2:39:01 PM

ROGER DEMOSS, SELF, PRUDHOE BAY (via teleconference), testified in favor of the bill. He had seen people working in the oil industry get laid off. He thought the bill was a win-win for the state. He wanted to see some projects start up.

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JEANIE PEIRCE, SELF, KASILOF (via teleconference), spoke against the bill. She believed the issue should be taken to the state residents for a vote. She reminded the committee the oil companies had been paid handsomely to extract oil in the state. She stated the bill was about paying the minimum or the maximum. She stressed that the state could not afford to pay the credits at the present and she did not believe companies had lived up to their obligations. She remarked that the state had not been receiving the bang for its buck since the passage of SB 21. She emphasized

that the PFD had been ripped off from people who were in bad times. She continued that the rate of people on welfare had increased and the state could not afford the credits to save a few jobs. She opined that the jobs were being thrown away by companies that wanted the credits to be paid. She wondered if the state was paying for less than it got. She thought there was something wrong when everyone had to be propped up.

Co-Chair Seaton thanked Ms. Peirce for calling.

Co-Chair Foster CLOSED public testimony. He reviewed the schedule for the remainder of the meeting.

Representative Wilson asked if there was any additional written testimony besides two letters in the packets.

Co-Chair Foster replied in the negative.

Co-Chair Foster transitioned the meeting to a discussion on the overriding royalty interest agreement and qualified capital expenditures in Section 10 of the bill with the Department of Natural Resources (DNR).

2:43:33 PM

JIM BECKHAM, DEPUTY DIRECTOR, DIVISION OF OIL AND GAS, DEPARTMENT OF NATURAL RESOURCES (via teleconference), spoke to the overriding royalty interest portion of the bill. He explained that the department would evaluate an additional agreement with an applicant. According to the bill there were seven or eight provisions that would have to be met and considered by the division in determining whether the overriding royalty interest or additional payment would meet the requirements of the lesser discount rate. The department would probably exercise the evaluation on a case-by-case basis because not all companies, leases, and production are the same. The work would be done by the DNR commercial analyst in the division's Commercial Section and it would work with the Department of Revenue (DOR) to determine whether what DNR found met DOR's requirements for the lesser discount rate.

Co-Chair Foster asked Mr. Beckham to comment on the qualified capital expenditures.

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AT EASE

2:46:06 PM
RECONVENED

Representative Guttenberg asked about the end of Section 10 on page 14. He referred to language in the section and asked what the meaning of commitment to the department meant in the case of the bill.

Mr. Beckham responded that he had not had an opportunity to look at what the commitment to the department would be. He interpreted the language to mean the commitment to give the department an overriding royalty interest in an amount and form that met the requirements of the eight criteria DNR was required to evaluate.

Representative Guttenberg asked Mr. Beckham to provide information regarding the criteria.

Mr. Beckham answered that the criteria DNR was supposed to evaluate for an offer of an overriding royalty interest included the anticipated cost for the issuance administration of the bonds, the production or projected production from the lease or leases subject to the proposed agreement, the value or projected value of the oil produced from those leases, the timing of the production (when production would occur and what the rates would be), and the likelihood of production from the lease if not currently under production. The department also had to consider the existence and burdens of other interests on the lease or leases being proposed - whether there were any other overriding royalty interests, any other expenses, liens, or claims to the leases, and any other information submitted with the offer or requested to be considered by the department.

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Representative Guttenberg asked if there was any oversight aside from the executive branch. He wondered if all of the agreements fell under the umbrella of confidentiality.

Mr. Beckham replied a certain amount of information would be subject to confidentiality agreements (e.g. a company's financial reports and any other internal information that could be considered proprietary). He believed after the

evaluation had been conducted by the Commercial Section, coming out with a certain percentage or payment rate based on the evaluation (including timing and amount) would be public information.

SHELDON FISHER, COMMISSIONER, DEPARTMENT OF REVENUE, highlighted that within HB 331 the word "department" when not otherwise defined, referred to DOR. Section 2, page 14 pertaining to overriding royalty interest, specifically referred to DNR. Section 3 pertained to DOR and the commitment where the credit holder/applicant would make a commitment to DOR that it intended to invest over a 24-month period, an amount equal to or greater than the amount they were receiving in the payment, which would allow them to qualify for the lower discount rate.

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Representative Guttenberg remarked that qualified capital expenditures were terms of art under tax law. He spoke to a situation where the commercial interests of the credit holder diverged from the state's (the state's interest was in production), but the credit holder was still qualified for qualified capital expenditures under the tax code. He asked how to reconcile something that may qualify under the tax code but was not in the state's best interest. He asked if there was a place where the state could challenge it.

KEN ALPER, DIRECTOR, TAX DIVISION, DEPARTMENT OF REVENUE, confirmed that qualified capital expenditure was a term of art in tax statute. He stated it was the origin of the old 20 percent capital credit from the PPT [Petroleum Production Tax] and ACES tax regimes in AS 43.55.023(o). An expense had to meet two criteria to be a qualified capital expenditure: 1) it had to be a lease expenditure (a broader definition meaning an upstream spend on the oil field), and 2) it was a depreciable expenditure under certain criteria of the IRS code (a capital expenditure). As written it was the only restriction on what it may be in the bill. Previously the state had said that for the most part, the credit holders were oil companies that had discovered something and had intent of bringing the resource into production. He believed the capital expenditures the companies would be embarking on would be the sort of thing he believed the legislature would want - developing oil towards production. It was difficult to imagine some other cost the companies may pursue that would not meet that

criteria; however, it was fair to say that the bill did not restrict that from happening. He continued that if there was a desire to include some brackets or limitations, the appropriate place would be on page 14, subsection (m)(3).

Representative Guttenberg remarked that when someone was working on the North Slope and it was all upstream it was hard to imagine there would not be a difference at some point.

Mr. Alper answered that DOR had an internal conversation about the issue. He explained that if the bill was meant for the long-term it would be a larger concern. He elaborated that with the bonding program, the great bulk of all of the decisions would be made in the first few months based on existing expenses and credits. He agreed that in 5 to 10 years there would be demobilization costs and late-stage maintenance costs; however, those issues did not come into play for the decisions specific to the bill and repurchase effort.

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Representative Wilson provided a scenario where a company already had a plan filed with DNR that may have changed because it did not have the money to follow through. She wondered if the company could use the existing plan as long as it fell underneath what a capital expenditure would be or whether they would be required to rewrite the plan. Alternatively, she wondered it DOR would require a plan.

Commissioner Fisher answered that the company would present a plan that would be a commitment for the 24-month period after the plan was submitted. He detailed that while DOR and DNR collected certain information, it was difficult to define it as a baseline. The department's proposal, which was reflected in the bill, would look forward to the commitment without respect to what preexisting plans may have been in the past.

Representative Wilson was trying to figure out what it [the plan] looked like. She wondered if it was a one-page document. She used Petro Star as an example - the company was going to do the asphalt portion, which would be fairly easy and would have included plans. She believed a plan was already required for leases to show when a company was going to move forward with development.

Commissioner Fisher replied that the department had not prescribed any particular document size. He imagined it would be fairly detailed and would describe the work a company intended to do over a period of time. He imagined most companies would have the material already for their internal work. He continued that the companies would attach a cost or budget as well. The department would look for whether the company had sources of capital and could reasonably make the commitment because it had secured commitments from lenders or other investors. Based on that information the department would allow the company to qualify for the reduced rate.

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Representative Wilson asked what would happen if the weather was poor or for some other reason the company was unable to follow through with its plan.

Commissioner Fisher replied there had been discussion there would be some sort of consequence if the companies did not follow through with the plan. He believed an amendment may be drafted in that regard. The department was comfortable with the notion that the company may have to pay back whatever decrement they did not invest so that they did not receive a benefit. The department was not looking for massive penalties, but there would be a true-up if the companies did not spend the expected amount.

Representative Wilson stated the company would have to earn the benefit twice. She did not want the companies to have to pay for something that was not their fault. She was uneasy about some of the items being in regulation and what it could possibly look like.

Co-Chair Foster asked the committee if it had additional questions for Mr. Beckham.

Representative Wilson did not understand the overriding royalty interest. She asked if the department could put something in writing with a hypothetical example. She understood they did not want to give any confidential information. She did not know if there would be a loss of funding or whether the state would get more funding.

Mr. Beckham would follow up in writing.

Co-Chair Seaton asked for the information to be sent through the co-chairs.

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Vice-Chair Gara thought the majority of the legislature would like to find a way to pay off the tax credits more quickly. He believed the bond bill represented a good faith effort to try to do that. His mind was not yet made up. He did not think there were any legislators who did not believe the credits were a state obligation. He did not think it helped the state's ability to attract business when the argument was given that the state had not honored its commitments. He clarified that the state had honored its commitments. He acknowledged that it may not have been as quickly as some would like. He reiterated that the legislature had paid the statutory due amounts. He did not believe the discussion did not help the state's ability to attract business. He asked the administration to spread the word that the state had honored its statutory commitments. He remarked that if the state continued to pay 10 percent of the revenue it got from oil production taxes, it would take 20 years at $40 million per year. He believed the state needed to do better than that, but he reasoned it was what people had signed up for. The state would try to do better than what people had signed up for. He did not believe it helped the state's business climate.

Commissioner Fisher believed the sentiment was fair. He remarked that he had probably been personally guilty of making some of the statements. The attempt of the bill was to balance a number of perspectives. The underpinning of the bill was based on the view that the state had an obligation over time and therefore inviting or asking the industry to take a discount was a reasonable request because it was an obligation over time. He speculated that he and Vice-Chair Gara probably disagreed about some of the differences, but he appreciated Vice-Chair Gara's comments. He would try to be more mindful about the issue.

Co-Chair Foster asked if there was anything more Commissioner Fisher wanted to put on the record before moving on.

Commissioner Fisher referenced statements that the bill was about debt and debt had to follow within certain criteria

within the constitution. He referenced the Carr Gottstein v. State case and spoke to the distinction between debt and constitutional debt. He read from the Alaska Supreme Court case findings:

> When taken together, this court finds that the foregoing Alaska cases and the cases cited by the Alaska Supreme Court define constitutional debt as a term of art used to describe an obligation involving borrowed money where there's a promise to pay whether funds are available or not.

Commissioner Fisher stated in other words that it was not subject to appropriation, which was the administration's basic premise. He did not mean to reopen the debate, but he wanted to highlight that the Alaska Supreme Court had made a distinction between constitutional debt (that had certain requirements and a process that had to be approved by the legislature and voters and the consequence of some fairly strict obligations to pay) versus other forms of debt that did not fall into the same bucket.

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Representative Guttenberg referenced public testimony by Mr. McGee about what would be in the issuance of the bonds regardless of the constitutionality of the question. He looked at page 4 of the bill that specified "nothing in this section creates a debt or liability to the state." He asked how it would impact someone looking to purchase bonds.

Commissioner Fisher answered that the bond obligation and documents would specify (in multiple places) the money was subject to appropriation by the legislature. He clarified that the language was included not because the administration thought there was a constitutional requirement to do so, but because securities laws require that all material facts be disclosed.

Representative Guttenberg stated there was a comment earlier that many of the things "that we've opened here" may increase the cost of the issuance of the bonds. He asked if "this" would be one of them.

Commissioner Fisher answered that subject to appropriation debt was typically a bit more expensive than a general

obligation bond, which had been factored into DOR's estimate on the cost of the debt. The 3.7 percent estimate based on current market conditions was for subject to appropriation debt. He explained that if it was general obligation bond debt it would be less.

Representative Guttenberg spoke about the signed lease agreement the state had signed with the remodeler of old Legislative Information Office [in Anchorage]. The state had paid a premium in the lease agreement because it had been included in the lease. He remarked that "now we're going from $35 or $40 million to $800 - $900 million." He surmised it seemed it would be a risky thing in a state without a stable fiscal climate to enter into purchasing those bonds. He was trying to determine how much it would cost.

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Commissioner Fisher answered that it would be less than 0.5 percent increase in debt rate. The marketplace had contemplated that. He noted that Deven Mitchell, Executive Director, Alaska Municipal Bond Bank Authority, Department of Revenue had testified there was an appreciation that the bonds represented a commitment to the marketplace. He believed the administration was taking the bonds as a very serious commitment and while it was subject to appropriation, the administration expected that money would be appropriated. He recognized appropriation was up to the legislature, but there would be substantial consequences to the state's credit rating if the money was not appropriated.

Mr. Alper elaborated it was important to recognize the 3.6 and 3.7 percent [cost of debt] figures were estimates. He furthered that if the discussion about constitutionality had injected uncertainty into the market and the state found it actually needed to give 4 percent, it would find its way through the formula and would result in a lower amount paid to the companies based on the total interest cost plus 1.5. The state was not really exposed in the deal, but the tax credit holders would receive an incrementally smaller payment.

Representative Ortiz referenced the legal opinion from Legislative Legal Services and the public testimony by three attorneys and asked whether it would be a leap of

faith to pass the bill because its constitutionality was in question.

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Commissioner Fisher wanted to be respectful of the opinion the legislature received, but he did not believe the bill's constitutionality was in question. He detailed that the state had issued the same kind of debt many times prior to and after statehood. He referenced earlier testimony that DOL was an advocate for the governor. He clarified that DOL had held the same position for many years under administrations with varying political persuasions. He understood the administration could not get an attorney general (AG) opinion to the legislature in the available timeframe due to the time the process took. He detailed that an AG opinion was almost quasi-law in terms of its standing. He believed the committee had heard the state's bond counsel testify that counsel needed the AG opinion in order to issue their opinion. For the state to issue bonds, it required an opinion from outside bond counsel (there was a certain amount of liability the counsel assumed by providing the opinion). Outside counsel had communicated they would require an AG opinion. He reiterated that he wanted to be respectful, but he did not believe there was a constitutional issue.

Vice-Chair Gara stated that if the AG and bond counsel determined the bill was constitutional, he was willing to go with that. He remarked that it was not relevant that the state had issued the same type of debt in the past if it had never been challenged. He continued that it was relevant if the issue had been challenged and there had been a supreme court ruling. He reasoned that issuing the debt and not having it be challenged did not create precedent. He underscored that precedent mattered.

Commissioner Fisher answered that [the past] was relevant because it appeared legislators and administrators who had been closer to the constitutional convention and the meaning that the drafters ascribed to the words, had issued the same kind of debt. He agreed it was not dispositive, but he believed it had some persuasive reasoning if people close to the drafting of the constitution believed it was legal.

Vice-Chair Gara stated that the constitutional history was fascinating, and he had read the constitutional minutes. He remarked when there was a body of people who agreed with something at the convention it gave significant weight when interpreting the constitution. There were also times when one person had said something that was not necessarily reflective of the intent of others. He had not read the constitutional history on the issue. He was not necessarily convinced by that argument at present.

HB 331 was HEARD and HELD in committee for further consideration.

Co-Chair Foster clarified that the amendment deadline was Wednesday at 5:00 p.m. He recessed the meeting [note: the meeting never reconvened].

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ADJOURNMENT

3:18:00 PM

The meeting was adjourned at 3:18 p.m.