

**SB**

**31**

<target><bill>SB 31</bill><subject>SB  
31</subject><comm>SENE26</comm></target>

26-LS0217C  
Kane  
2/11/09

**CS FOR SENATE BILL NO. 31( )**  
**IN THE LEGISLATURE OF THE STATE OF ALASKA**  
**TWENTY-SIXTH LEGISLATURE - FIRST SESSION**

**BY**

**Offered:**

**Referred:**

**Sponsor(s): SENATORS MCGUIRE, Ellis**

**A BILL**

**FOR AN ACT ENTITLED**

1 "An Act relating to an alternative energy production tax credit that may be claimed or  
2 applied against tax due under the Alaska Net Income Tax Act; and providing for an  
3 effective date."

4 **BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:**

5 \* Section 1. AS 43.98 is amended by adding a new section to read:

6 **Sec. 43.98.040. Alternative energy production tax credit.** (a) An energy  
7 producer that produces alternative energy may claim an alternative energy production  
8 tax credit if

9 (1) the alternative energy produced supplies all or part of the energy  
10 required by commercial units owned or used by the energy producer; or

11 (2) the energy producer sells all or part of the energy produced as a  
12 commercial enterprise.

13 (b) An energy producer may claim a tax credit under this section in the  
14 amount of 35/100 cent for each kilowatt-hour of alternative energy produced or sold.

1 A tax credit may be claimed for each of the first four years after the date the system  
2 used to produce alternative energy is placed into service.

3 (c) An unused tax credit under this section may be carried forward and applied  
4 against the tax liability of the energy producer for four years after the date the system  
5 used to produce alternative energy was placed into service.

6 (d) A tax credit provided under (a) of this section may be sold, assigned,  
7 exchanged, conveyed, or otherwise transferred, in whole or in part.

8 (e) A taxpayer acquiring a transferable tax credit may use the tax credit or a  
9 portion of the tax credit to offset taxes imposed under AS 43.20 (Alaska Net Income  
10 Tax Act). Any portion of the credit not used may be used at a later time or transferred  
11 under (d) of this section.

12 (f) The department shall

13 (1) prepare an application form for a tax credit under this section; and

14 (2) adopt regulations necessary for the administration of this section.

15 (g) In this section,

16 (1) "alternative energy" includes geothermal, solar, hydroelectric,  
17 wind, biomass, hydrokinetic or tidal, and wave energy;

18 (2) "energy producer" means an electric utility holding a certificate of  
19 public convenience and necessity under AS 42.05 or an independent power producer.

20 \* Sec. 2. This Act takes effect January 1, 2010.

# FISCAL NOTE

**STATE OF ALASKA**  
**2009 LEGISLATIVE SESSION**

Fiscal Note Number: 1  
 Bill Version: CSSB 31(ENE)  
 (S) Publish Date: 3/2/09

Identifier (File Name): CSSB31(ENE)-DOR-TAX-03-02-09 Dept. Affected: Revenue 04  
 Title: Alternative Energy Production Tax Credit RDU: Taxation and Treasury  
 Component: Taxation and Treasury  
 Sponsor: Senators McGuire, Ellis, Thomas  
 Requester: (S) Energy Component No.: 2476

**Expenditures/Revenues** (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

	Appropriation Required		Information				
	FY 2010	FY 2010	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015
<b>OPERATING EXPENDITURES</b>							
Personal Services	108.9	0.0	108.9	108.9	108.9	108.9	108.9
Travel	2.0	0.0	2.0	2.0	2.0	2.0	2.0
Contractual	34.9	0.0	4.9	4.9	4.9	4.9	4.9
Supplies	0.5	0.0	0.5	0.5	0.5	0.5	0.5
Equipment							
Land & Structures							
Grants & Claims							
Miscellaneous							
<b>TOTAL OPERATING</b>	<b>146.3</b>	<b>0.0</b>	<b>116.3</b>	<b>116.3</b>	<b>116.3</b>	<b>116.3</b>	<b>116.3</b>
<b>CAPITAL EXPENDITURES</b>	<b>0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>
<b>CHANGE IN REVENUES ( )</b>	<b>*</b>	<b>0.0</b>	<b>*</b>	<b>*</b>	<b>*</b>	<b>*</b>	<b>*</b>

**FUND SOURCE** (Thousands of Dollars)

1002 Federal Receipts							
1003 GF Match							
1004 GF	146.3	0.0	116.3	116.3	116.3	116.3	116.3
1005 GF/Program Receipts							
1037 GF/Mental Health							
Other Interagency Receipts							
<b>TOTAL</b>	<b>146.3</b>	<b>0.0</b>	<b>116.3</b>	<b>116.3</b>	<b>116.3</b>	<b>116.3</b>	<b>116.3</b>

Estimate of any current year (FY2009) cost: 0

**POSITIONS**

Full-time	1.00	0	1.00	1.00	1.00	1.00	1.00
Part-time							
Temporary							

**ANALYSIS:** (Attach a separate page if necessary)

See Attached.

Prepared by: Dan Stickel, Economist Phone (907) 465-3279  
 Division: Tax Division Date/Time: \_\_\_\_\_  
 Approved by: \_\_\_\_\_ Date: \_\_\_\_\_  
 Agency: \_\_\_\_\_

FISCAL NOTE # 1

STATE OF ALASKA  
2009 LEGISLATIVE SESSION

BILL NO. CSSB 31(ENE)

**ANALYSIS CONTINUATION**

**Bill Language:**

This bill will create a tax credit for electricity production from new alternative energy projects in the state. The amount of the credit will be 2.1 cents for each kilowatt hour of alternative energy produced or sold in "each of the first four years after the date the system used to produce alternative energy is placed into service," up to a limit of 20 percent of capital costs. The tax credit would be applicable only to the Alaska Corporate Net Income Tax. Unused tax credits could be carried forward or transferred.

For purposes of this bill, "alternative energy" means geothermal, solar, hydroelectric, wind, biomass, hydrokinetic or tidal, and wave energy. The credit could be claimed by an "electric utility holding a certificate of public convenience and necessity under AS 42.05 or an independent power producer." The term "independent power producer" would need to be defined in regulation and could potentially include any entity that chooses to implement an eligible alternative energy project.

The effective date of the bill is January 1, 2010. There bill includes a sunset date of January 1, 2025.

**Revenues:**

Revenues from this bill are indeterminate because we do not know the size or number of projects that would qualify for the credit. According to the US Department of Energy, Alaska currently produces 1.3 billion kilowatt hours of alternative energy annually (hydroelectric, biomass, solar and wind power; there is currently no commercial geothermal electric generation). For each 10 percent increase in alternative energy production, tax revenue to the state would be reduced by \$2.7 million per year for four years.

Some examples of credits generated by possible projects include the following ( These examples are for illustrative purposes only. They are based on publicly available information and typical capacity utilization rates):

- A 14-megawatt hydroelectric project such as the Lake Dorothy project near Juneau could be eligible for a \$1.5 million annual credit (assuming the project operates at 60% of capacity). Over four years, this credit would amount to about 9.7% of the estimated \$64 million capital cost.

- A 30-megawatt wind farm such as the Fire Island project near Anchorage could be eligible for a \$1.7 million annual credit (assuming the project operates at 30% of capacity). Over four years, this credit would amount to about 12.3% of the estimated \$54 million capital cost.

- A 1.2-megawatt wind farm such as the Nome wind farm could be eligible for a \$66,000 annual credit (assuming the project operates at 30% of capacity). Over four years, this credit would amount to about 4.8% of the estimated \$5.5 million capital cost.

Many smaller projects would likely also qualify for the credit. Based on our analysis of the sample projects listed above, we believe that for most projects, the total credit over four years would amount to less than 20 percent of capital expenditures.

We anticipate that this credit will mostly be used by corporations that acquire the credit through the transferability provision. The transferability provision will be used because many power producers are owned by municipalities, non-profits or S-corporations and therefore are not subject to the corporate income tax. Also, independent power producers, once defined in regulation, could potentially include individuals, sole proprietorships, LLC's, S-corporations, non-profits and other entities that are not subject to the corporate income tax.

**Expenditures:**

This bill would require the Department of Revenue to administer a new tax credit program, including the review and approval of credit applications and issuance and tracking of credit certificates. This new credit program will likely involve a large number of projects and millions of dollars in credits claimed annually.

The Department is requesting a Corporate Income Tax Auditor III position (Range 22) to audit the tax credits and manage the approval, issuance and tracking of the credits. There will also be \$30,000 in one-time startup expenses: \$20,000 for enhancements to our tax examination system, and \$10,000 for an education and public outreach program.

# ALASKA STATE LEGISLATURE

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Co-Chair  
Senate Resources Committee

Chair  
Senate Special Committee on Energy  
Senate Special Committee on World Trade,  
Technology & Innovation

Member  
Senate Judiciary Committee  
Joint Armed Services Committee

## SENATOR LESIL MCGUIRE

### SPONSOR STATEMENT

#### SB 31: Alternative Energy Production Tax Credit

SB 31 encourages the development of Alaska's vast alternative energy resources by offering power producers and utilities a valuable production tax credit for each kilowatt-hour of electricity they produce from geothermal, wind, hydro, tidal, wave, biomass, in-river, or solar energy.

In its simplest terms, a tax credit is a direct reduction in the amount of taxes owed. The production tax credit created by SB 31 rewards power producers in the state of Alaska for producing electricity from alternative energy sources by offering to directly reduce the amount of state corporate income tax they owe. In Alaska, the corporate income tax rate is graduated from 1% to 9.4% in increments of \$10,000 of taxable income. The 9.4% maximum rate applies to taxable income of \$90,000 and over.

SB 31 offers a production tax credit in the amount of 0.35 cents per kilowatt-hour (kWh). What this means is that the state will directly reduce the amount of corporate tax owed by 0.35 cents for each kWh of energy produced. The tax credit is calculated based on one year of production and there are 8,760 kilowatt-hours in a year. A power plant that produces 100 kW of energy would be able to reduce their corporate tax by \$3,066 per year (100 kW x \$0.0035 x 8,760 kWh/year = \$3,066/year). A 100 megawatt (1MW = 1000 kW) power plant, similar in size to the proposed Mt. Spur geothermal power plant, would be able to reduce their corporate tax liability by over \$3 million per year. The credit can only be claimed for each of the first four years after a power plant is placed into service.

However, the dominant model for energy production in Alaska is not the privately owned power producer that pays corporate tax, but rather the publically owned cooperatives and municipal utilities that are tax exempt. To level the playing field and to ensure that all power producers in the state can benefit from the tax credit, SB 31 proposes a transferable tax credit. A transferable tax credit can be sold or traded on an open market to other corporate entities that are required to pay the state corporate income tax.

Because the production tax credit can only be claimed by a power producer that has made a significant investment in infrastructure and is already producing electricity, SB 31 allows a way to incentivize alternative energy development without requiring hefty state appropriations to unproven projects and technologies.

In energy plans across the nation, production incentives are playing an increasingly important role in encouraging the development of alternative energy resources. Twenty-five states offer some sort of alternative energy corporate tax incentives and five states and the federal government offer a production tax credit similar to the one proposed by SB 31.

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Co-Chair  
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Member  
Senate Judiciary Committee  
Joint Armed Services Committee

## Explanation of Changes

Explanation of changes from SB 31 (Version R) to CSSB 31 (Version C):

- (1) Expanded from just geothermal to include other types of alternative energy: geothermal, solar, hydro, wind, biomass, tidal, and wave.
- (2) Made the production tax credit transferable so that publically owned utilities could benefit as well.
- (3) Corrected the misdrafted 35 cents to 0.35 cents.
- (4) Added an effective date to comport with the January 1 start date of a new tax year.



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Fax: 907-561-5547  
www.alaskapower.org

February 10, 2009

Senator Lesil McGuire  
Chair, Senate Special Committee on Energy

Re: Committee Substitute of SB 31, Alternative Energy Production Tax Credits

Dear Honorable Chair McGuire:

Alaska Power Association (APA) is the statewide trade association for the electric utilities that supply power to more than a half-million Alaskans in communities from Barrow to Unalaska and down the Inside Passage.

APA strongly supports the development of alternative energy projects. State financial assistance and incentives will play a critical role in getting these projects off the drawing board. The Committee Substitute for Senate Bill 31 would help encourage the construction of alternative energy projects through the use of tax credits. It is for these reasons that Alaska Power Association supports the Committee Substitute for Senate Bill 31.

I would like to offer the following suggested changes:

APA suggests defining the time during which a renewable energy producer could claim a credit as 48 months instead of four (4) years. Under the existing bill, if a utility or independent power producer started producing power in August, it could only claim a few months worth of production for that year. By counting months instead of years, the bill would allow for a full four (4) years of production to be claimed over a five-year period. The change could be made by amending subsection (b) to read as follows:

(b) An energy producer may claim a tax credit under this section in the amount of .35 cents for each kilowatt-hour of alternative energy produced or sold. A tax credit may be claimed for each of the first ~~four years~~ **forty-eight months** after the date the system used to produce alternative energy is placed into service.

APA also suggests amending subsection (e) to clarify that it is referring to the credits described in subsection (d). The clarified language would read as follows:

(e) A taxpayer acquiring a ~~transferable~~ tax credit **under (d) of this section** may use the tax credit or a portion of the tax credit to offset taxes imposed under AS 43.20 (Alaska Net Income Tax Act). Any portion of the credit not used may be used at a later time or transferred under (d) of this section.

*APA comments on draft CS SB 31, page 1*

APA believes that this minor change to section (b) and the clarification to subsection (e) are consistent with the intent behind Committee Substitute for SB 31.

If you have any questions regarding this letter, please contact me at 907-771-5703 or [mleland@alaskapower.org](mailto:mleland@alaskapower.org). I will be traveling to an out-of-state meeting the day of the first hearing on this bill. As a result, I regret that I will not be able to testify at the hearing.

Thank you for your work on this and other issues of importance to the Alaska electric utility industry.

Sincerely,

A handwritten signature in black ink, appearing to read 'Marilyn Leland', written in a cursive style.

Marilyn Leland  
Executive Director



# Alaska Conservation Alliance

*Uniting for Alaska's Future*

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February 12, 2009

The Honorable Lesil McGuire  
Alaska State Senate  
Alaska State Capitol  
Juneau, Alaska 99801-1182

Dear Senator Lesil McGuire,

On behalf of the 40 conservation groups and the 38,000 Alaskans that are represented by the Alaska Conservation Alliance, I am pleased to acknowledge our strong support for SB 31 to establish an Alternative Energy Production Tax Credit. This credit will give Alaskan communities, utilities and entrepreneurs the incentive needed to develop clean, stably priced clean energy sources.

As you are well aware, Alaska is at an energy crossroads. Much of the state's aging electricity generation infrastructure will have to be replaced in the next decade. With power plant life spans of 20 to 100 years, decisions made today about electric power technology will affect generations of Alaskans to come. A decision now to base Alaska's energy infrastructure solely on fossil fuels will result in decades of energy price volatility. Additionally, it is commonly accepted that a carbon cap and trade system to limit the greenhouse gas emissions of fossil fuels, further increasing the costs associated with fossil fuels, will soon likely be implemented. An alternative energy production tax credit gives rural and urban communities incentive to tap a fuel-free, zero-carbon energy source that will stabilize Alaska's future energy costs.

Investing in clean energy production and research can help Alaska become an exporter of clean energy technologies to the world in addition to supplying Alaskans with clean and stably priced energy. Through incentives similar to the Geothermal Tax Credit, Germany built an \$8.7 billion renewable energy industry, creating 170,000 jobs.

The Alaska Conservation Alliance would like to thank you for this opportunity to voice our support for SB 31 and we encourage passage of this bill.

Sincerely,

Kate Troll  
Executive Director

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**February 12, 2009**

**Alaska Senate Energy Committee**

**Kip Knudson, Tesoro Alaska**



**TESORO**

February 12, 2009

# Tesoro - A Collection of Independent Refiner/Marketer Companies

## • No upstream assets

- Headquartered in San Antonio, Texas
- Seven Refineries
- 660,000 bpd total crude capacity
- Retail network of over 850 sites
- 5,500 Employees
- Traded on NYSE: symbol TSO

Kenai, Alaska  
 • 72,000 bpd  
 • Key products:  
 Jet & Gasoline

Martinez, California  
 • 166,000 bpd  
 • Key products:  
 CARB Gasoline  
 & CARB Diesel

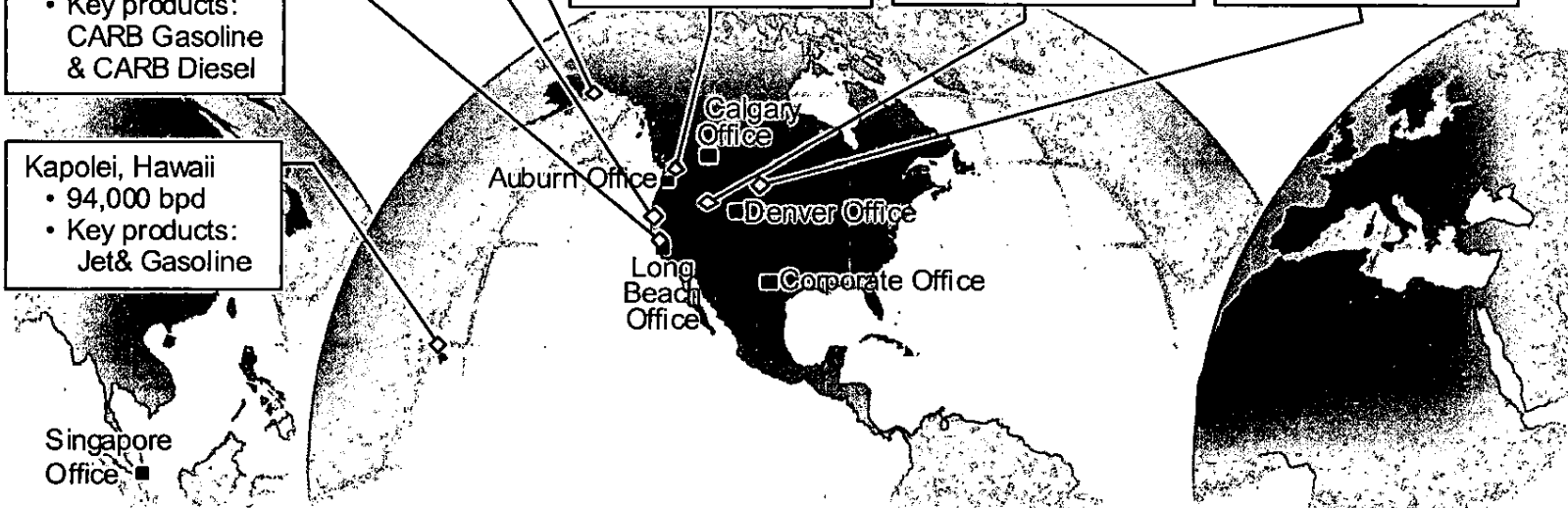
Wilmington,  
 California  
 • 100,000 bpd  
 • Key products:  
 CARB Gasoline  
 & CARB Diesel

Kapolei, Hawaii  
 • 94,000 bpd  
 • Key products:  
 Jet & Gasoline

Anacortes,  
 Washington  
 • 115,000 bpd  
 • Key products:  
 Gasoline & Diesel

Salt Lake City, Utah  
 • 58,000 bpd  
 • Key products:  
 Gasoline & Diesel

Mandan,  
 North Dakota  
 • 58,000 bpd  
 • Key products:  
 Gasoline & Diesel



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# Kenai Refinery

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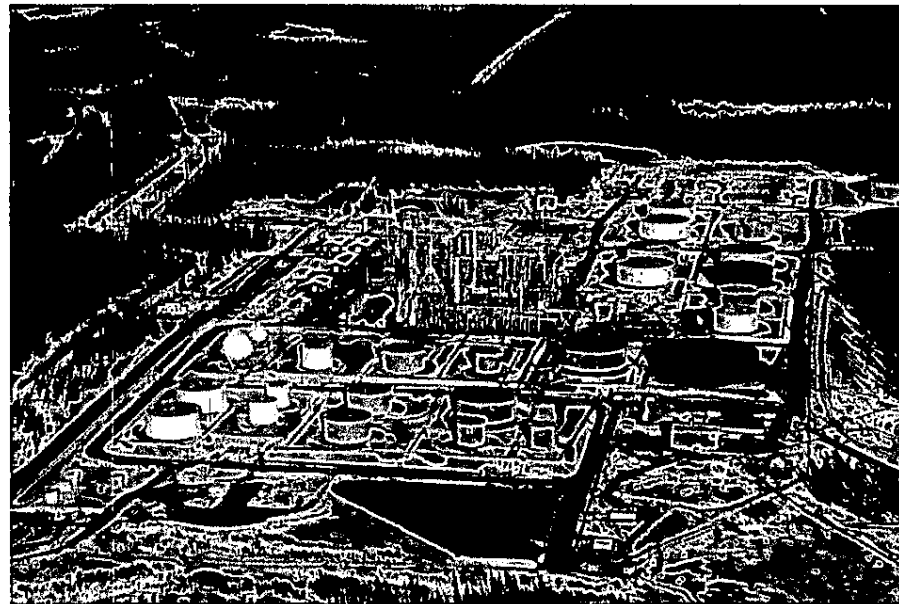
## History

- Built in 1969
- Constructed to operate on 100% ACI
- Crude capacity 17,500 b/d (17 employees)
- Cook Inlet production peaked at 225,000 bpd in 1970



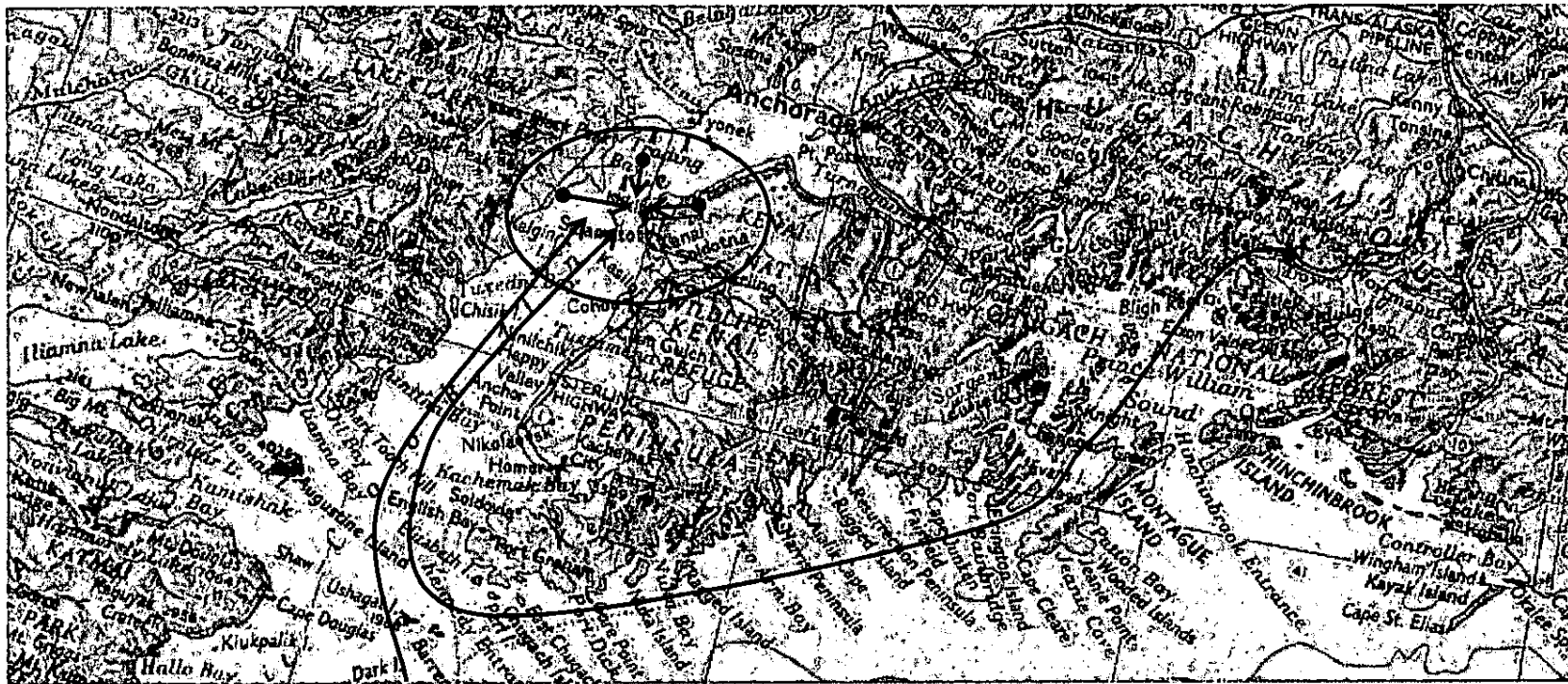
## Today

- 72,000 bpd nameplate crude capacity
- Employs over 200 people
- Award-winning safety record
- Product mix
  - Propane
  - Gasoline
  - Jet Fuel
  - Diesel Fuel
  - Heavy Vacuum Gas Oil
  - Fuel Oil / Bunker
  - Road Asphalt



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# Crude Types



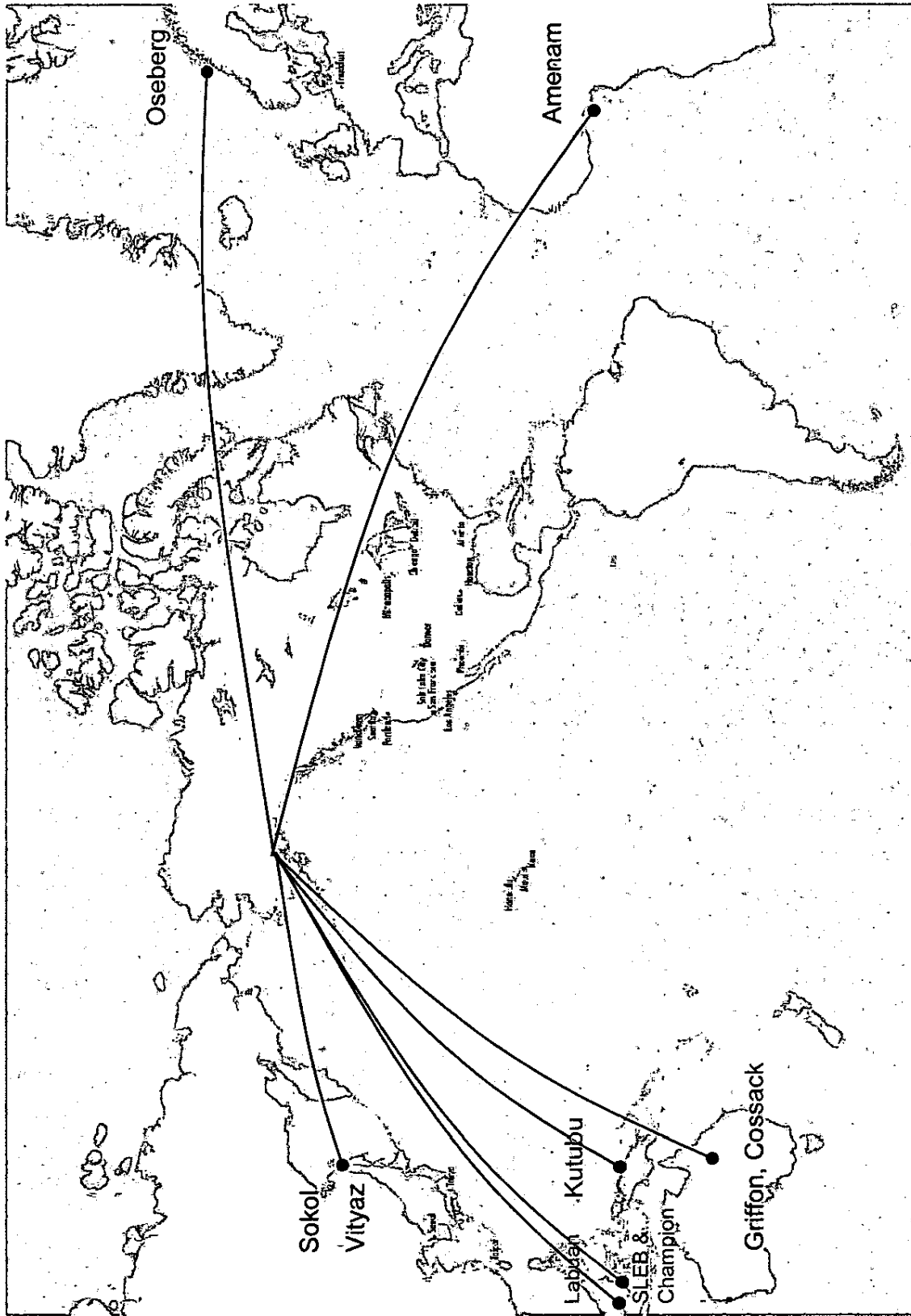
- Alaska North Slope - approximately 50%
- Cook Inlet - approximately 25%
- Light Foreign - approximately 25%

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# Foreign Crude

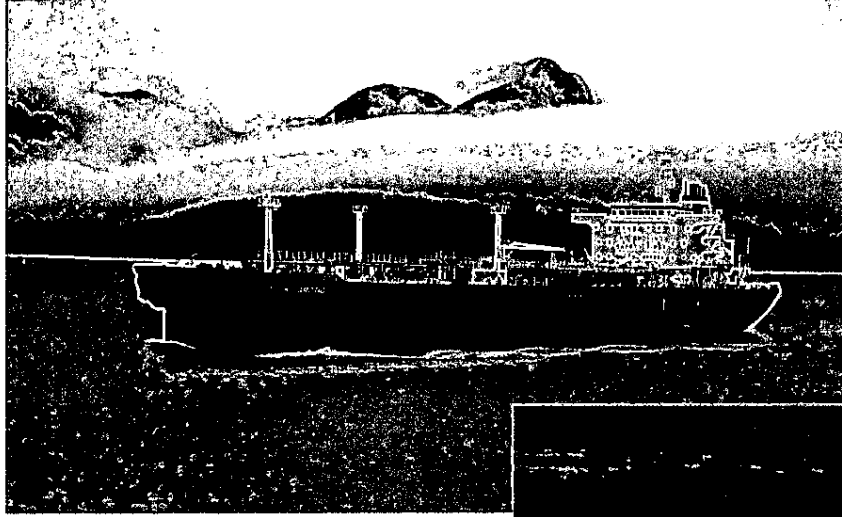


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# Marine Operations

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- Three Jones Act double-hull tankers
- Double-hull ice-class foreign tankers
- Assist tug for Cook Inlet

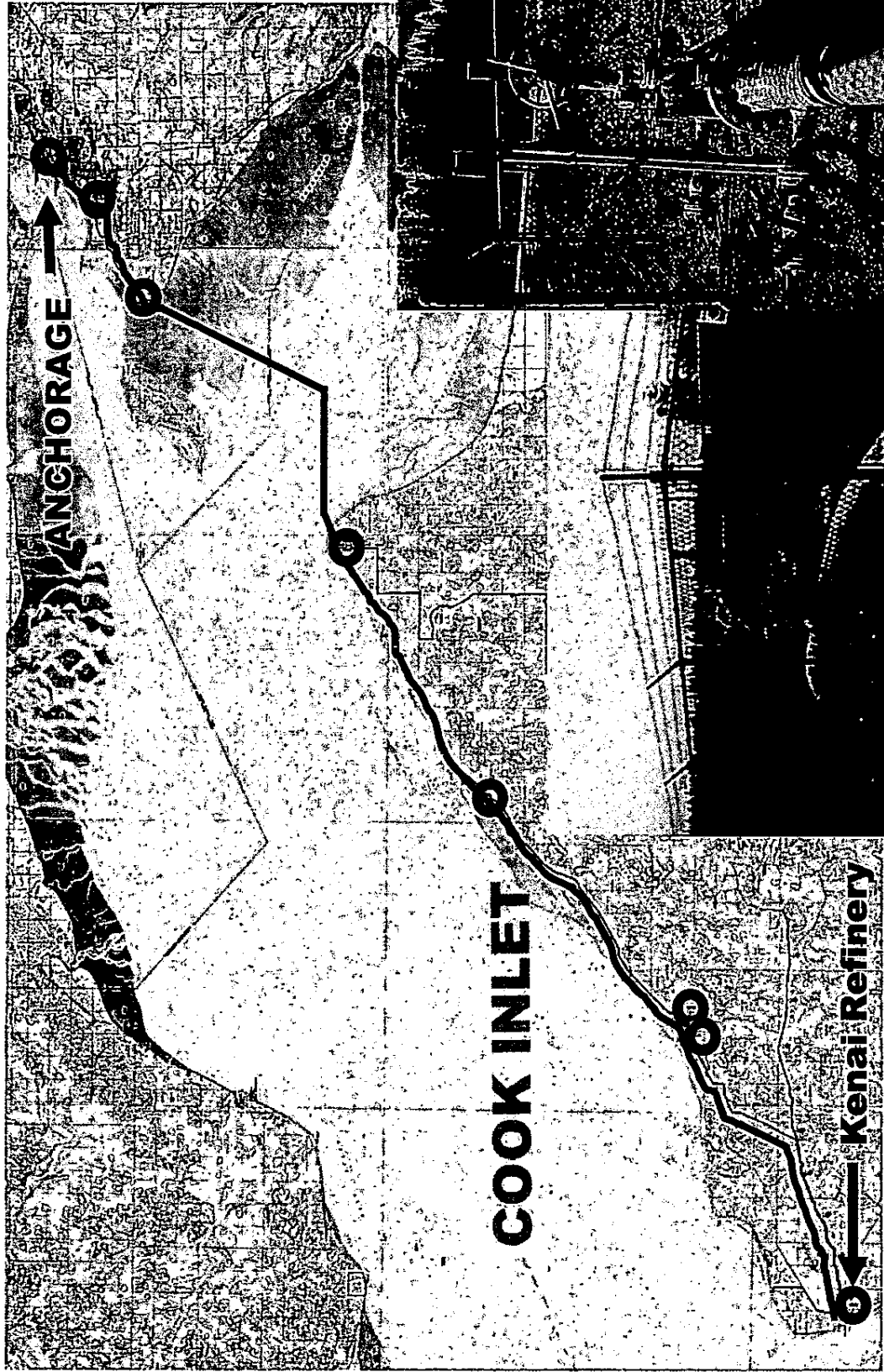


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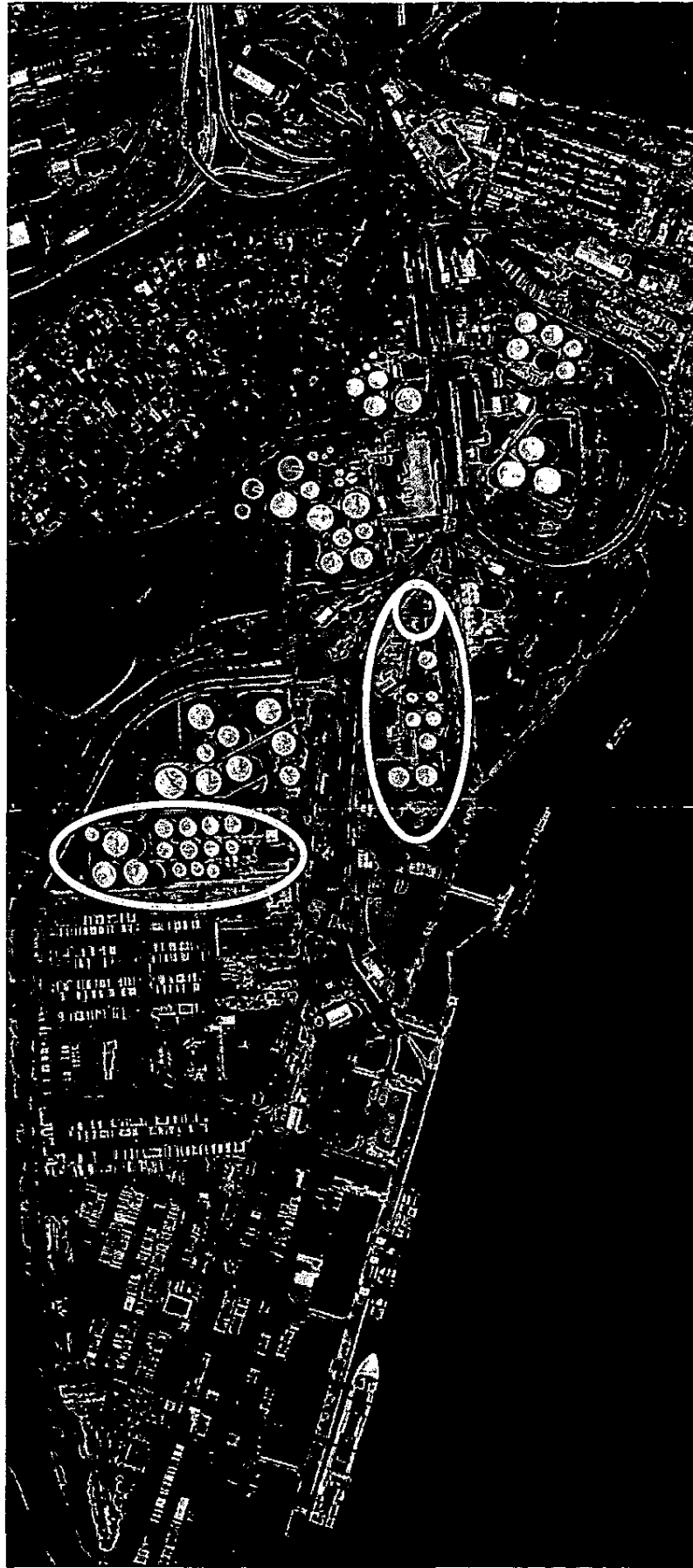
# Tesoro Alaska Pipeline



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# Tesoro's Anchorage tank farm

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# Tesoro Marketing in Alaska

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- 31 company-owned convenience stores - 29 sell fuel
- 56 wholesale branded sites as of 10-17-08



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## Commodity fundamentals

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- If the market experiences an oversupply of a commodity, prices fall
- If demand for a commodity cannot be met, prices increase
- Commodity markets, in the short term, are agnostic to the cost to produce
- In the long run, if commodity producers go out of business, the remaining producers must fill the customer demand, and prices likely will rise
- Two commodity examples that Alaskans are more familiar with:
  - Salmon
  - Oil



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# Refining/marketing has gotten very complicated over the past decades

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- Lead
- Oxygenate
- Vapor recovery
- Sulfur
- Spill response
- Pipeline integrity
- Underground storage tanks
- Flares
- Mixing zones
- PWS and CI marine navigation
- Above-ground storage
- Transportation Security Administration
- Metrology
- Biofuels in the NW
- Boutique fuels

Up next:

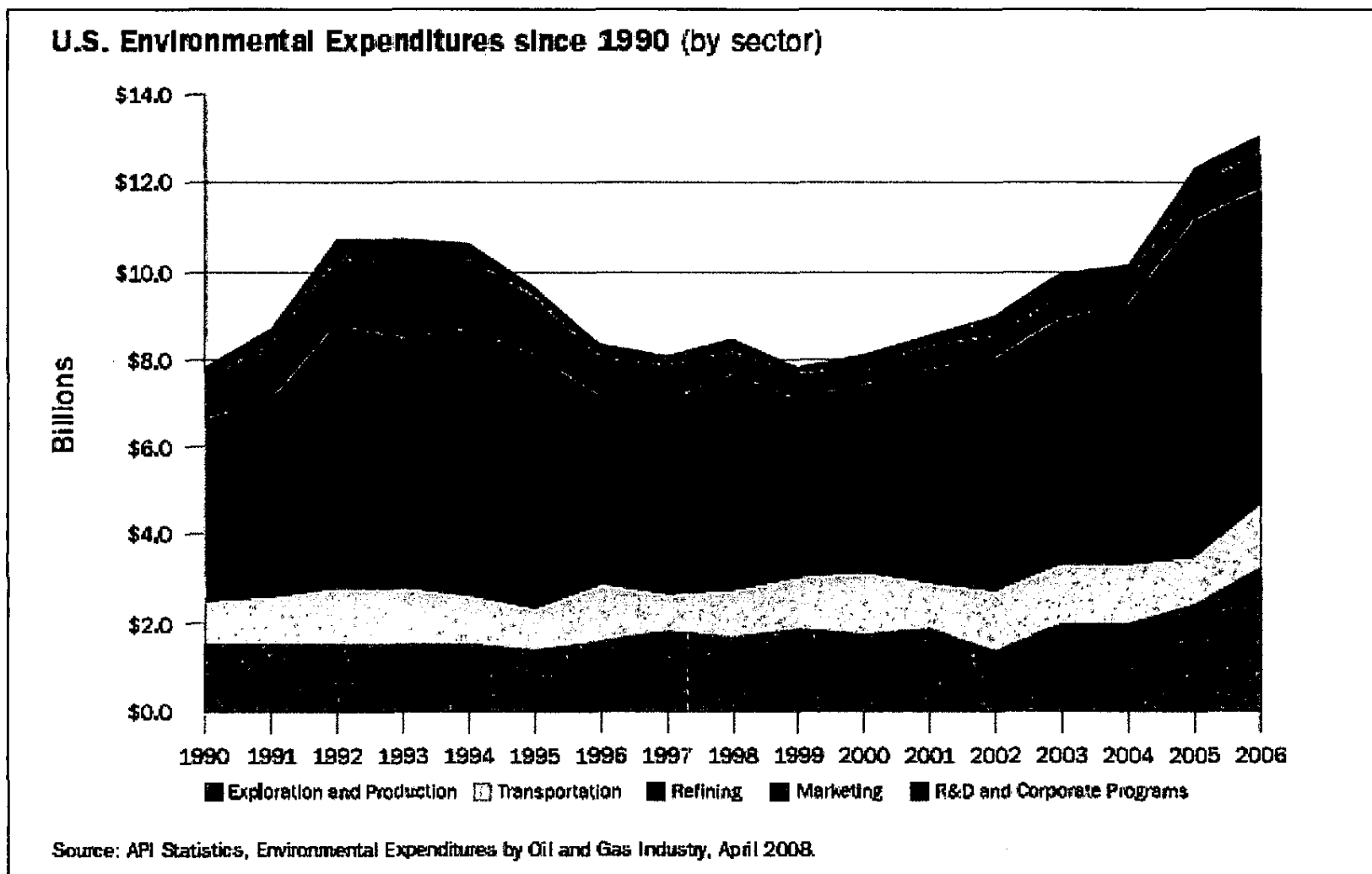
- Benzene
- Greenhouse gases
- Beluga whales



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# Refiner investment just to stay in business



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## Independent refiner

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- An independent refiner's economic model is based on being more efficient and providing a competitive alternative to an integrated major.
- An independent refiner does not profit from high prices, but makes profit/loss based on the difference between the market cost of crude and market price of products



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## Two manufacturers, but lots of marketers

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- Refiners make product (gasoline, diesel, jet, bunker, propane, etc.) on a ratable basis – let's say 50,000 barrels per day.
  - Low complexity refineries like those in Alaska have limited ability to vary the mix of production, and all refineries have minimum run rates and it is very complicated to turn refineries off, and then back on
  - Refiners, like all manufacturers, follow best-practices that encourage just-in-time inventories
  - Each refiner builds storage and distribution networks to satisfy customer needs, but does not engage in long-term storage of product
- Refiners then have to sell those 50,000 barrels of product on a ratable basis – every day, 365 days a year
- Which means that a refiner sells products in the following ways (referred to as “channels”):



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# Marketing terminology

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- Retail
  - Company operated sites that sell fuel to the public
  - Refiner/marketer invests capital; owns/leases real property
  - Refiner/marketer employs staff
- Wholesale Branded Rack Sales
  - Distributors
    - Long-term commitment
    - Brand offerings (advertising, promotion, credit cards network and settlement)
    - Refiner/marketer invests capital for image
  - Dealers
    - Individual retailers that purchase refiner branded products
    - Long-term commitment
    - Refiner brand offerings (advertising, promotion, credit cards network and settlement)
    - Refiner/marketer invests capital for image



## Marketing terminology (cont.)

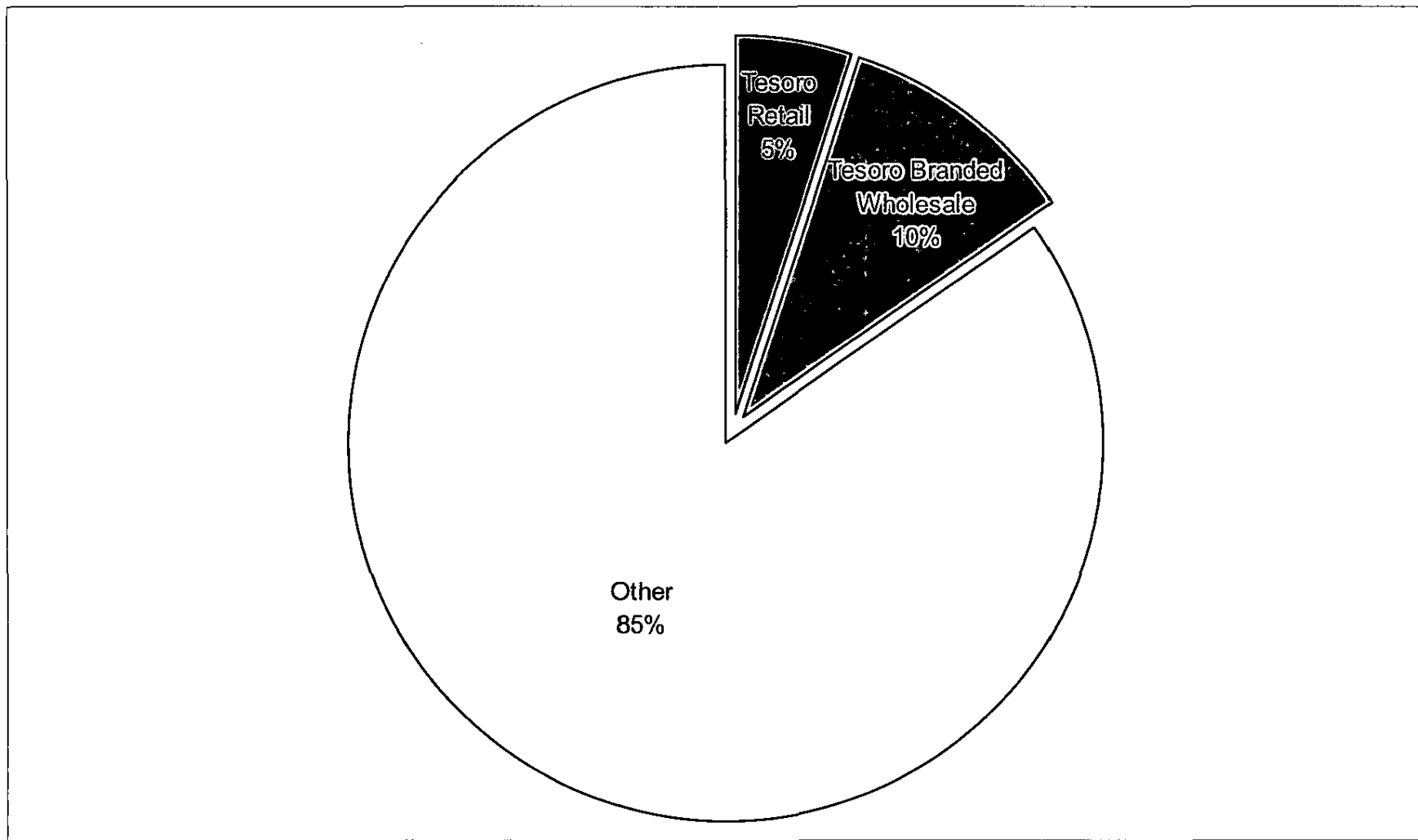
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- Wholesale Unbranded Rack Sales
  - Contract
    - Term supply commitment that establishes volume and pricing basis
    - No brand support
  - Open Rack
    - Flexible supply arrangement that does not obligate either party on volumes
    - No brand support
- Bulk Sales
  - Large volume sales to customers with significant infrastructure and financial strength
    - Waterborne sales over wharf
    - Terminal sales
  - Exchanges
    - Deliveries (receipts) with other suppliers



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# Tesoro branded outlets compared to total Alaska market



Source: 2007 National Petroleum News Station Count

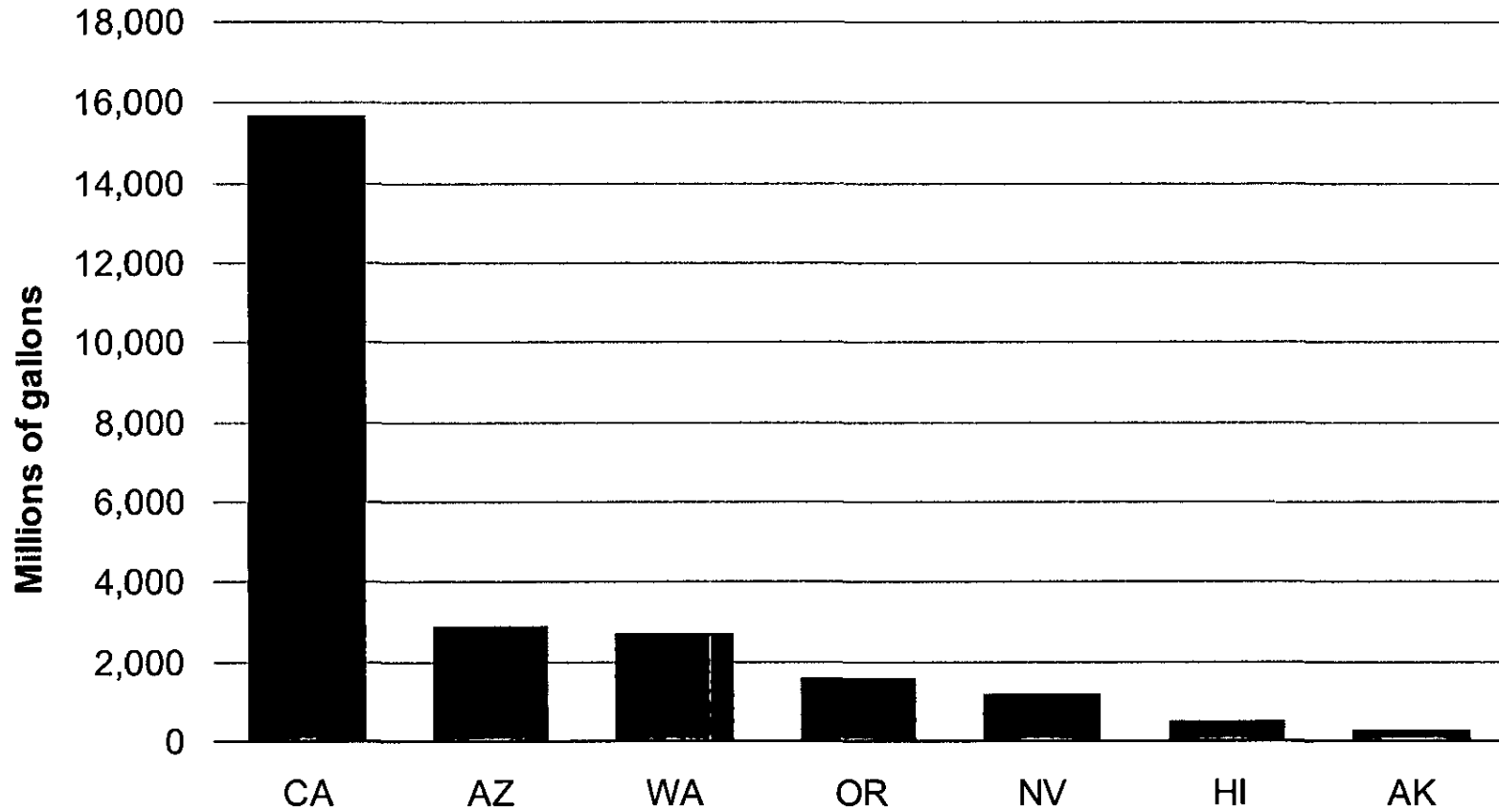


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# Demand

## 2007 Gasoline Demand



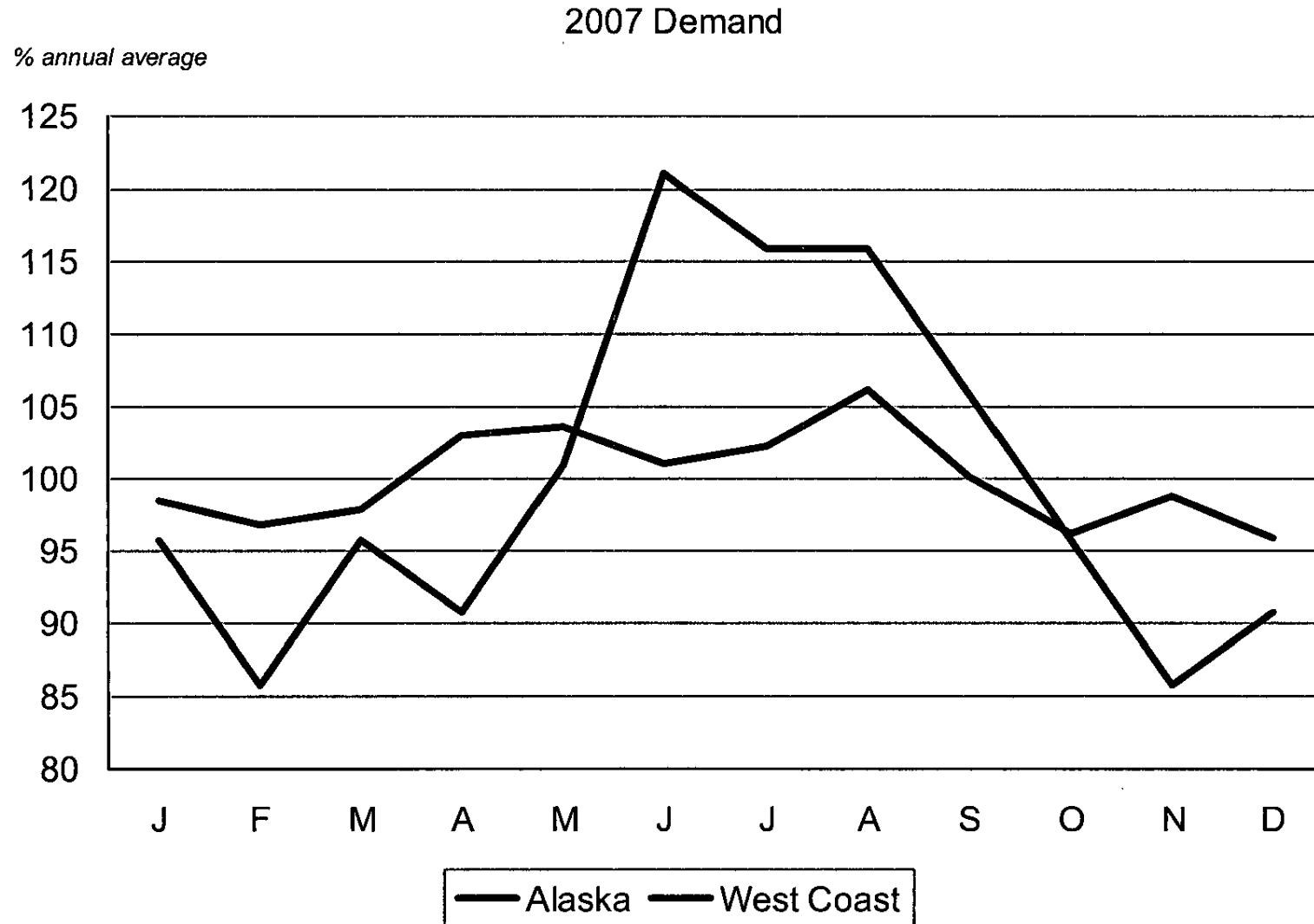
Source: Federal Highway Administration



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# Alaska market shows more seasonality



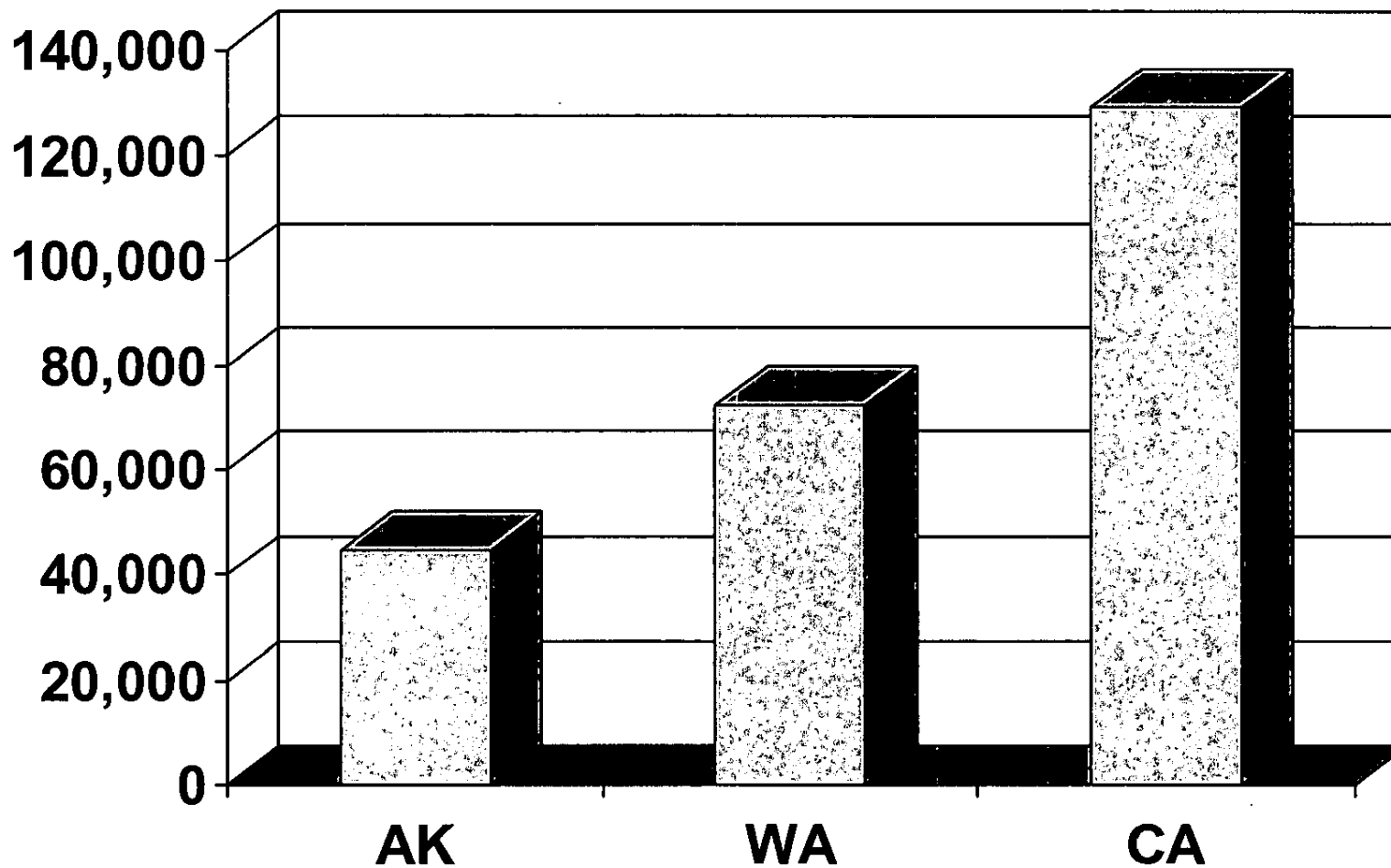
Source: Federal Highway Administration, DOE

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# Average monthly gallons sold per retail site



Sources: Energy Information Agency, National Petroleum News

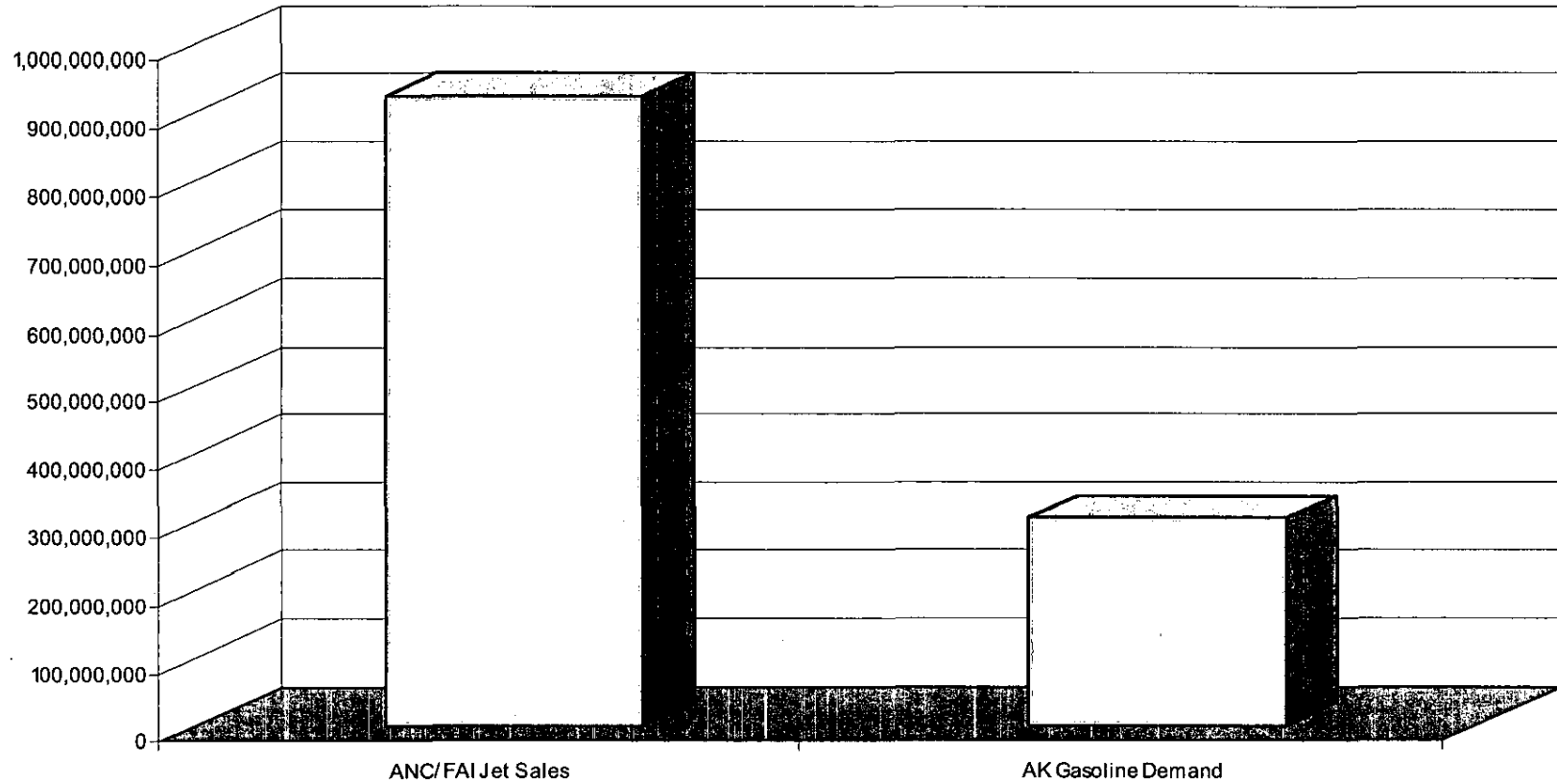
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# Jet fuel sold at ANC/FAI vs. total gasoline demand

2007 ANC/FAI Jet Sales vs. Total State Gasoline Demand

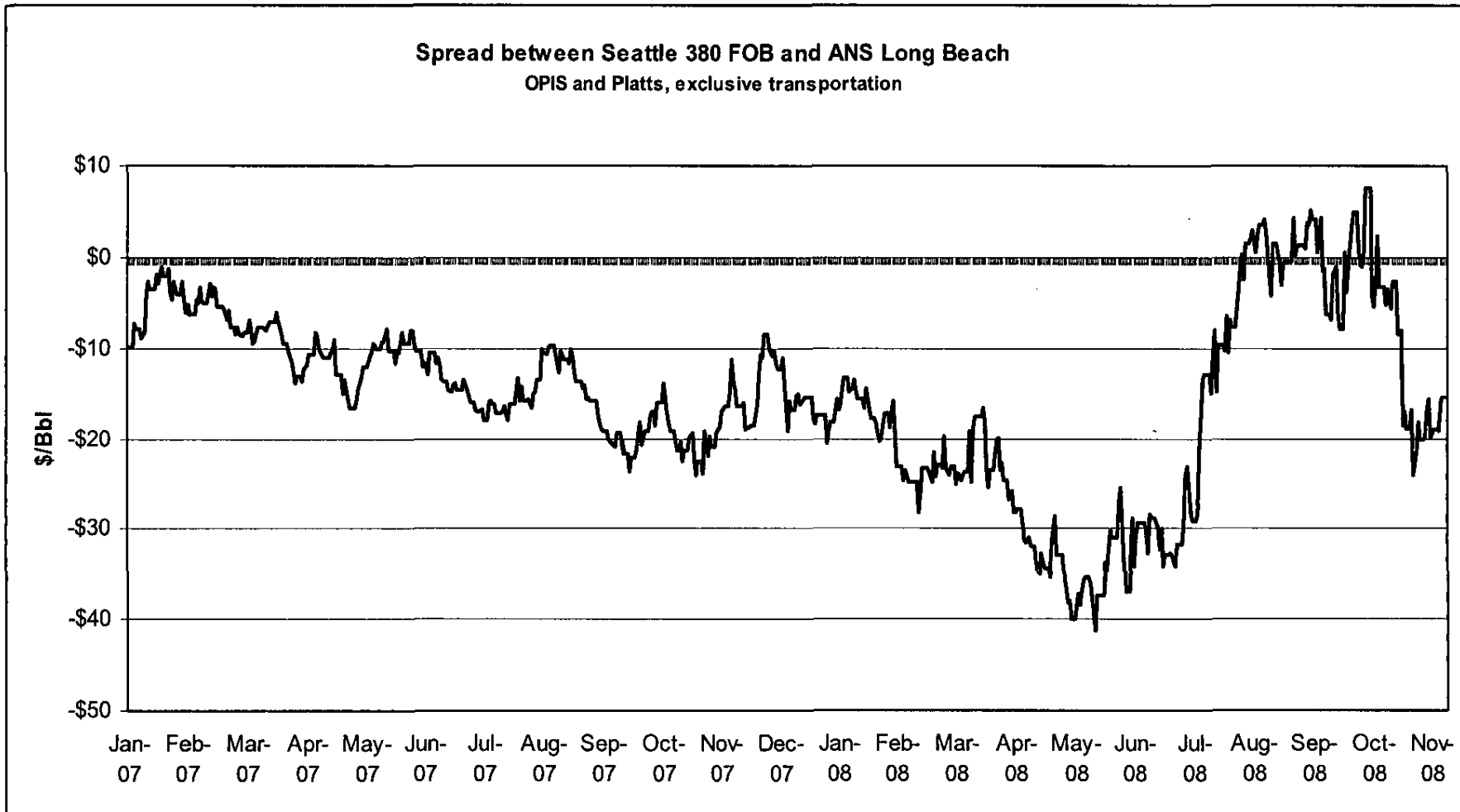


Sources: AK International Airport System and Federal Highway Administration



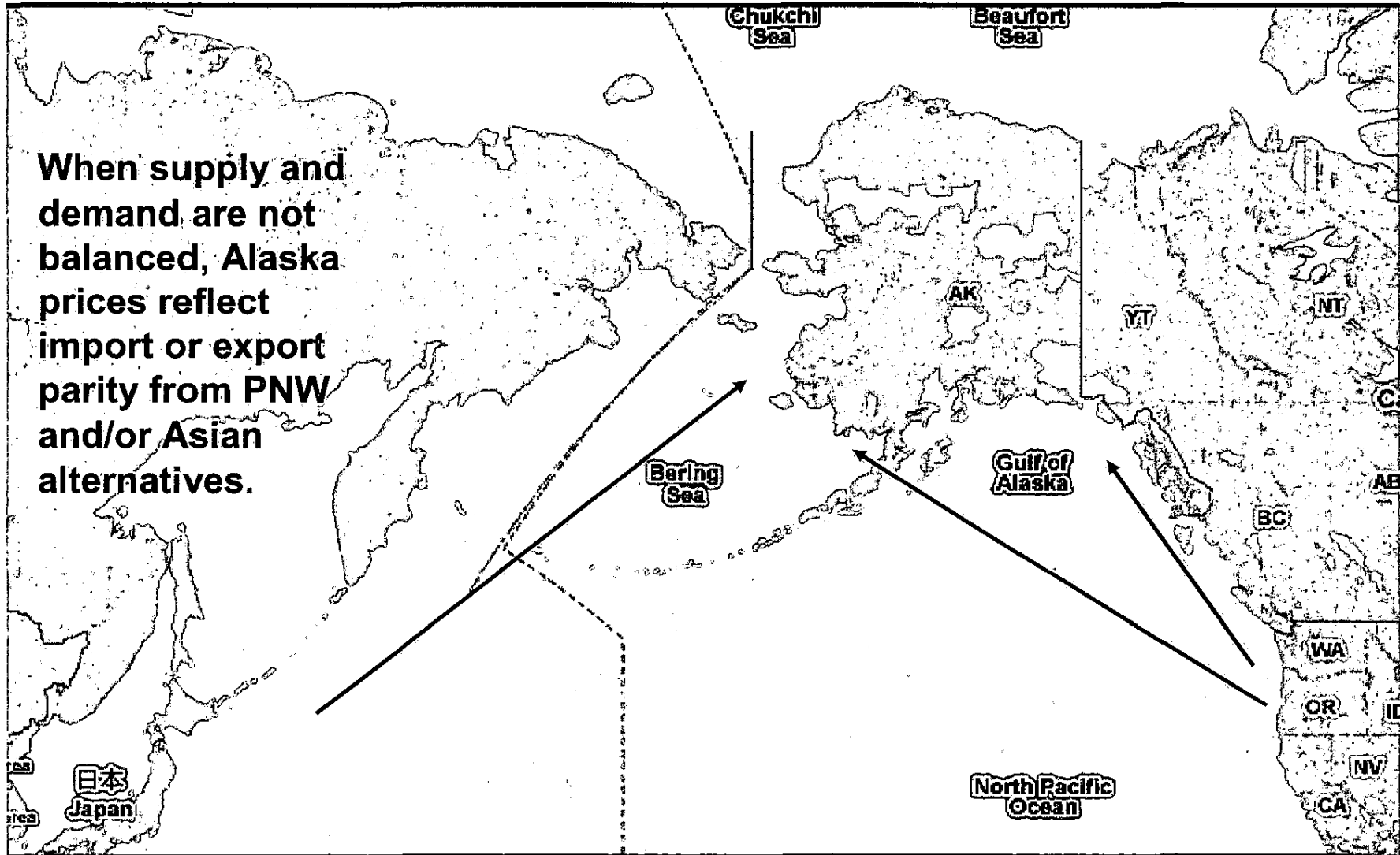
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# The market for Kenai "bottoms"



February 12, 2009

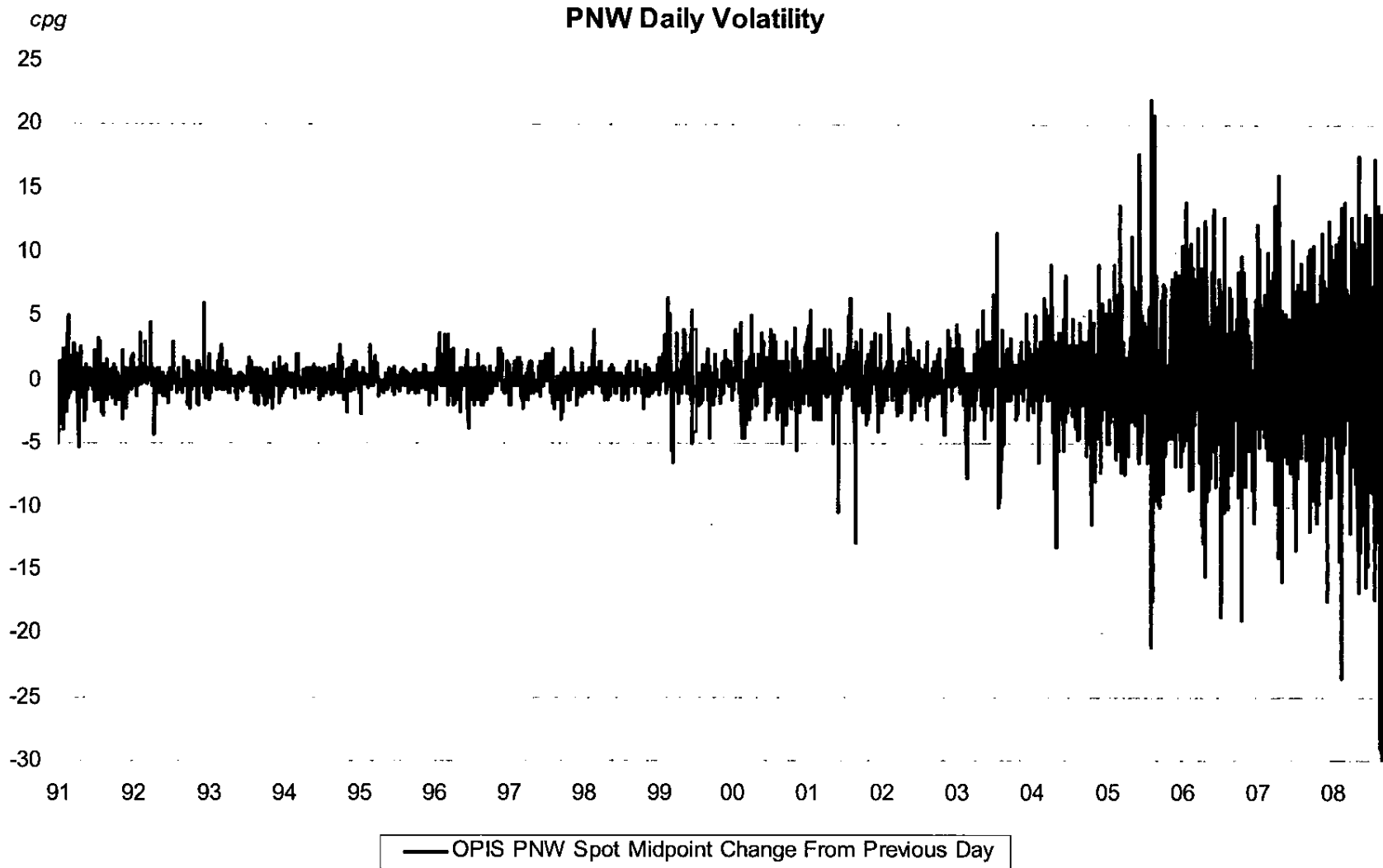
# Price is determined by last barrel into market



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# West coast market volatility

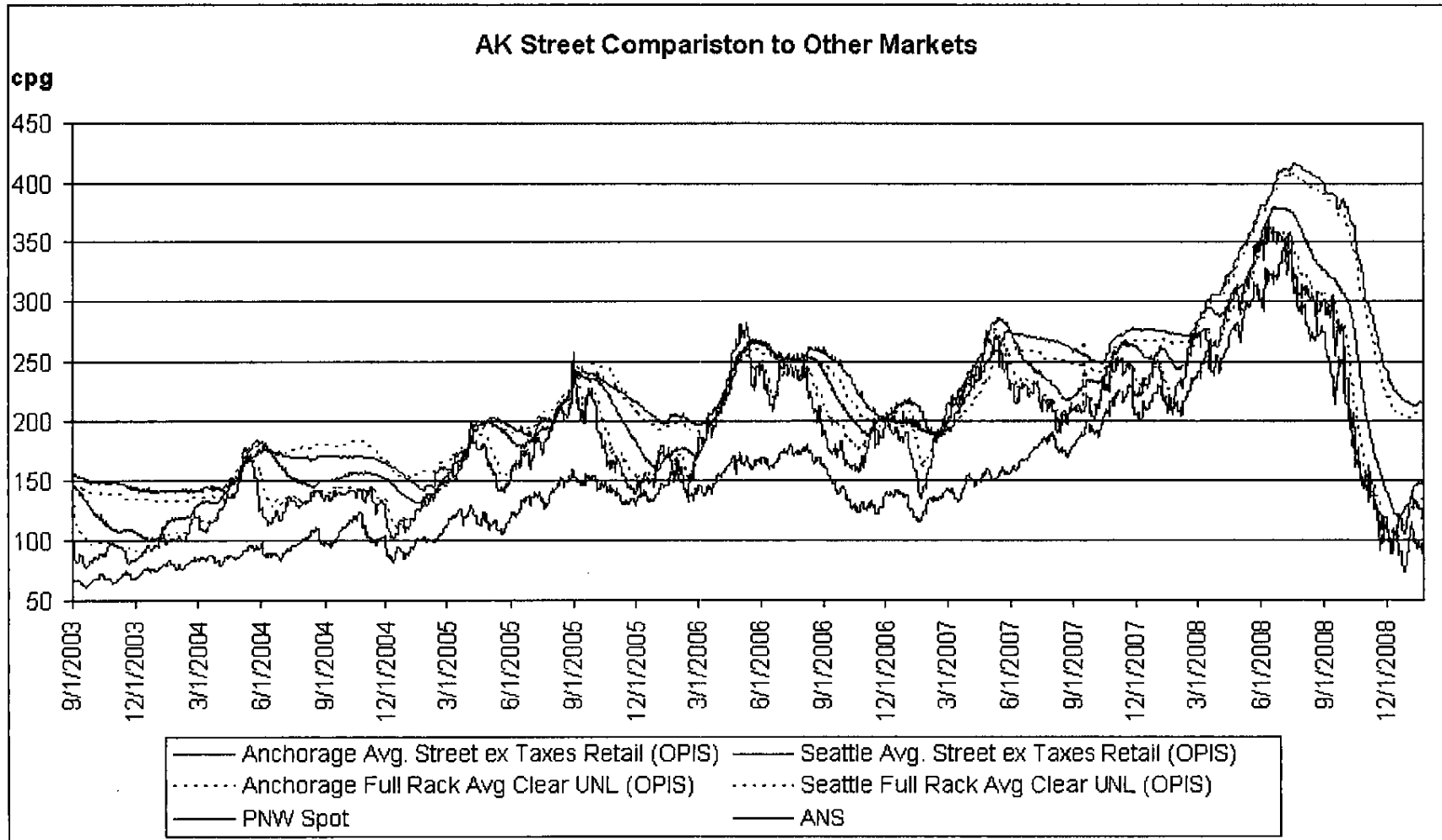


Source: OPIS

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# Daily comparison of prices (ex. tax)

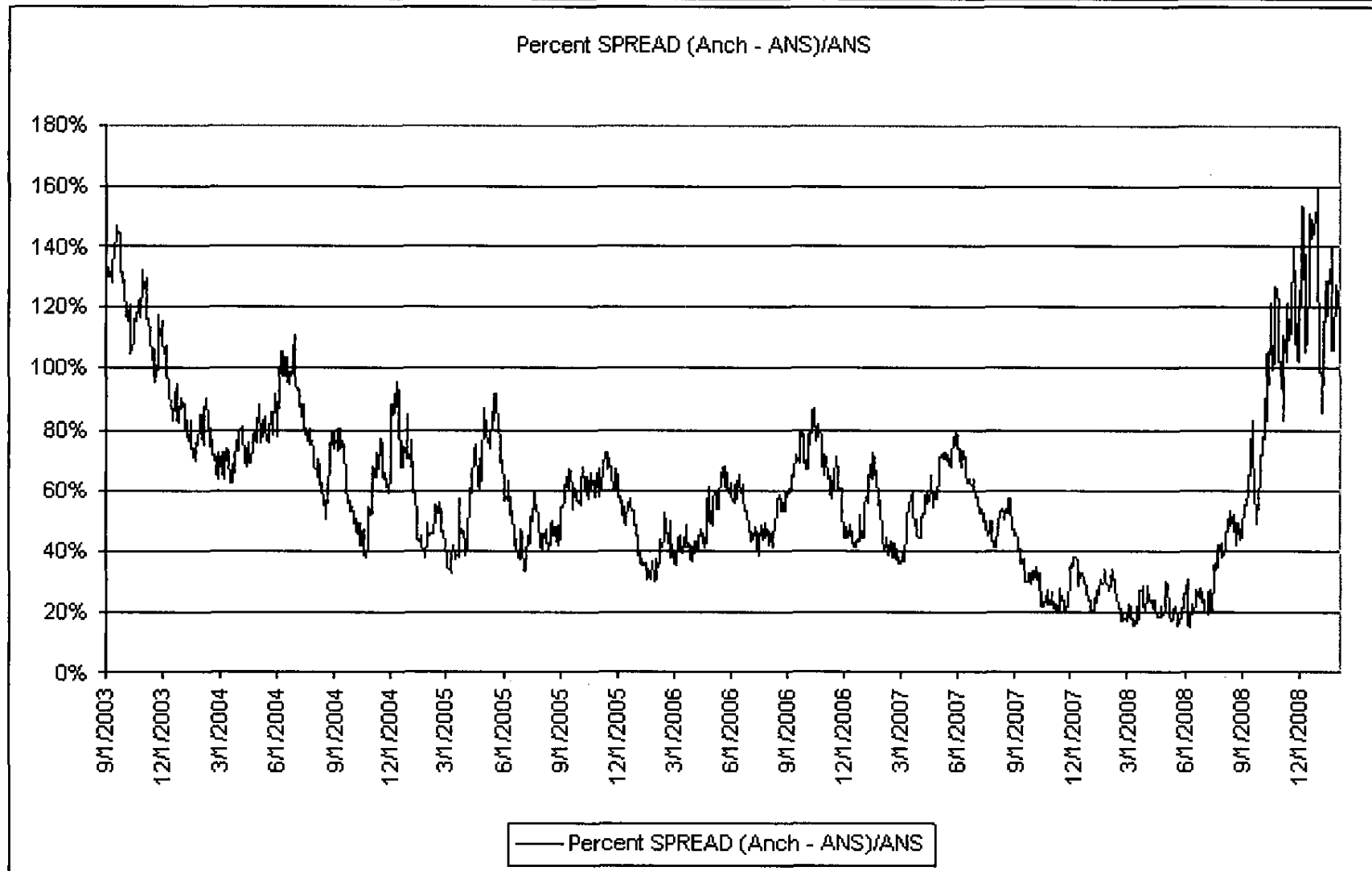


Source: OPIS and Platts



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# Daily street percentage spread Anchorage – Platts ANS (ex. tax)



Source: OPIS and Platts

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## Value-add success story

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- Over 39 years of adding value to Alaska oil
- Alaskans employed to make products that Alaskans buy
- Economists conclude that refineries result in a jobs multiplier of nine – so today the Kenai Refinery accounts for 1,800 jobs
- The existence of in-state refineries has helped underpin the growth of the international air cargo business
- The air cargo business has helped Alaska refiners to continue making gasoline and diesel
- Even though we are geographically distant from large fuel markets, reliability of supply is excellent



## Alaska market is competitive and unique

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- OR and AZ have no refineries
- AK refiners sell products through multitude of channels and also compete with import barrels
- Seasonality
- Volume
- Some manufactured products have no market in Alaska
- Government price caps will distort these market forces

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## Tesoro opposes price cap legislation

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- This is not anti-gouging legislation, it is a price cap
- Regardless of the details, price caps are bad public policy – both for consumers and for refiners
- Price cap legislation will damage Tesoro's ability to do business in Alaska
- Price cap legislation will damage Alaska's value-add manufacturing future



**SB 31 – Testimony**  
***(in the following order)***

- 1.) Paul Thompson (via off-net)  
Ormat
- 2.) Nick Goodman (via off-net)  
TDX Power
- 3.) Sue Ely (in person)  
Alaska Conservation Alliance / Alaska Conservation Voters
- 4.) Dan Stickel (in person)  
Tax Division

There will probably be a couple of people calling in representing various utilities from around the state, but I don't have any confirmed names.

Available to provide the Department of Revenue's perspective and to answer questions will be:

Johanna Bales (via off-net)  
Deputy Director, Tax Division

**SB 54 – Invited Testimony**

Potential Testifiers:

Kip Knutson, Tesoro Alaska  
Justin Powell @ fairbanksgas.com (confirmed)  
Gabe Aceves at AKPIRG (invited)  
Called Lon Garrison – Sitka School Board (invited)  
Jim Schwartz – Petersburg School Board (invited)  
Mayor Weinstein (invited)  
Magaret Hansen – Kotzebue (confirmed)  
Merrick Pierce – Fairbanks (confirmed)