

**HB**

**280**

# SENATE COMMITTEE REPORT

DATE: 3/25/10

FURTHER: Finance

DATE TURNED  
IN TO OFFICE: \_\_\_\_\_

**Resources Committee** considered CS FOR HOUSE BILL NO. 280(FIN) am

## HB 280 NATURAL GAS: STORAGE/ TAX CREDITS

"An Act relating to a gas storage facility; relating to the Regulatory Commission of Alaska; relating to the participation by the attorney general in a matter involving the approval of a rate or a gas supply contract; relating to an income tax credit for a gas storage facility; relating to oil and gas production tax credits; relating to the powers and duties of the Alaska Oil and Gas Conservation Commission; relating to production tax credits for certain losses and expenditures, including exploration expenditures; relating to the powers and duties of the director of the division of lands and to lease fees for a gas storage facility on state land; and providing for an effective date."

and recommends:

- be replaced with  SCS or  CS HB 280 (RES)
- adopt previous  SCS or  CS \_\_\_\_\_
- attached amendment(s)
- adopt \_\_\_\_\_ Letter of Intent
- further referral to \_\_\_\_\_ Committee

<b>SENATE BILL:</b>	
<input checked="" type="checkbox"/>	Same Title
<input type="checkbox"/>	New Title
<hr/>	
<b>HOUSE BILL:</b>	
<input type="checkbox"/>	Same Title
<input type="checkbox"/>	Technical Title Change
<input type="checkbox"/>	New Title w/ SCR # _____


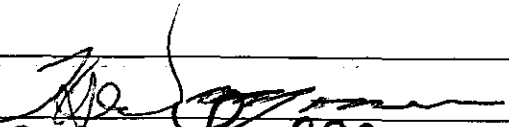
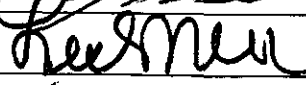
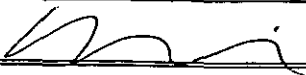
**NEW FISCAL NOTE(S):**

Department	Date	Fiscal	Indet.	Zero	FN#

**PREVIOUS FISCAL NOTE(S):**

Department	Date	Fiscal	Indet.	Zero	FN#
ADMIN	2/8			✓	1
DCCED	2/8			✓	2
DNR	3/5			✓	3
HFIN	3/23			✓	5

APPROPRIATION - no fiscal note

SIGNATURES AND RECOMMENDATIONS:	PRINTED LAST NAME	DO PASS	DO NOT PASS	NO REC	AMEND
	French			✓	
	WAGONER	X			
CO-CHAIR: 	McIure	✓			
CO-CHAIR: 	wiel	✓			

AMENDMENT

OFFERED IN THE SENATE

TO: CSHB 280 (FIN) am

1 Page 2, line 11:

2 Delete "and"

3

4 Page 2, line 13, following "day":

5 Insert "; and

6 (3) that the facility qualifies as a gas storage facility for the purposes of  
7 this section"

8

9 Page 9, line 4:

10 Delete ", treaters, and separators"

11 Insert "and gas treatment plants, but not including a liquefied natural gas or  
12 manufacturing plant or facility"

13

14 Page 9, line 19:

15 Delete "claimed"

16 Insert "received for each gas storage facility"

17

18 Page 10, lines 11 - 12:

19 Delete all material and insert:

20 "(4) must be regulated under AS 42.05 as a utility and be available to  
21 furnish the service of natural gas storage to the public for compensation; in this  
22 paragraph, "service of natural gas storage" has the meaning given in AS 42.05.990"

23

24

1 Page 10, line 28:

2 Delete "any taxable year ending before the date of the refund claim"

3 Insert "the calendar year in which the claim is made"

4

5 Page 11, lines 25 - 28:

6 Delete all material.

7

8 Reletter the following subsections accordingly.

9

10 Page 12, following line 24:

11 Insert a new bill section to read:

12 **\*\* Sec. 14.** AS 43.55.020(t) is amended to read:

13 "(f) If oil or gas is produced but not sold, **gas is produced but is stored in a**  
14 **gas storage facility**, or [IF] oil or gas is produced and sold under circumstances where  
15 the sale price does not represent the prevailing value for oil or gas of like kind,  
16 character, or quality in the field or area from which the product is produced, the  
17 department may require the tax to be paid upon the basis of the value of oil or gas of  
18 the same kind, quality, and character prevailing for that field or area during the  
19 calendar month of production or sale."

20

21 Renumber the following bill sections accordingly.

22

23 Page 12, line 25:

24 Delete "a new subsection"

25 Insert "new subsections"

26

27 Page 13, line 4:

28 Delete ""gas storage facility,""

29

30

1 Page 13, following line 5:

2 Insert a new subsection to read:

3 "(j) In this section, "gas storage facility" has the meaning given in AS 31.05.032"

4

5 Page 15, line 26 through page 16, line 12

6 Delete all material.

7 Insert "(o) For the purposes of (m) and (n) of this section, a Cook Inlet well lease

8 expenditure is a lease expenditure that is incurred in the Cook Inlet sedimentary basin that is

9 (1) directly related to an exploration well, a stratigraphic test well, a producing well,

10 or an injection well other than a disposal well, if the expenditure is a qualified capital

11 expenditure and an intangible drilling and development cost authorized under 26 USC

12 (internal Revenue Code) as amended and 26 C.F.R. 1.612-4, regardless of the elections

13 made under 25 U.S.C. 263(c); in this subparagraph an expenditure directly related to a

14 well includes an expenditure for well sidetracking, well deepening, well completion or

15 recompletion, or well workover, regardless as to whether the well is or has been a

16 producing well; or

17 (2) an expense for seismic work conducted within the boundaries of a production or

18 exploration unit."

# FISCAL NOTE

**STATE OF ALASKA**  
**2010 LEGISLATIVE SESSION**

Fiscal Note Number: 1  
 Bill Version: CSHB 280(L&C)  
 (H) Publish Date: 2/17/10

Identifier (file name): HB280-DOA-AOGCC-02-08-10 Dept. Affected: Admin  
 Title: "An Act relating to natural gas; relating to a gas storage facility; relating to the Regulatory Commission of Alaska..." RDU: AOGCC  
 Component: AOGCC  
 Sponsor: Representatives Hawker and Chenault  
 Requester: (H) L&C Component Number: 2010

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

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

	Appropriation Required	Information						
		FY 2011	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016
<b>OPERATING EXPENDITURES</b>								
Personal Services	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Travel	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Contractual	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Supplies	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Equipment	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Land & Structures	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Grants & Claims	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Miscellaneous	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<b>TOTAL OPERATING</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>0.0</b>	<b>0.0</b>

<b>CAPITAL EXPENDITURES</b>								
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<b>CHANGE IN REVENUES ( )</b>								
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**FUND SOURCE** (Thousands of Dollars)

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

Estimate of any current year (FY2010) cost: \_\_\_\_\_

**POSITIONS**

Full-time								
Part-time								
Temporary								

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

Additional work for the Alaska Oil and Gas Conservation Commission resulting from this bill could be managed by existing staff. The agency therefore submits a zero fiscal note.

Prepared by: Jody J. Colombie, Special Assistant I  
 Division: Alaska Oil and Gas Conservation Commission  
 Approved by: Rachael Petro, Deputy Commissioner  
Department of Administration

Phone (907) 793-1221  
 Date/Time 02/08/10 12:00pm  
 Date 2/8/2010

# FISCAL NOTE

**STATE OF ALASKA**  
**2010 LEGISLATIVE SESSION**

Fiscal Note Number: 2  
 Bill Version: CSHB 280(L&C)  
 (H) Publish Date: 2/17/10

Identifier (file name): HB280-CED-RCA-02-08-10 Dept. Affected: DCCED  
 Title: Natural Gas RDU: Regulatory Commission of Alaska (399)  
 Component: Regulatory Commission of Alaska  
 Sponsor: Hawker, Chenault  
 Requester: House Labor & Commerce Component Number: 2417

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

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

	Appropriation Required	Information						
		FY 2011	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016
<b>OPERATING EXPENDITURES</b>								
Personal Services	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Travel								
Contractual								
Supplies								
Equipment								
Land & Structures								
Grants & Claims								
Miscellaneous								
<b>TOTAL OPERATING</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>0.0</b>	<b>0.0</b>
<b>CAPITAL EXPENDITURES</b>								
<b>CHANGE IN REVENUES ( )</b>								

**FUND SOURCE** (Thousands of Dollars)

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

Estimate of any current year (FY2010) cost: 0.0

**POSITIONS**

Full-time								
Part-time								
Temporary								

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

The proposed legislation would provide financial incentives for natural gas storage facilities and for exploration in the Cook Inlet basin, and provide general guidance to the Regulatory Commission of Alaska (RCA) on natural gas pricing. Statutes governing the general powers and duties of the RCA would be revised to require the RCA, when considering whether approval of a natural gas supply contract is in the public interest, to (1) recognize the public benefits of a utility's ability to negotiate different pricing mechanisms with different suppliers and maintain a diversified portfolio of gas supply contracts to protect customers from the risks of inadequate supply or excessive costs that may arise from a single pricing mechanism, and (2) consider whether the utility could meet its responsibility to the public in a timely manner should the rate of gas supply contract not be approved.  
 (ANALYSIS CONTINUED)

Prepared by: Robert M. Pickett, Chairman  
 Division: Regulatory Commission of Alaska  
 Approved by: Emil R. Notti, Commissioner  
Commerce, Community, and Economic Development

Phone 907.276.6222  
 Date/Time 2/8/10 11:30 AM  
 Date 2/8/2010

**FISCAL NOTE #2**

**STATE OF ALASKA  
2010 LEGISLATIVE SESSION**

**BILL NO. CSHB 280(L&C)**

**ANALYSIS CONTINUATION**

This legislation would require that certain factors be recognized or considered when the RCA determines whether to approve natural gas supply contracts. The RCA expects to implement the provisions of this legislation with existing resources. The RCA can incorporate this review into the existing review process for natural gas supply contracts.

# FISCAL NOTE

**STATE OF ALASKA**  
**2010 LEGISLATIVE SESSION**

Fiscal Note Number: 3  
 Bill Version: CSHB 280(RES)  
 (H) Publish Date: 3/17/10

Identifier (file name): CSHB280-DNR-DOG-03-05-10 Dept. Affected: Natural Resources  
 Title: Cook Inlet Recovery Act RDU: Resource Development  
 Component: Oil and Gas Development  
 Sponsor: Rep. Hawker and Chenault  
 Requester: HRES Component Number: 439

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

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

	Appropriation Required	Information						
		FY 2011	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016
<b>OPERATING EXPENDITURES</b>								
Personal Services								
Travel								
Contractual								
Supplies								
Equipment								
Land & Structures								
Grants & Claims								
Miscellaneous								
<b>TOTAL OPERATING</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>0.0</b>	<b>0.0</b>

**CAPITAL EXPENDITURES**

**CHANGE IN REVENUES ( )** indeterminate

**FUND SOURCE** (Thousands of Dollars)

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

Estimate of any current year (FY2010) cost: \_\_\_\_\_

**POSITIONS**

Full-time								
Part-time								
Temporary								

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

HB 280 offers tax credits for Cook Inlet gas storage facilities and attempts to promote gas exploration and production in the Cook Inlet.

There is no anticipated fiscal impact to the Division of Oil and Gas for the management of gas storage on state land. However, Sec. 4 of the bill will provide a ten year "holiday" on all storage fees and rentals for the storage lease. Also, the accounting convention described means that "non-native" gas will be withdrawn from storage first and no royalty revenue will accrue to "native" gas until all non-native gas is withdrawn. How industry will respond to the tax credits offered by this bill is unknown, therefore, the impact on fees, rents, and royalty revenues is negative indeterminate.

Prepared by: Kevin Banks, Director  
 Division: Oil and Gas  
 Approved by: Tom Irwin, Commissioner  
Natural Resources

Phone 269-8800  
 Date/Time 3/5/10 12:00 PM  
 Date 3/5/2010

# FISCAL NOTE

**STATE OF ALASKA**  
**2010 LEGISLATIVE SESSION**

Fiscal Note Number: 4  
 Bill Version: CSHB 280(RES)  
 (H) Publish Date: 3/17/10

Identifier (file name): CSHB280(L&C)-REV-TAX-03-07-10 Dept. Affected: Revenue  
 Title: Cook Inlet Recovery Act RDU: Taxation and Treasury  
 Component: Tax Division  
 Sponsor: Representative Mike Hawker  
 Requester: (H) Resources Component Number: 2476

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

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

	Appropriation Required	Information						
		FY 2011	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016
<b>OPERATING EXPENDITURES</b>								
Personal Services	108.9	108.9	108.9	108.9	108.9	108.9	108.9	108.9
Travel	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0
Contractual	4.9	4.9	4.9	4.9	4.9	4.9	4.9	4.9
Supplies	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5
Equipment	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Land & Structures	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Grants & Claims	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Miscellaneous	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<b>TOTAL OPERATING</b>	<b>117.3</b>	<b>117.3</b>	<b>117.3</b>	<b>117.3</b>	<b>117.3</b>	<b>117.3</b>	<b>117.3</b>	<b>117.3</b>
<b>CAPITAL EXPENDITURES</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>0.0</b>	<b>0.0</b>
<b>CHANGE IN REVENUES ( )</b>	<b>***</b>	<b>***</b>	<b>***</b>	<b>***</b>	<b>***</b>	<b>***</b>	<b>***</b>	<b>***</b>

**FUND SOURCE** (Thousands of Dollars)

1002 Federal Receipts	0.0	0.0	0.0	0.0	0.0	0.0	0.0
1003 GF Match	0.0	0.0	0.0	0.0	0.0	0.0	0.0
1004 GF	117.3	117.3	117.3	117.3	117.3	117.3	117.3
1005 GF/Program Receipts	0.0	0.0	0.0	0.0	0.0	0.0	0.0
1037 GF/Mental Health	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Interagency Receipts	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<b>TOTAL</b>	<b>117.3</b>	<b>117.3</b>	<b>117.3</b>	<b>117.3</b>	<b>117.3</b>	<b>117.3</b>	<b>117.3</b>

Estimate of any current year (FY2010) cost: 0.0

**POSITIONS**

Full-time	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Part-time	0.0	0	0	0	0	0	0
Temporary	0.0	0	0	0	0	0	0

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

HB 280 would make multiple changes to the existing law on tax credits and gas storage facilities. The portions of the bill that specifically apply to the Department of Revenue would change the treatment of credits under AS 43.55.023 (Qualifying Capital Expenditures) and create a credit against corporate income tax (CIT) for gas storage facilities (AS 43.20.046). The language relating to credits has the potential to be interpreted quite broadly with the potential for large reductions in state revenues when compared to future developments that might occur under the current law.

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 new and modified state credits. (continued)

Prepared by: Cody Rice, Petroleum Economist II  
 Division: Tax Division  
 Approved by: Ginger Blaisdell, Director  
Administrative Services Division

Phone 907-269-1024  
 Date/Time 03-04-10; 4:27pm  
 Date 03-07-10; 1:31pm

FISCAL NOTE #4

STATE OF ALASKA  
2010 LEGISLATIVE SESSION

BILL NO. CSHB 280(RES)

**ANALYSIS CONTINUATION**

There are three gas storage facilities currently operating in the Cook Inlet region. None of the existing gas storage facilities would qualify for the corporate income tax credits under this bill as currently written. However, it is unclear if the existing gas storage facilities could qualify for credits if they shut-down and re-opened or changed ownership. Any estimate of the change in revenues to the state under this legislation would be based on hypothetical development in the future. As a result, the full revenue impact of this legislation cannot be accurately determined at this time.

The following scenarios may provide some perspective on the range of potential revenue impacts.

**Scenario 1: Corporate income tax credit effects on a small facility**

The first scenario assumes the construction of a small gas storage facility in a depleted reservoir similar to one of the smaller currently operating gas storage facilities. The facility is assumed to be capable of approximately 1.25 cycles a year and to have a working gas capacity of approximately 1Bcf. Under the terms of HB 280 this facility would be entitled to a credit of \$1.5 Million against state CIT.

In 2004, the Federal Energy Regulatory Commission (FERC) estimated the median cost-of-service rate for firm storage service at \$0.64/Decatherm. One Decatherm is equal to one Mcf of natural gas if the natural gas contains 1,000 Btu/cubic foot. Escalating this cost for inflation produces a 2009 cost-of-service rate of approximately \$0.72/Mcf of firm storage service.

Given the estimated cost-of-service, volume of gas cycled and reasonable assumptions about debt to equity and other factors, the Department of Revenue estimates that this gas storage facility would owe approximately \$95,000/year in state CIT. This rough estimate suggests that the corporate income tax credit for gas storage created under AS 43.20.046 of this bill would entirely offset the state corporate tax liability for nearly the first 16 years of operation. It is important to note that the credit created in this bill under AS 43.20.046 is eligible to be transferred or refunded.

There is a credit clawback provision that applies if the gas storage ceases commercial operations within ten years. However, in this scenario, the amount of the original credit remaining after ten years of commercial operations is estimated to be \$550,000. This means the storage operator in this scenario could cease to operate at the beginning of year 11 and theoretically retain as much as \$550,000 in refundable state credits. Additionally, under HB 280, the facility would be exempt from rental and storage fees charged by the Department of Natural resources (DNR) for the first ten years of commercial operations. There is also some question about whether the existing statute of limitations would allow the state to exercise the clawback provision.

Under this scenario the reduction in state taxes to the state is \$1.5 million in undiscounted terms for each qualifying facility of this type. This does not include reductions in estimated rental and storage fees.

**Scenario 2: Corporate income tax credit effects on a large facility**

Scenario two assumes the construction of a large gas storage facility in a depleted reservoir. The facility is assumed to be capable of cycling approximately one time each year and to have a working gas capacity of

FISCAL NOTE #4

STATE OF ALASKA  
2010 LEGISLATIVE SESSION

BILL NO. CSHB 280(RES)

**ANALYSIS CONTINUATION**

Under the terms of HB 280 this facility would be entitled to the maximum credit of \$30 million against state corporate income tax.

Using the same cost-of-service and financial assumptions as scenario one, the Department of Revenue estimates that the gas storage facility owner would owe approximately \$1.5 million annually in state CIT. This rough estimate suggests that the corporate income tax credit created under AS 43.20.046 would completely offset the state corporate income tax liability for about 20 years of operation. It is important to note again that the credit created in this bill under AS 43.20.046 is eligible to be transferred or refunded. There is a credit clawback provision that applies if the gas storage ceases commercial operations within ten years. However, in this scenario, the amount of the original credit remaining after ten years of commercial operations is estimated to be \$15,000,000. This means the storage operator in this scenario could cease to operate at the beginning of year 11 and theoretically retain as much as \$15,000,000 in refundable state credits. The facility would also be exempt from rental and storage fees charged by the Department of Natural resources (DNR) for the first ten years of commercial operations.

Under this scenario the reduction in state taxes to the state is \$30 million in undiscounted terms for each qualifying facility of this type. This does not include reductions in estimated rental and storage fees.

**Scenario 3: Broader interpretation of HB 280 benefits**

Previous scenarios have assumed gas storage facilities operated at nearly 100% of capacity, using 100% of certified storage capacity. This scenario assumes a gas storage operator takes full economic advantage of a broad interpretation of the language in HB 280. Specifically, the facility uses a reservoir with a working gas capacity of 20 Bcf and the operator only cycles the minimum amount of gas to prevent the loss of the credits: 10,000 Mcf of natural gas annually. Using the same cost-of-service and financial assumptions as the previous two scenarios, the Department of Revenue estimates that the gas storage facility owner would owe less than \$1,000 annually in state CIT. The storage facility owner would be eligible for a credit of \$30,000,000 for the facility based on the working gas capacity. In this scenario it would take nearly 4,000 years of operation under this scenario for a gas storage operator to exhaust the state corporate income tax credit provided under this bill. Alternatively, after 10 years of commercial operation the owner could shut the facility down and retain \$29,990,000 in refundable state credits.

**Scenario 4: Lost or deferred production and production tax revenue**

Previous scenarios have assumed gas storage in a depleted reservoir. It is possible that an oil and gas lessee could elect to shut-in production at a currently producing field earlier than would have otherwise occurred in order to take full advantage of plentiful native gas for free cushion gas. Under this bill the remaining native gas could be produced at the end of commercial operations for the gas storage facility. This deferred or lost production tax revenue would be in addition to lost revenue impacts equivalent to any of the previous three scenarios. The time value of deferred production is not calculated but could be substantial.

**Scenario 5: Tax Ceiling**

Existing state law provides the benefit of a tax ceiling for certain production under AS 43.55.011(j)(k) and (o). The tax ceiling applies to Cook Inlet production as well as any natural gas produced for use in state. Currently, credits earned under AS 38.05.180(i), AS 41.09.010, AS 43.55.024 or AS 43.55.025 are required to be applied first to a producers tax liability under AS 43.55.011(e) as though it were not limited by AS 43.55.011(j)(k) or (o).

FISCAL NOTE #4

STATE OF ALASKA  
2010 LEGISLATIVE SESSION

BILL NO.

CSHB 280(RES)

**ANALYSIS CONTINUATION**

Under HB280, the limitation on application of credits does not apply to Cook Inlet production after January 1, 2011. This change would allow credits from Cook Inlet expenditures to also be applied to other non-Cook Inlet tax liability. In essence producers would earn credits and apply their full value against state wide tax liability and also receive the benefit of the reduced tax rate resulting from the comparison of actual tax rate (using those credits) and the prior ELF rate or ceiling rate. This repeal is likely to have the effect of reducing Cook Inlet tax collections to zero and allowing Cook Inlet credits to be used to shield taxes due from operations in other parts of Alaska such as the North Slope. This provision would be a particular benefit to companies operating in both Cook Inlet and on the North Slope.

Scenario five entails a producer with production in both Cook Inlet and on the North Slope. Assume the producer is entitled to a credit of \$12 million under AS 43.55.025 because of Cook Inlet Exploration Expenditures, and assume that the producer's total production taxes are approximately \$18 million, with \$16 million attributed to North Slope production and \$2 million attributed to Cook Inlet production.

Under existing law, AS 43.55.011(m) requires the producer to apply the \$12 million in Cook Inlet credits to the full value of its hypothetical .011(e) Cook Inlet tax liability even though the Cook Inlet tax ceiling rate is applicable. Applying the \$12 million credit against \$2 million of .011(e) Cook Inlet production tax leaves \$10 million in excess credits that may be used to offset tax liability elsewhere in the state. The tax ceiling rate on Cook Inlet oil is zero; therefore \$2 million of the credit is considered "used" under AS 43.55.011(m).

Under current law, the North Slope tax liability of \$16 million would be offset by the \$10 million in credits left over after application of AS43.55.011(m), leaving a production tax liability of \$6 million. Under HB 280, the producer would not have to draw down its \$12 million of Cook Inlet tax credits, and instead be allowed to apply the full \$12 million to the \$16 million North Slope tax liability. As a result, the producer would pay a total of \$4 million in production tax under this scenario, or \$2 million less than under the existing law.

This scenario is a simplified version of how HB 280 might affect state revenues. Because AS 43.55.011(m) applies to multiple types of credits, and multiple taxpayers, the revenue effects could be significant.

**Additional Scenarios and Fiscal Impacts:**

The effect of increasing the value of credits for well work in Cook Inlet to 40% under AS 43.55.023(m) is not quantified in this analysis but would reduce tax revenues.

There could be additional reductions in state tax revenues if other existing facilities or natural gas pipelines were certified as gas storage and eligible for credits. This bill does not limit the credit for gas storage to the Cook Inlet, and in fact could be applied to gas stored on the North Slope or other areas of the state.

Cook Inlet production tax and additional production caused by the injection or withdrawal requirements under this proposal are very unlikely to generate more than a small fraction of the revenue that would be required to fund this credit. This means production taxes from other areas of the state, such as the North Slope would likely be the source of funds to the tax credit fund for the state to repurchase this credit.

# FISCAL NOTE

STATE OF ALASKA  
2010 LEGISLATIVE SESSION

Fiscal Note Number: 5  
 Bill Version: CSHB 280(FIN)  
 (H) Publish Date: 3/24/10

Identifier (file name): CSHB280(FIN) -REV-TAX-3-23-10 Dept. Affected: Revenue  
 Title: Cook Inlet Recovery Act RDU: Taxation and Treasury  
 Component: Tax Division  
 Sponsor: Representative Hawker  
 Requester: House Finance Committee Component Number: 2476

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

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

	Appropriation Required	Information						
		FY 2011	FY 2012	FY 2013	FY 2013	FY 2014	FY 2015	FY 2016
<b>OPERATING EXPENDITURES</b>								
Personal Services								
Travel								
Contractual								
Supplies								
Equipment								
Land & Structures								
Grants & Claims								
Miscellaneous								
<b>TOTAL OPERATING</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>0.0</b>	<b>0.0</b>

<b>CAPITAL EXPENDITURES</b>								
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<b>CHANGE IN REVENUES ( )</b>								
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**FUND SOURCE** (Thousands of Dollars)

1002 Federal Receipts								
1003 GF Match								
1004 GF								
1005 GF/Program Receipts								
1037 GF/Mental Health								
Other-AHFC Receipts								
<b>TOTAL</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>0.0</b>	<b>0.0</b>

Estimate of any current year (FY2009) cost: \_\_\_\_\_

**POSITIONS**

Full-time								
Part-time								
Temporary								

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

Prepared by: Co-Chair Rep. Stoltze  
House Finance Committee  
Co-Chair Rep. Hawker  
House Finance Committee

Phone 465-4958  
 Date/Time 3/23/2010 4:55PM  
 Date 3/23/2010

# Representative Mike Hawker

## Alaska State Legislature



### House Bill 280

### "The Cook Inlet Recovery Act"

### Sponsor Statement

Residents of South Central Alaska are at risk that in the near future there will not be enough natural gas produced in Cook Inlet to heat and light their homes and businesses. Legislative action now can help address this challenge before it becomes a crisis.

A critical and universally recognized part of the solution is large-scale gas storage, allowing utilities to purchase gas during lower demand periods; hold the gas in storage; then withdraw it when needed. Establishing gas storage is crucial, and the state needs to promote the rapid development of storage facilities. House Bill 280, the Cook Inlet Recovery Act (CIRA), provides tax incentives and regulatory assurances to attract the private investment necessary to develop storage facilities and help reduce the cost of storage to consumers.

Specifically, CIRA provides a 10-year exemption from state land lease fees and rents to owners of new gas storage facilities. Since storage is needed urgently, these financial incentives will be available only for facilities put into operation before December 31, 2015. CIRA sets standards, such as minimum size and access requirements, for qualifying projects. Consumers will benefit from increased energy security and lower energy costs, as any financial incentives are required to pass through the supply chain to utilities and, in turn, to their customers.

In addition to storage, South Central also needs new gas discoveries. CIRA increases the incentives for exploration in Cook Inlet and allows explorers and producers to take their full benefit in one year rather than over two years.

CIRA also provides statutory guidance to the Regulatory Commission of Alaska in its consideration of utility gas supply contracts to help ensure adequate supplies of reasonably priced gas in the years ahead.

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*Girdwood*  
*Portage*  
*Whittier*  
*Sunrise*  
*Hope*

2/5/10

## HB 280

### Cook Inlet Recovery Act - Sectional Analysis

Prepared by Representative Mike Hawker's Office

- Section 1:** Sets out a short title for the legislation: Cook Inlet Recovery Act (CIRA).
- Section 2:** Establishes an application process, criteria and timeline for the Alaska Oil and Gas Conservation Commission (AOGCC) to certify that a gas storage facility (GSF) meets the minimum working gas storage capacity and daily delivery rate requirements to be eligible for the financial incentives provided in this bill.
- Requires a GSF owner to notify the AOGCC if the facility ceases operation.
- Provides definitions for terms used in CIRA.
- Section 3:** Requires the Director of the Division of Mining, Land and Water to give priority to and expedite "when reasonably possible" any applications, permits and lease assignments needed for development and operation of a GSF.
- Section 4:** Prohibits the Department of Natural Resources from denying a lease application for a natural gas storage facility solely because the facility would be used exclusively or primarily to store gas owned by the owner or operator of the facility.
- Section 5:** Directs the Department of Natural Resources (DNR) to waive any state land lease fees or rents for the first 10 years of a GSF's operation. The waiver would stop if the storage facility ceases commercial operations.
- States that any waivers of lease fees or rents would be public record.
- Requires that the GSF pass on the financial benefits of any lease exemption to utilities that use its service.
- Clarifies that any gas withdrawn from a GSF is considered to be non-native gas and not subject to royalty until all non-native gas is withdrawn.
- Section 6:** Directs the Regulatory Commission of Alaska (RCA), when considering the approval of a utility's gas supply contract, to consider the impact on consumers if the commission rejects a utility's gas supply contract and to recognize the value of a utility holding a diversified portfolio of gas supply contracts with different pricing mechanisms in order to protect consumers from inadequate gas supplies and the risk of a single pricing mechanism.
- Section 7:** Requires that a utility's cost of gas storage that is passed on to consumers reflect the financial benefits of any tax credits and state lease exemptions provided in this legislation.
- Section 8:** Clarifies that a natural gas storage facility that is part of a regulated natural gas pipeline (regulated under AS42.06) shall not also be regulated as a utility under the new provisions of AS42.05 in this bill.

**Section 9:** Specifies that the Regulatory Commission of Alaska has jurisdiction over natural gas storage services provided for gas that is owned by a regulated utility.

**Section 10:** Further defines "natural gas storage facility" and clarifies what is considered part of the storage facility.

Further defines that RCA regulation of gas storage facilities is limited to facilities operated primarily or exclusively for third-party customers; regulation does not extend to a proprietary storage facility operated exclusively or primarily to hold gas owned by the storage facility owner or operator.

**Section 11:** Clarifies that the names of taxpayers and the amount of credits claimed for gas storage facilities under this legislation shall be public information. Requires the Department of Revenue (DOR) to furnish the information to the RCA.

**Section 12:** Establishes a credit against corporate income taxes of \$1.50 per thousand cubic feet of new gas storage capacity opened in Alaska during 2011-2015. The credit is limited to the lesser of \$15 million or 25% the costs incurred to establish the GSF. This section sets out minimum capacity and deliverability requirements to qualify for the credit, including that the GSF must be available for use by regulated utilities and, if utilizing state land, must be in compliance with its DNR storage lease. The credit can be refunded by the state at full value if the owner does not have enough taxable income to fully utilize it.

**Section 13:** Sunsets on Jan. 1, 2011, the rule that limits how certain tax credits arising from activity in Cook Inlet or from producing gas for in-state use are used. This would allow a Cook Inlet explorer or producer to explore or produce elsewhere in the state and have full access to the credits it earned from its Cook Inlet activities.

**Section 14:** Clarifies that any native gas in a gas storage facility shall be deemed not to be produced for production tax purposes until all of the non-native gas injected into the storage facility has been withdrawn.

**Section 15:** Allows explorers in Cook Inlet to receive their full production tax credit in the first year rather than over two years (as in current statute).

**Section 16:** Makes additional statutory changes to allow explorers in Cook Inlet to receive their full production tax credit the first year rather than over two years (as in current statute).

**Section 17:** Adds the new Cook Inlet-related well tax credits to the section in statute dealing with audits of transferred tax credits.

**Section 18:** Provides a 40% credit for exploration expenses in Cook Inlet against production taxes, rather than the two-tiered 30% / 40% credit in existing statute. In addition, all well-related lease expenditures in Cook Inlet, including non-capital and non-exploration related lease expenditures, also qualify for the credit. The section also defines which expenses qualify as a "Cook Inlet well lease expenditure" to be eligible for the tax credit.

- Section 19:** Allows the state to use funds from the oil and gas tax credit fund to refund the tax credits issued to a GSF.
- Section 20:** Makes additional changes to make it easier for a company to sell its Cook Inlet exploration credits to the state. Current law requires that before a company can sell credits back to the state it must prove it has spent an amount equal to the credit in Alaska. HB 280 would eliminate that requirement for Cook Inlet exploration credits.
- Section 21:** Authorizes the Department of Revenue to write regulations implementing certain aspects of Section 17.
- Section 22:** Directs the Office of Public Advocacy for regulatory affairs at the Department of Law, when considering whether to participate in a utility rate case regarding a utility's gas supply contract before the RCA, to consider the impact to consumers if the commission rejects a utility's gas supply contract and to recognize the value of a utility holding a diversified portfolio of gas supply contracts with different pricing mechanisms in order to protect consumers from inadequate gas supplies and the risk of a single pricing mechanism.
- Section 23:** Immediate effective date clause.