

**ALASKA STATE LEGISLATURE
HOUSE RESOURCES STANDING COMMITTEE**

January 22, 2018

1:03 p.m.

MEMBERS PRESENT

Representative Andy Josephson, Co-Chair
Representative Geran Tarr, Co-Chair
Representative Harriet Drummond
Representative Justin Parish
Representative Chris Birch
Representative DeLena Johnson
Representative George Rauscher
Representative David Talerico
Representative Chris Tuck (alternate)

MEMBERS ABSENT

Representative Mike Chenault (alternate)

OTHER LEGISLATORS PRESENT

Representative Paul Seaton

COMMITTEE CALENDAR

HOUSE BILL NO. 288

"An Act relating to the minimum tax imposed on oil and gas produced from leases or properties that include land north of 68 degrees North latitude; and providing for an effective date."

- HEARD & HELD

PREVIOUS COMMITTEE ACTION

BILL: HB 288

SHORT TITLE: OIL AND GAS PRODUCTION TAX

SPONSOR(S): REPRESENTATIVE(S) TARR

01/16/18	(H)	READ THE FIRST TIME - REFERRALS
01/16/18	(H)	RES, FIN
01/22/18	(H)	RES AT 1:00 PM BARNES 124

WITNESS REGISTER

No witnesses to report

ACTION NARRATIVE

[1:03:21 PM](#)

CO-CHAIR ANDY JOSEPHSON called the House Resources Standing Committee meeting to order at 1:03 p.m. Representatives Josephson, Birch, Parish, Talerico, Rauscher, Tuck (alternate), Johnson, Drummond, and Tarr were present at the call to order. Also present was Representative Seaton.

HB 288-OIL AND GAS PRODUCTION TAX

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CO-CHAIR JOSEPHSON announced that the only order of business would be HOUSE BILL NO. 288, "An Act relating to the minimum tax imposed on oil and gas produced from leases or properties that include land north of 68 degrees North latitude; and providing for an effective date."

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CO-CHAIR TARR informed the committee HB 288, in a manner similar to other proposed legislation, is before its first committee of referral and many changes will be made as the bill is discussed. She directed attention to a PowerPoint presentation entitled, "House Bill 288 Fairness in Oil Taxes," [undated] and recalled the House majority coalition announced last session there are four pillars to its [fiscal plan]: strategic cuts; oil tax fix; broad-based measure; percent of Market Value (POMV) [from the Earnings Reserve Account of the Alaska Permanent Fund] (slide 2). She recalled the plan began [in 2017] with a major tax fix, which was the removal of the cash credit system. Further, House Bill 111 [passed in the Thirtieth Alaska State Legislature] created a bicameral/bipartisan working group, which seeks to continue working on oil tax structure.

REPRESENTATIVE JOHNSON urged for the aforementioned working group to make recommendations regarding the proposed legislation.

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CO-CHAIR TARR directed attention to slide 3, noting the fundamentals of the current oil tax structure remain in place [within HB 288] including the 35 percent tax base rate, the per

barrel credit, the gross value reduction, the minimum tax, and the lease expenditure deductions. She pointed out [HB 288] would change one calculation for the minimum tax, but the working group will focus on the fundamental structure of Alaska's oil tax because [legislative] consultants have made recommendations to improve the fundamental oil tax structure (slide 4). For example, consultants have noted the oil tax functions as both a gross and net profits tax; she attributed the decision to choose the system enacted by Senate Bill 21 [passed in the Twenty-Eighth Alaska State Legislature] to the price of oil at that time, which was \$100 per barrel. Since the enactment of Senate Bill 21, when oil is at lower prices, the state's tax structure functions as a gross tax, and when prices are higher it functions as a net profits tax. Currently, the tax structure is functioning as a gross tax, and she opined [the minimum tax] should be between 10 percent and 18 percent instead of 4 percent. Another challenge with the current system is it has components of both a severance tax and a corporate income tax and she explained that a severance tax is applied once to the value of a nonrenewable resource; however, corporate income tax allows oil companies to deduct for the same expenses in both severance and corporate income taxes. Co-Chair Tarr advised the working group will discuss a severance tax, carryforward losses, and other components more typical of corporate income taxes. A third challenge to the existing system is there are too many components linked to price - for example, oil prices have fluctuated by \$25 to \$50 in one year - and consultants suggested a more appropriate link is to the production tax value (PTV). Finally, the present system is too complicated, and she gave an example. Co-Tarr stressed understanding oil tax revenue will be integral to Alaska's budget for the foreseeable future.

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CO-CHAIR TARR continued to slide 5 and acknowledged at this time the state has heard lots of good news related to exploration, new development, the National Petroleum Reserve-Alaska (NPR-A), and lease sales, but there are looming budget deficit issues. She advised the announcements of good news should be followed by three questions: How much profit per barrel, how many barrels total, and how much revenue would there be to the state? (slide 6). She reviewed the current tax structure on expenditures and costs - at oil prices ranging from \$40-\$140 per barrel of taxable oil - and identified each component at a \$60 per barrel oil price (slide 7). She opined the impact of per barrel credits at lower oil prices was not discussed during the debate

on Senate Bill 21: the net tax [at \$60 per barrel of oil] is negative.

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REPRESENTATIVE BIRCH pointed out revenue from royalty share is not reflected on [slide 7]; in fact, if there is no oil production, the state does not receive any royalty revenue, and if revenue from royalty is not considered, [slide 7] is a misrepresentation of the overall state revenues that are derived from increased production.

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CO-CHAIR TARR said information on revenue from royalty shares will be reflected on upcoming slide 9. She observed one of the challenges to interpreting data is all companies differ related to expenses and operations and Department of Revenue (DOR) aggregate data is based on averages, thus "it doesn't tell the full story." She noted a consultant recommended looking at the tax as a percentage of PTV, not as a percentage of gross value at the point of production (GVPP) or as a percentage of price. This would be a true net profits tax system with allowable expenses deducted before the tax is applied, and would result in the current effective rate of 10 percent (slide 7). Representative Tarr opined a 10 percent tax is not working in Alaska's favor, and there are lessons to be learned about the volatility of oil prices. She directed attention to slide 8, which illustrated state oil tax revenue, using 20,000 barrels as an example; this amount was used in the example because the increase in oil production on the North Slope has been approximately 20,000 barrels per day. She concluded increased production of 1.2 billion barrels of oil is needed to equal the budget shortfall of \$2.5 billion.

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CO-CHAIR TARR continued to slide 9, which used the example of 20,000 barrels per day and a 12.5 percent royalty rate to estimate royalty revenue. Calculating royalty uses GVPP, thus with taxable barrels added to royalty share barrels, the state would need to produce about 47 billion more barrels of oil [to equal the budget shortfall of \$2.5 billion]. She reviewed the prospects of new discoveries and possible future increases to oil production affected by property and corporate income taxes, and related the industry has concerns about the lack of stability, planning, and overdue unpaid oil tax credits. Co-

Chair Tarr continued to slide 10, which illustrated changes to the revenue stream by increased minimum tax rates. Also shown on slide 10 were the impacts of taxes at \$60 oil prices on legacy and new fields, and she provided examples. Co-Chair Tarr suggested the committee discuss modest [minimum tax] adjustments at a rate that could be made without jeopardizing investment, and said there is no intent to rush the bill through the committee. Further, proposals for other sources of income to the state "seem to be off the table" which leaves the legislature only with the options of oil taxes and fuel taxes.

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REPRESENTATIVE RAUSCHER questioned how the bill would cure instability because the industry is currently operating according to previous legislation.

CO-CHAIR TARR said the committee will hear testimony on the bill from industry at an upcoming hearing. She related the industry urges the state to diversify its revenue sources to those other than oil and gas; however, there are few other options. She pointed out the bill looks at a range of minimum taxes from 4 percent to 7 percent, [and seeks] to avoid threatening investment and jobs. Co-Chair Tarr returned attention to slide 7 and said a 10 percent rate is not too low at \$30 per barrel prices; however, the crossover point is between \$60-\$80 per barrel, which may be the short-term stable price for oil. The working group will address the underlying structure of oil tax policy and long-term oil prices.

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REPRESENTATIVE BIRCH asked whether the sponsors would have introduced HB 288 if a broad-based income tax was passed during [2017].

CO-CHAIR TARR, speaking for herself, said she preferred a fair fiscal package; the passage of a tax would have [decreased] the state's deficit outlook and, therefore, "the math would be different."

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REPRESENTATIVE BIRCH advised there have been great increases to oil production on the North Slope due to the present tax environment. He asked how the proposed legislation would

contribute to three years of increased production and cautioned the bill is "going the wrong direction."

CO-CHAIR TARR said from her perspective diversifying [state revenue] would change the present situation but the legislature must come to agreement. She returned to slide 2 and the four pillars of a plan to [address the budget deficit], noting her constituents seek to "spread the burden more evenly." She restated her interest in comments from the industry and in following the working group process. She returned attention to slide 7 and observed there are different perspectives from those who must provide state services and from those of an industry that answers to its shareholders.

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REPRESENTATIVE BIRCH recalled last year the legislature created a working group to address this issue, but the bill has been introduced without the benefit of the working group. He stressed the House Resources Standing Committee is a resource committee that has a duty and responsibility to focus on increasing production and recognizing the importance of revenue earned by royalty oil. He directed attention to the sponsor statement and expressed his belief that the bill appears to be a bargaining chip in the issue of broad-based taxation. Representative Birch said he does not support the bill; the committee has a duty and obligation to increase production since increased production is beneficial to all. He urged to return to the process established through the working group.

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CO-CHAIR TARR acknowledged the legislation is not the only option and she has no wish to repeat an extended oil tax legislative session, thus the bill is limited in scope. In further response to Representative Birch as to whether the administration has embraced the bill, she said the administration will testify during an upcoming hearing on [1/26/18].

REPRESENTATIVE JOHNSON agreed the bill is a bargaining chip and noted after House Bill 111 [passed in the Thirtieth Alaska State Legislature], her desire was to address the issue of paying off the tax credits, which is not being discussed. She strongly opined introducing an oil tax bill to the committee at this time is the opposite of stability and is again sending the wrong message. She asked the following questions: How would the bill

bring stability to the industry; how is the bill not creating "an oil tax session," how is the bill advancing ...? Lastly, she disagreed that consultants supported the intent of the bill, and asked which consultants are in support.

CO-CHAIR TARR, in response to the question of stability, said without a diversified revenue stream the pressure for raising revenue will always be on the oil and gas industry. She pointed out there is instability created by a citizens' initiatives regarding resource development policy, the use by the legislature of the [Alaska Permanent Fund], and other issues. She acknowledged consultants have not made recommendations about specifics in oil policy, but they do urge for the state to make fundamental changes such as taxing based on PTV. She stressed legislation last year was not a fundamental rewrite of oil tax policy.

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CO-CHAIR JOSEPHSON noted his support for paying down the tax credits which will cost about \$900 million; there is bipartisan support to do so if a plan emerges. He agreed that a consultant advised making a change to the state's tax structure. Regarding ["whiplash," caused by] the introduction of a new bill that would increase the gross tax, he recalled the governor recommended this legislation in January of 2016, and since then the committee as seen this issue as a consistent theme.

REPRESENTATIVE PARISH questioned whether it is typical for an oil company to utilize profits earned in Alaska for use by its global business.

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CO-CHAIR TARR said data from the Department of Revenue is limited and she cannot comment.

REPRESENTATIVE PARISH asked whether the 10 percent tax received from severance taxes [shown on slide 7] is typical when compared to other nations.

CO-CHAIR TARR said the percentage varies widely thus it is hard to find a fair comparison. She restated her belief if Senate Bill 21 [passed in the Twenty-Eighth Alaska State Legislature] was written now, the [minimum] percentage would have been in the 13 percent to 18 percent range, but perhaps still linked to price. However, at that time, the "new normal" was not

considered; discussion related to the percentage of minimum tax has been ongoing for over ten years.

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REPRESENTATIVE PARISH read from the Alaska State Constitution as follows:

Article VIII - Natural Resources

General Authority

The legislature shall provide for the utilization, development, and conservation of all natural resources belonging to the state, including land and waters, for the maximum benefit of its people.

REPRESENTATIVE PARISH asked Co-Chair Tarr whether she believes the state is securing maximum benefit for the people of Alaska.

CO-CHAIR TARR stated she is but one member of the collective body of the legislature who seeks to debate the issue of the minimum 10 percent tax in the present price environment. She returned attention to slide 7 which illustrated several proposed minimum tax percentages and expressed her personal hope that the [state budget] can maintain a strong [Alaska Permanent Fund] dividend and public safety.

CO-CHAIR JOSEPHSON, in further response to Representative Parish, pointed out there are differing opinions as to how maximum benefit can be achieved, such as increases to [Alaskans'] salaries and to [oil and gas] production in Alaska.

REPRESENTATIVE PARISH opined the work of the committee is not finished in regard to oil taxes and brought up points suggested by various legislative consultants.

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REPRESENTATIVE RAUSCHER inquired as to the aforementioned company that [transferred its Alaska profits to global projects.]

REPRESENTATIVE PARISH offered to provide written information on BP.

REPRESENTATIVE TALERICO recalled data from "those old [oil tax] plans" resulted in an alarming 6-8 percent decrease in annual production that inspired much of the ongoing work on various tax plans. His concern is the current surges in production and price should have taught a lesson that Alaska is subject to pricing decisions made by the Organization of the Petroleum Exporting Countries (OPEC). He said one of his biggest concerns is how the bill would impact throughput, volumes, exploration, and investment. He cautioned that although the bill is limited to one subject, the bill may acquire creative amendments related to, for example, changes to gross value reduction (GVR) or to gross value at the point of production. Representative Talerico said, "I do also appreciate though, the fact that you put ... several different scenarios to look at because I think, I think we should do that as we work forward"

CO-CHAIR TARR restated lessons learned from Senate Bill 21 and from the original intent of the tax credits, which were intended to encourage smaller independent and new companies in the industry in Alaska. She questioned whether the intent to diversify the North Slope was undermined. These are issues that can be thoroughly evaluated by the working group process and restated her concerns as above.

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CO-CHAIR JOSEPHSON asked whether the sponsor would have offered the legislation had [oil] prices remained in the \$45 [per barrel] range.

CO-CHAIR TARR returned attention to slide 7. At the \$60 price range there is an approximate split of \$18 of profit to the oil company and \$2 to the state, and she asked whether that is a fair split of profit. In response to Representative Parish's question as to when the committee would hear invited testimony on the bill, she said state and industry representatives are scheduled to provide testimony on [1/26/18].

REPRESENTATIVE JOHNSON asked whether the legislation would be presented to the working group.

CO-CHAIR TARR said no. She clarified the working group will not review proposed legislation, but will evaluate tax policy and other state actions such as infrastructure investment. For example, a permanent road system built by the state to replace ice roads in oil development areas would be an opportunity for the state. Representative Tarr pointed out portions the tax

credit program paid large sums of money for some projects that did not lead to increased production, or new development, and suggested a better use of state money may be infrastructure development. Further, she stated her understanding a bill could not be referred to the working group for a hearing to due to public notice procedures.

REPRESENTATIVE JOHNSON urged for bill in general to be discussed in the working group as is appropriate.

[HB 288 was held over.]

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ADJOURNMENT

There being no further business before the committee, the House Resources Standing Committee meeting was adjourned at 2:15 p.m.