Alaska's Oil Production Tax: A Brief History

By Lisa Weissler

Abstract: For decades, Alaska's politicians and the oil industry have sparred over the state's tax on its oil resources. This paper examines newspaper accounts, legislative history, and Alaska history books to construct a narrative of the people and politics involved in the state's long and contentious oil tax debate – a debate that continues in the halls of Alaska's capitol today.

The history of oil in Alaska is the latest chapter in the saga of natural resource exploitation that began long before the United States purchased Alaska from Russia. First came the Russian fur traders who decimated wildlife populations, oppressed Alaska Natives, and left little of lasting value. After the 1867 purchase of the territory by the U.S., individuals and corporations mined, harvested, fished, and trapped without being burdened by much in the way of taxation. The result was a territory rich in resources yet still lacking the funds for its own economic development.

Upon assuming his appointment as Alaska's territorial governor in 1939, Ernest Gruening found Alaska to be a land of both promise and problems. The promise lay in the people, the land and the territory's abundant natural resources. Among the territory's problems was its lack of taxation that would capture economic benefit from resource extraction. Gruening made it his mission to establish a tax system that would provide revenue for the improvement and welfare of the territory.

For the next nine years, outside interests, primarily salmon canning and mining companies, exerted enough influence on territorial legislators to succeed in defeating every major tax measure that Gruening put forward. The territory's financial condition deteriorated to the point that vendors were threatening to cut off delivery of supplies and the University of Alaska was on the brink of collapse. Finally, in 1948, Alaskans voted out most of the sitting legislators, including the staunchest tax opponents. During the 1949 legislative session, the new crop of legislators passed a comprehensive tax system that would raise revenue for the territory and help fund needed public services. Gruening praised legislators' action, saying they represented the desire of the people to "plow back" the wealth derived from Alaska's resources into the development of Alaska and to making the territory their home.[1]

The long-running battle over taxation between Gruening, territorial legislators, and the mining and fishing industries set the stage for Alaska's future relationship to oil and the oil industry. As is often the case, the past was prelude to the future.[2]

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Major components of Gruening's 1949 tax system were an income tax and a general property tax. In 1953, the legislature swung from a Democratic majority to Republican. Republican legislators had long opposed Gruening's general property tax and one of the new majority's first acts was to repeal the tax. Two years later, an attempted resurrection of the property tax played a major role in establishing Alaska's first oil and gas tax.

Among the new legislators joining the 1955 territorial legislature was Representative Irene Ryan, a Democrat from Anchorage. Ryan stood out as the first woman to fly solo in Alaska, the first woman to graduate from the New Mexico School of Mines, and the first female mining engineer and geologist in Alaska. In 1954, Ryan foretold an oil-producing era in Alaska that would "rank with the largest in North America."[3]

Rep. Stanley McCutcheon, D-Anchorage, shared Ryan's conviction. In 1949, McCutcheon helped shepherd Governor Gruening's tax package to success. McCutcheon made reinstatement of the general property tax a priority for the 1955 territorial legislative session. He and Ryan, along with fellow Democrats who were now back in the majority, wanted the property tax in place as a way to tax the oil industry if one developed in Alaska.

In the course of the session, mining and fishing interests succeeded in turning a majority of senators against the property tax legislation. At one point, McCutcheon accused the Senate of being the "salmon-controlled senate" and said that their sympathies were with people "not concerned about the best interests of Alaska."[4]

After months of bitter debate, a solution presented itself. The House majority agreed to drop the general property tax proposal and instead introduce stand-alone oil and gas production tax legislation crafted by Ryan. A production tax, also known as a severance tax, is a tax levied by a sovereign government as compensation for the taking of a nonrenewable resource. Unlike a property tax that would apply to the resource in the ground, a production tax is levied when production takes place based on either the quantity produced or the value of the produced resource.

Under Ryan's proposal, Alaska would put a one percent tax on the gross value of oil produced in the territory. The gross value was determined by measuring production at the wellhead and subtracting transportation costs from the destination sales price. The production tax would be in lieu of a property tax.

The oil and gas production tax legislation passed the full House on the same day it was introduced on a vote of 17 to 2. The Senate passed it the next day with just three "no" votes. Three days later, on April 6, 1955, Governor Frank Heintzleman signed the bill into law without comment. With that, Alaska had its first oil and gas production tax.[5]

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Though the oil and gas production tax passed without much dissent, the story might have been different with more time for debate. Three days after the bill was signed into law, the Anchorage Daily Times owner, Robert "Bob" Atwood, published a scathing editorial blasting the new tax. He declared it "one of the worst pieces of legislation passed by the 1955 legislature," and complained that the tax would discourage oil companies from doing business in Alaska.[6]

At the time, Atwood and several other Anchorage businessmen, known as the "Spit and Argue Club," were working with the Richfield Oil Corporation in an effort to jumpstart oil development in Alaska. Richfield was in the process of applying for oil and gas leases in the Kenai National Moose Range. To prevent a monopoly on oil development in the range, the federal government imposed a 100,000-acre limit on the amount any one company could lease. To get around the limit, Richfield entered into an agreement with Spit and Argue club members where members would apply for leases. If oil was found, Richfield would buy their leases and pay them royalties on the oil production.[7]

Atwood and his fellow businessmen were ardent statehood supporters. They hoped that the possibility of oil revenue would convince President Eisenhower and Congress that Alaska could support itself as a state. Though their intent in working with Richfield may have been driven by their desire for statehood, the agreements paid off handsomely when, in 1957, Richfield discovered commercial quantities of oil in the Swanson River oil and gas field located in the Kenai Moose Range. Besides making millions for the Anchorage businessmen, this discovery set in motion Alaska's first oil boom, and the start of a long battle over the state's oil and gas production tax.[8]

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In the years following the discovery of oil in commercial quantities on the Kenai Peninsula, oil and gas development in the region increased exponentially. In 1964, companies developed the first producing oil wells on state owned offshore lands in Cook Inlet. By the end of 1965, there were seven producing offshore oil wells and fifty-three producing wells on the federally owned Swanson River field. An oil pipeline connected the Swanson field to a refinery in Nikiski; a natural gas pipeline transported Kenai gas to Anchorage; and the first offshore pipeline would soon be completed to connect offshore Cook Inlet fields to central production facilities being constructed on the Kenai Peninsula shore. On the North Slope, more than fifteen oil companies held leases on federal lands, and an oil and gas lease sale was scheduled for additional areas.

During the 1966 legislative session, Rep. Norbert Skinner, D-Clear, introduced the first proposed increase to the state's oil and gas production tax. House Bill 416 would raise the tax from one to eight percent. It also required that the increased oil tax revenue be used as a basis for a decrease in the state income tax. Skinner said he introduced the bill because he didn't want to see a repeat of what happened in the salmon industry. "Take some and leave some," he said, "the state must take the initiative to see that a reasonable return is realized for the people. Once the oil comes out of the ground, the opportunity for revenue is gone forever."[9]

The attacks on Skinner's proposal came fast and furious, both from fellow legislators and oil industry officials. Sen. John Butrovich, R-Fairbanks, said the bill was "nothing more than a baseball bat," that would discourage oil and gas development in Alaska. Oil company representatives warned that any increase to the production tax would have an adverse effect on further exploration. And Rep. Bruce Kendall, R-Anchorage, went so far as to introduce a resolution requesting consideration of a constitutional amendment that would prohibit changing the laws on oil and gas taxation. The resolution was referred to a special committee on the constitution where it died with no action taken.[10]

On a vote of 15 to 22, the House voted to postpone action on HB 416 indefinitely. A 1967 proposal to increase the production tax to four percent also failed to garner support. It would take a disaster for legislators to agree to the state's first oil and gas production tax increase.

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In August 1967, a massive flood devastated the Fairbanks region. At the end of September, Governor Walter Hickel called a special legislative session to deal with the costs of recovery. Among other relief measures, the governor proposed a two-part tax program – a $10 annual tax on every employed person in Alaska, both resident and nonresident; and a "Disaster Severance Tax" that added a one percent tax to the existing oil and gas production tax. The new revenues would go into a disaster relief account that would be used to help pay flood recovery costs, and to provide a cushion for future disaster costs. Tax collections would automatically cease once accumulated funds reached $7.5 million, and automatically be reinstated when the fund went below $5 million.[11]

The legislative debate on the proposed oil and gas production tax increase took a different track from prior attempts at raising the tax rate. For one thing, oil company opposition was absent. For another, legislators who previously opposed a tax increase got behind Hickel's proposal. Conversely, legislators who supported a higher production tax opposed the legislation, partly because they thought there were sufficient existing funds to cover flood relief, and because they viewed the one percent disaster oil tax as a ploy to prevent higher taxes as the oil industry grew in the future.[12]

House majority leader Rep. Ted Stevens, R-Anchorage, led the effort to pass the flood relief package. Stevens and other House leaders made it clear that the relief package was an all-or-nothing proposition. The pressure worked and, after just six days, the special session concluded with passage of the entire relief package, including the addition of the one percent disaster oil tax, bringing the total oil and gas production tax rate to two percent.[13]

Legislators unhappy with the outcome of the 1967 special session introduced oil tax legislation within days of the legislature convening in January 1968. Senator Maurice Smith, R-Fairbanks, introduced Senate Bill 235 that would raise the oil and gas production tax to 3.5 percent. Rep. Tom Fink, R-Anchorage, followed suit with HB 376, a bill to repeal the disaster production tax of one percent and increase the total oil tax rate to four percent on high volume producing wells.

"As a matter of equity," Fink said, "the oil extracted from state lands should be paying at least a four percent severance tax." Fink noted that four percent was considerably less than the tax being paid in other states. Twenty House members signed on as co-sponsors to Fink's bill, eleven Republicans and nine Democrats.[14]

While oil companies were largely absent during the 1967 oil tax debate, the new bills caught their attention. During a joint House and Senate Finance Committee hearing, K.C. Vaughan, an oil industry representative, presented what would become the industry's script for decades to come. Vaughan urged legislators to maintain a political climate and incentives conducive to continuing investment by the industry; warned that Alaska must be competitive with other oil and gas regimes; and argued for tax stability.[15]

Most legislators were not swayed by Vaughan's testimony. They were particularly frustrated by his refusal to provide figures on industry profits. Vaughan willingly provided extensive, detailed information about the overall costs of oil exploration and development in Alaska and projected benefits to the state. However, he consistently asserted there were too many unknowns to answer legislators' questions about the potential industry profit from Alaska oil, and that the companies would consider any available information confidential. Senator Smith complained that without that information, legislators were "just crawling around in the dark," trying to determine the right tax rate.[16]

Despite broad Republican and Democratic support for an oil tax increase, the Republican leadership in the House opposed the tax bills. When the House Finance Committee chairman, Rep. Harold Strandberg, R-Anchorage, refused to bring any oil tax bill up for a hearing in his committee, Rep. Fink took the unprecedented move of circulating a petition among House members asking the Rules committee chair, Rep. Clem Tillion, R-Halibut Cove, to block the budget appropriation bill from being voted on until Strandberg took up a Senate version of the oil tax bill. Strandberg finally capitulated and allowed a vote when twenty-six House members indicated they were prepared to force the senate bill out of the House Finance committee.[17]

In the end, the legislature passed an oil and gas production tax increase raising the base oil tax rate from one to three percent. With the disaster tax, the total tax would be four percent on the gross value of oil and gas. The bill passed with just six no votes in the Senate and eight in the House. Though Governor Hickel was not a fan of the increase, he allowed the measure to become law.[18]

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By the time the next legislature convened in January 1969, Prudhoe Bay had been confirmed as a world-class giant oil field on Alaska's North Slope. The find spurred an increase in the number of oil company lobbyists converging on the state capitol. Oil companies had cause for concern. A tax study initiated by the 1968 legislature recommended increasing the oil production tax on a scale from seven to ten percent.[19]

Rep. Fink introduced new oil tax legislation a few days after the start of the legislative session. Under HB 75, Fink proposed a cents-per-barrel tax system that would effectively raise the oil tax from four percent to eleven percent in basins with more than 100,000 barrel per day production; and put the tax at three percent for basins producing less. As HB 75 progressed through the session, two camps formed. One, headed by Fink, contended Alaska wasn't getting a fair share of oil revenue when compared to other states. The other, led by Senate President Brad Phillips, R-Anchorage, opposed any tax increase out of concern that a higher tax rate would jeopardize the amount companies would be willing to bid in an upcoming North Slope oil and gas lease sale. After HB 75 passed the House on a vote of 31 to 9, Phillips buried it in three committees, leaving the measure no chance to get through the Senate before the end of the session.[20]

Commenting on the failure to pass a tax increase that year, Rep. Barry Jackson, D-Fairbanks, opined that maintaining a low tax rate was "an invitation to the oil industry to intervene in the politics of the state." Jackson said, "The oil companies intend to buy the State of Alaska and its government, and in such a manner we won't know what's happening."[21]

In September 1969, oil companies paid a record $900 million in bonus bids for North Slope leases and the right to drill for oil and gas on state-owned land. The same week as the lease sale, the first shipment of pipe for an 800-mile trans-Alaska oil pipeline arrived in Valdez, the pipeline's southern terminus.[22]

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While a majority of House members maintained their support for HB 75 that had carried over from the previous legislative session, most of the Senate remained lukewarm to any new oil tax proposal in the 1970 session. Along with Governor Keith Miller, senators were concentrating their efforts on making a deal with oil companies to jumpstart construction of a North Slope pipeline access road. The plan was for the state to build the road and the companies would repay the costs later. Senators feared an oil tax increase would keep companies from agreeing to the road deal.[23]

Near the end of the long legislative session, friction between the House and Senate grew to the point that Rep. Mike Bradner, D-Fairbanks, accused Senate President Phillips of consistently having motives "identical to those of the oil industry." Bradner lamented the "amount of effectiveness the oil lobbyists" had gained in Juneau, saying that, "If the taxpayers don't get a fair severance tax this year they may never get it." For their part, the oil lobbyists were arguing that the state should take the majority of its oil money from bonus bids for oil and gas leases rather than production taxes.[24]

On June 7, 1970, the final day of the 147-day session, the House and Senate settled on a version of HB 75 that established a stair-stepped oil and gas production tax where the more a well produced, the greater the tax – three percent on a well's first 300 barrels a day; five percent on its next 700; six percent on its next 1500; and eight percent on any production in excess of 2500 barrels a day. As with the original tax, the new tax rates would be assessed on the value of oil at the wellhead – the market price less transportation costs. The one percent disaster production tax was repealed, and the tax rate for gas was raised to four percent. The final version of HB 75 passed the Senate on a vote of 17 to 2; in the House it passed 30 to 9.[25]

With agreement on the production tax, the House approved the North Slope road authorization bill the Senate wanted, but inserted a clause requiring that the cost of the road be paid back to the state within five years at 7.5 percent interest. The legislature also approved a $120 million appropriation to fund the road's construction. However, it was all for naught. Ultimately, Governor Miller and the pipeline owners were unable to agree on a plan for North Slope road construction. The oil company pipeline consortium, now called the "Alyeska Pipeline Service Co.," finally constructed the road in 1974.[26]

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In 1972, a new problem presented itself. The massive North Slope oil find remained untapped due to delays in pipeline construction. Once built and oil was flowing, the companies that owned the pipeline would recover construction and operating costs through tariffs charged to the producers transporting oil through the pipeline. The producers would be allowed to deduct the tariff in calculating their production tax and royalty obligations to the state. A study commissioned by Governor Bill Egan showed that escalating pipeline construction costs would result in such high tariffs that their deduction would reduce the state's production tax and royalty revenue to less than zero.[27]

There was another twist. The companies that were part of the Alyeska pipeline partnership were also part of the same corporations as the companies that would be producing the oil. Egan worried that with monopolistic control of oil production and transportation, the companies would profit from oil development even when the state got nothing. He was also concerned about inadequate constraints on construction costs and limited federal regulatory authority over the amount of tariff Alyeska could charge for transporting oil through the pipeline. As a solution, Egan proposed the state construct and own the pipeline itself.[28]

The Senate rejected the state ownership concept, proposing instead its own solution for controlling pipeline costs. Alyeska would need right-of-way leases from the state to build the pipeline across state lands. Senator Chancy Croft, D-Anchorage, proposed using the state's contracting authority as a landowner to condition the right-of-way leases so that the more tariff the company charged, the higher the rent on the leases. The idea was that this would discourage Alyeska from charging high tariffs.[29]

Not convinced that the right-of-way leasing legislation would sufficiently protect Alaska's interests, Governor Egan proposed an alternative cents-per-barrel oil production tax; the tax paid would be the greater of the existing wellhead value tax or the new cents-per-barrel alternative. The cents-per-barrel tax would ensure the state received revenue no matter how low the wellhead value tax went down.[30]

In the Capitol halls, oil lobbyists hinted that companies would pull out from the North Slope pipeline project or sue the state if the right-of-way leasing act or oil tax amendments passed. Egan responded to these rumors, saying, "Lobbyists can tell you anything, and I know they'll be telling legislators everything – they'll be using every trick in the book to try to keep from just having a fair and honorable profit off the people of Alaska's crude oil resources." Senator Croft commented, "Anytime the state has significantly improved its position as far as the oil companies are concerned, they've always threatened that they would either pull out or consider pulling out."[31]

In June 1972, at the end of another long contentious session, the legislature passed the alternative cents-per-barrel oil production tax and the right-of-way leasing legislation. No oil company withdrew from Alaska; though they did follow through on their threat to sue the state. In September of that year, ten companies joined together in lawsuits filed in state superior court challenging the right-of-way and oil tax legislation as well as a pipeline regulatory oversight bill that also passed in the 1972 session.[32]

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The start of the legislative session in January 1973 saw continuing delays in pipeline construction, and increasing budget problems for the state. However, the energy crisis engendered by conflicts in the Middle East was prompting national interest in North Slope oil and in getting the Trans Alaska Pipeline built as quickly as possible.

During the 1973 regular session, Governor Egan and legislators adopted a "wait and see" approach regarding the pending lawsuits over the 1972 oil legislation. If the court ruled against the state, legislators would then address how to tax and regulate the oil industry in Alaska.[33]

The resolve to wait did not last. As Congress began taking action on federal legislation to encourage pipeline construction, Governor Egan feared that the state lawsuits would cause further delays and that he would be blamed. During the summer of 1973, Egan had his attorney general, John Havelock, secretly negotiate a tentative out-of-court settlement on the pending lawsuits with the oil companies.[34]

Egan announced the tentative settlement in September 1973 and called for a special session to start in October for lawmakers to consider the legislation needed to implement the settlement. The secret talks had concluded with the oil companies agreeing to more tax revenue for Alaska in exchange for the state backing off its right-of-way leasing requirements. The settlement included a 25-cent-per-barrel minimum oil production tax and a 20-mill statewide property tax on oil and gas equipment.[35]

After almost a month of wrangling, legislators passed a package fairly close to the original settlement proposal, including an increased oil production tax rate and the 20-mill oil and gas property tax. The right-of-way leasing act was gutted; rather than using the state's contract powers to control pipeline costs, the state switched to more conventional regulatory right-of-way leasing provisions. The legislative package satisfied the oil companies' major points of litigation and the lawsuits were settled.[36]

The Middle East oil embargo began in October 1973. On November 16, 1973, President Nixon signed the Trans-Alaska Pipeline Authorization Act, eliminating most of the federal legal challenges to the pipeline. Construction on the massive Trans-Alaska Pipeline System (TAPS) began in March 1975 and was completed in May 1977. The final cost was eight billion dollars.[37]

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During the 1976 legislative session, motivated by rising oil prices and increasing oil company profits on Cook Inlet oil, legislators introduced tax proposals for increasing the state's share of the profits. Governor Jay Hammond requested that the legislature delay any tax changes for a year. He warned that new taxes would reduce the value of a temporary reserves tax on Prudhoe Bay oil and gas – a tax on resources in place – that was enacted in 1975 as a way to bridge the budget gap during pipeline construction.[38]

After many hearings over various tax schemes, legislators went along with Hammond's request and tabled their oil tax legislation. Instead, they opted to fund a study of oil taxation to be considered in the 1977 session.[39]

In February 1977, the Department of Revenue issued a comprehensive report on Alaska's oil and gas tax structure that identified multiple problems with the existing oil and gas production tax. One problem was that the system failed to address varying economic factors for oil fields in different regions of the state. Another was the "economic limit" for fields – the point when costs of production exceed profits. Reaching the economic limit could result in the premature shutdown of a field while oil or gas resources still remained. The state's production tax was seen as contributing to production costs and potentially hastening the time when the economic limit for Alaska's oil fields was reached.[40]

The department report recommended replacing the existing stair-step production tax system with an Economic Limit Factor (ELF) to be used in calculating the amount of tax owed. As the cost of producing oil or gas got closer to its economic limit, application of the ELF would reduce the production tax that was owed. This was seen as an advantage over the stair-step approach because it could be tied to the actual economic condition of a field anywhere in the state and would differentiate between the new high yield North Slope fields and the older, declining Cook Inlet fields.[41]

Governor Hammond introduced oil tax legislation based on the report's recommendations. He described the legislation as being designed to protect the state from the "manipulations of multinational oil corporations and the vagaries of Lower 48 politics," and said it would insure Alaskans received a "fair share" of revenue from oil development. House Speaker Hugh Malone, D-Kenai, predicted the proposal would spark "screams of protest like you've never heard," and that the oil companies were "going to threaten to take their marbles and go." Malone said, "It's going to come down to whether the people of Alaska will listen to scare tactics like that."[42]

Oil companies did oppose the new tax proposal. A Standard Oil of Ohio spokesman testified that Alaska might already be taxing the oil industry to the point where there was a disincentive for future exploration and production. Atlantic Richfield Co. (ARCO) argued that increased taxes were unnecessary in light of projected state surpluses of billions of dollars. The spokesman acknowledged that ARCO could absorb the taxes and still show a profit, but said the legislation was "neither necessary nor warranted." A lobbyist for Standard complained that legislators kept saying they were giving the companies something, but the only thing he saw was that they were "getting the shaft."[43]

The House largely supported the governor's package while half the Senate pushed for a lower state take. Referencing the ten Senate members opposing the governor's tax proposal, Rep. Malone opined that, "The people here in the Senate are buying the oil company line. They haven't acquainted themselves with the facts because the facts don't support them. We see an undue influence by the oil industry in the Senate." Harkening back to the past, Rep. Charlie Parr, D-Fairbanks, said that for too long the state had been treated like a colony by outsiders clamoring for resources, concluding, "I for one don't intend for Alaska to be exploited any longer."[44]

With compromises made by both sides, the 1977 legislature passed a major overhaul of the state's oil and gas production tax that incorporated the proposed economic limit factor. Application of the ELF formula would lower or raise the effective tax rate up to a maximum of 12.25 percent depending on a field's per-well productivity. The new system was designed to bring the state additional revenue from high production fields, and to serve as an incentive to encourage production in marginal and declining fields by reducing the tax as production declined.[45]

The first flow of oil through the Trans-Alaska Pipeline System reached the Valdez Marine Terminal on July 28, 1977. By 1981, North Slope production was around 600,000 barrels per day on its way to peak production of two million barrels per day in 1989.

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In the late 1970s, the corporate income tax – a tax on a company's profits – became a point of contention between the state legislature and oil and gas companies. The formula apportionment method that assigned a percentage of a company's worldwide income to Alaska failed to account for much of the oil production income that should have been subject to state taxation. In 1978, to better capture value earned in the state, a separate accounting method was enacted where oil and gas companies were taxed on their income earned in Alaska, separate from income earned elsewhere. Atlantic Richfield, Sohio/BP, and Exxon objected and sued the state.

As the lawsuit slowly progressed through the courts, the companies paid the oil and gas corporate income tax under protest. Starting in 1980, Governor Hammond became concerned that if the companies ultimately prevailed in their lawsuit, the state would be on the hook for billions in tax refunds. However, settlement options would have required the state giving up hundreds of millions in revenue. Legislators urged the administration to find solutions that would not require this revenue loss.

In March 1981, Governor Hammond and the legislative leadership opted to stand firm. They issued a joint statement saying, "any significant decreases in State oil and gas revenues appear both unwarranted and unsupported by a majority of Alaskans ... All agree that any changes which would give large sums of money to the oil industry at the expense of the people of Alaska are unacceptable."[46]

During the 1981 legislative session, "backstop" legislation was crafted to protect Alaska in the event the state lost the companies' lawsuit. In June, the House and Senate established a conference committee to settle their differences on the legislation. Meanwhile, the oil companies circulated a settlement proposal to the administration and legislature. A legislative analysis of the proposal concluded it would decrease state revenues by an average of $820 million per year during the remainder of the 1980s.[47]

Before the conference committee concluded its deliberations, the legislative world shifted. In the House, Democrats were in the majority with 22-members. Jim Duncan of Juneau had been elected speaker following a three-week organizational battle; Russ Meekins, an Anchorage Democrat, served as majority leader. On June 12, while his fellow Democrats were in caucus, Meekins took the speaker's chair, convened the floor session with minority Republicans and fellow dissident Democrats, and led a vote to elect a new speaker.

When they heard what was happening, the other Democrats charged into the House chambers, accidentally knocking aside the pages who had been told to block the door. Much yelling and objections ensued, to no avail. The Democrats quickly filed a lawsuit to null the actions taken that day. But in the end, the 16-member Republican caucus, two Libertarians, and five rural Democrats prevailed to form a new majority.

Reasons given for the "coup" included dissatisfaction with the length of the session, conflicting personalities, and inattention by the House leadership to a variety of issues. The main driver though was money; around $4 billion in oil revenue was anticipated for the coming year, almost double from the previous year. As the governor and legislative leadership devised ways to divvy up the oil dollars, some rural Democrats felt excluded from the discussions and worried that their communities were being shortchanged. They joined in the coup hoping that the new leadership would be more responsive to rural Alaska's funding needs.[48]

Though most legislators at the time said they did not believe oil companies were involved in orchestrating the coup, the companies benefited from the change of leadership. Newly elected Speaker Joe Hayes, R-Anchorage, changed the membership of the House conference committee that was considering the backstop income tax legislation. Led by Senator Ed Dankworth, R-Anchorage, the reconstituted committee abandoned the backstop proposal and replaced the separate accounting oil and gas corporate income tax with a modified apportionment method more acceptable to the oil and gas companies.

Governor Hammond signed the modified apportionment legislation into law based on the advice of his attorney general who was concerned about how much the state would have to repay the oil companies if the state lost the lawsuit over separating accounting. Former Senator Chancy Croft, who was instrumental in the passage of separate accounting, is reported to have later stated, "The demise of separate accounting marked the day that Alaska capitulated to the oil industry. That's when the state became a seller rather than a regulator of oil…" He bemoaned the loss of information that separate accounting provided the state, saying, "The state's power to tax is limited, but information can give you a good idea of what the limits are. [Separate accounting] gave the state some basis to form an intelligent policy towards the oil industry, and Alaska lost that."[49]

Also in 1981, the legislature amended the oil and gas production tax in an attempt to compensate the state for lost revenue resulting from the repeal of separate accounting. They passed legislation increasing the production tax rate from 12.25 percent to 15 percent for oil produced after June 30, 1981. Fields commencing commercial production after that date had a tax holiday of sorts with a tax rate of 12.25 percent for the first five years of production, and the 15 percent rate kicking in after five years. The legislation suspended application of the ELF formula on Prudhoe Bay production until 1987. That meant the tax for the next six years of production from the prolific Prudhoe field would be the full applicable tax rate with no downward adjustments.[50]

Even though Alaska oil production levels were steadily increasing, revenue from the oil and gas corporate income tax dropped from $860 million in 1981 to $236 million in 1983. Due to volatile oil prices and transportation costs, oil production tax income increased only around $300 million, from $1.2 billion in 1981 to $1.5 billion in 1983.[51]

In 1985, the Alaska Supreme Court upheld the constitutionality of separate accounting. Multiple efforts to reinstitute separate accounting have been unsuccessful and a modified apportionment method remains in place to this day.

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The coup demonstrated how the influx of oil money created leverage for legislative leaders to influence legislators' behavior, particularly rural Democrats who needed to secure funds for much-needed capital projects in their regions. Alaska's elections started changing as well, with campaign contributions increasingly coming from oil interests.

In the 1984 election, VECO, an Anchorage-based oil field service company owned by Bill Allen, ranked as the top contributor to state legislative races, giving away $109,720 in campaign donations. VECO was later found to have violated state campaign laws with a payroll deduction program that deducted $100 from employees' paychecks for political contributions and passed the funds to candidates selected by company officials. Around nine dollars out of every ten went to Republicans.[52]

As a VECO lobbyist, former Senator Ed Dankworth implemented the payroll deduction plan. Dankworth joined VECO after leaving the legislature under a cloud of controversy. In 1982, he was indicted on two counts of criminal conflict of interest for using his position as Senate Finance co-chair to try to get the state to buy a surplus pipeline camp he owned. He bought the property for $900,000 and then sought a $3 million appropriation for purchase by the state. After a lengthy court battle, the case was dismissed based on legislative immunity.[53]

Dankworth became known for getting industry-friendly legislators elected and having a hand in organizing the Senate. His influence was so pervasive that he was known as the "21st senator." The 1985 legislature saw the placement of Fairbanks Republican Don Bennett as Senate President. Bennett was one of five senators who received campaign contributions through VECO's illegal payroll deduction plan. When Bennett ran for lieutenant governor in 1986, he received over $21,000 from VECO and around $5,000 from other oil interests, far more than any other statewide candidate. Bennett lost that election and resumed his position as senator until his death in August 1987.[54]

Dankworth concentrated VECO's other 1986 election efforts on the Republican dominated Senate; donating $65,150 to fourteen Republicans and just $4,250 to two Democrats. ARCO, a major Prudhoe Bay oil producer, surpassed VECO's donations, making them the number one campaign contributor and VECO number two. Most of the oil money went to Republican candidates. Of forty-three donations ranging from $1,000 to $4,525, ARCO contributed to thirty-three Republicans. An ARCO spokesman explained the company contributed to candidates who were "sound in their fiscal views and pro-development." John Kerrigan, vice president of VECO, said his company was supporting candidates who favored resource development and "a stable tax policy."[55]

Oil industry interest in the 1986 election was spurred by the pending tax break for the Prudhoe Bay oil field – the 1981 suspension of application of the ELF formula to Prudhoe production was scheduled to expire in 1987. Oil companies wanted to ensure that the tax break remained in place and the election offered them an opportunity to get like-minded legislators elected. "We need to flex our political muscle," ARCO president Harold Heinze wrote in an in-house publication. "We're the largest private employer in the state. People know we've got a loaded gun. They don't know yet if it's a blank or silver bullet. They will see the proof in this election."[56]

The biggest beneficiary of oil related campaign contributions was Senator Jan Faiks. An Anchorage Republican and former schoolteacher, Faiks first won election in 1982. Considered friendly to industry, VECO officials and employees contributed $20,100 to her 1986 reelection campaign – almost double the next highest contribution. At the start of the 1987 legislative session, Dankworth helped to install Faiks as President of the Senate, a move that paid off in a big way for the North Slope major oil producers.[57]

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A 1986 legislative report identified several problems with the ELF tax system – among them that once the suspension of the ELF formula to Prudhoe Bay expired in 1987, the system would provide the field with a tax reduction decades before it could be considered marginal. At the time, Prudhoe Bay and the nearby Kuparuk oil field were North America's top two largest oil fields. Application of the ELF to Kuparuk was already reducing the field's oil production tax rate from fifteen percent to six percent, costing the state $58 million in tax revenue. Unless application of the ELF for Prudhoe Bay was delayed or repealed, Alaska would lose hundreds of millions more in oil revenue in the coming years. [58]

In March 1987, the Department of Revenue Commissioner, former legislator Hugh Malone, testified to the legislature that application of the ELF formula to Prudhoe Bay would result in a loss to the state of $80 million the first year, and $100 million per year in following years. The revenue situation was particularly critical for the state due to a sharp decline in oil prices and a potential budget deficit. Concerned about the loss in needed oil revenue, Governor Steve Cowper introduced legislation to continue the ELF suspension on Prudhoe Bay for another five years along with other modifications to assist marginal fields.[59]

The House Democratic majority took up the governor's proposed ELF legislation and passed its version of the bill on April 1, 1987 by a vote of 25 to 15. Senate President Jan Faiks gave the bill five committee referrals, effectively killing it for the session and allowing the ELF formula to begin applying to the highly productive Prudhoe Bay oil field.[60]

In 1988, Governor Cowper and the House Democratic majority tried again to get changes to the ELF, both to address the application of the formula to the Prudhoe Bay field, and to make the tax system more effective for encouraging marginal field development. Senate President Faiks again stymied their efforts. She asserted that the ELF was working, that it was prompting more drilling and creating new jobs, and declared the Senate would not even consider repealing the tax break.[61]

In 1989, the North Slope was at its peak production of two million barrels of oil per day. Yet, with low oil prices, state revenue was declining and a deficit of approximately $213 million was projected.[62]

For the 1989 legislative session, Governor Cowper announced his continuing support for revision to the ELF tax system. Without a change, the administration estimated Alaska would lose more than $1 billion in revenue over the next five years. The House Democratic majority renewed their efforts to modify the ELF. Soon after the start of session, the House Finance committee introduced its own measure to reduce the ELF tax break on the productive North Slope fields and increase the tax advantage for marginal fields.

In supporting the House proposal, Cowper said, "we all own the oil fields on the North Slope and we have granted the companies the right to remove the oil." House Republicans took a different view, saying, "Members of the oil industry have proven to be good corporate citizens in Alaska and a stable tax policy is important to encourage economic development." The Republicans' priority was reducing the state operating budget.[63]

The new Senate President, Senator Tim Kelly, R-Anchorage, said he didn't see any better prospect for getting the tax changes passed than in the past two years. In the 1986 election, Kelly received more than $23,000 in campaign contributions from oil and mining interests, with nearly $12,000 coming from individuals and companies related to VECO.[64]

The House passed the oil tax revisions on March 22, 1989 on a vote of 21 to 19. Senate President Kelly gave the bill three committee referrals. Indications were that the proposal would meet the same fate as past attempts and not even get a hearing.[65]

Then, on March 24, 1989, the Exxon Valdez went aground in Prince William Sound.
As spilled oil spread through the resource-rich waters and public animosity toward the oil industry grew, senate leaders began reconsidering their view on the production tax legislation. Senator Dick Eliason, R-Sitka, a former opponent of the tax changes, introduced a measure nearly identical to the House bill. "Public support (for the oil companies) has dwindled," Eliason said. "A lot of people think we've been betrayed."[66]

The House bill began moving in the Senate. At one point it became something of a bargaining chip. Senate Republicans were pushing a bill to recriminalize marijuana, a measure strongly opposed by House Democrats – it was then legal for adults to possess up to four ounces. Kelly bluntly declared, "Marijuana will be a condition for ELF."[67]

Then it happened. Late on a Sunday night, on May 7, the full Senate held a vote on the House version of the ELF changes. The bill failed on a vote of 9 to 11. There was a call for reconsideration, setting up the bill for another vote the next day. Before the vote, Governor Cowper issued a statement, saying, "The oil companies won Sunday night. It's as simple as that. Monday's final vote on this issue will prove one thing: whether the oil industry runs this state or whether the people of Alaska are in charge." On reconsideration the next day, the bill passed on a vote of 11 to 9.[68]

The revised ELF legislation was signed into law on May 31, 1989. This marked the last significant change to the oil and gas production tax for the next seventeen years.

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In 2003, a legislative research report found that applying the ELF formula from 1995 to 2002, particularly as applied to the North Slope, reduced revenue to the state by approximately $1.7 billion. In addition, the ELF was not encouraging investment in future exploration and development; even with low taxes, the major producers were not significantly reinvesting in Alaska.[69]

In 2004, Democratic legislators introduced legislation to change the ELF so that Alaska would get more in production taxes when oil prices were high, as they were at the time. The idea was not popular with the Republican-led majorities and the bills received scant attention.[70]

Starting in 2005, discussions for a new oil and gas production tax system became an integral part of Governor Frank Murkowski's contract negotiations with the three major North Slope oil and gas producers on a proposed natural gas pipeline project. If built, the pipeline would transport gas from the North Slope to outside markets. To secure their commitment to consider building the gas line, ExxonMobil, BP, and ConocoPhillips wanted the existing ELF oil tax system locked-in through the gas line contract to provide tax certainty and stability through the life of the pipeline project. Though likely unconstitutional, Murkowski offered a contractual term of 20 years of certainty for oil taxation if the production tax system was changed.

In 2006, as part of the continuing gas pipeline negotiations, the Murkowski administration and producers agreed to shift from an oil and gas production tax system based on gross value to a net profits tax. Under the proposed Petroleum Production Tax (PPT), companies could deduct certain operating and capital lease expenditures to determine the amount of profit subject to the tax.

By this time, production from the North Slope oil fields averaged 760,000 barrels per day and was declining at a rate of around six percent per year. Combined with multiple tax credits, the proposed net tax system was designed to encourage the major producers to invest in new technologies that would maintain or increase production in the large legacy fields, and encourage new entrants to invest in new exploration and development that would help maintain production in the future.

In February 2006, the Murkowski administration and producers settled on a 20 percent net profit tax rate and 20 percent tax credit as part of the gas line negotiations. The subsequent legislation became known as the "20/20" proposal.[71]

In committee hearings on the PPT legislation, ExxonMobil, BP, and ConocoPhillips representatives offered reluctant support for the 20/20 proposal. Though they felt that the 20 percent tax rate was too high, they told lawmakers they would support the bill as it represented part of the negotiated agreement on the gas pipeline contract. They said their main interest was a "predictable and durable" tax system that would enable the gas project to move to the next phase.[72]

Both the administration and producers opposed any legislative attempts to change the tax rate, arguing that the 20/20 proposal was essential to getting a gas line and attracting the investment necessary to lead to more production from Alaska's oil fields. The producers and other oil interests ran multiple ads to convince the public that a higher tax rate would discourage investment and do harm to the industry.

Legislators pushed back, with one saying they would not be bullied into a bad deal. Another complained that the rules were being changed; that they had been told the issue was that the current ELF was "broken," and now they were being told that if they increased the proposed tax rate of 20 percent, it would negatively impact negotiations to secure a natural gas pipeline.[73]

In an attempt to find a middle ground, the Senate passed SB 305 with its version of the PPT. The legislation proposed a 22.5 percent tax rate with a 25 percent capital expenditure tax credit and included a progressivity factor triggered when oil prices exceeded $50 per barrel. A progressivity factor increases the tax rate as the net value on a barrel of oil increases, and decreases the rate when oil prices fall; this helps ensure the state benefits commensurate with the producing companies when oil prices are high, and helps producers when oil prices are low.

The administration objected to the 22.5/25 proposal. Governor Murkowski said that the higher tax credit created too much risk for the state, and the higher tax rate would deter companies from making the investment needed to curtail the decline in oil and gas production. The administration's consultant, Dr. Pedro van Meurs, also cautioned against the 25 percent tax credit, pointing out that if there were several years of low oil prices, the credits could pile up so much that the state would not collect any production tax.[74]

On May 6, 2006, the House Finance committee passed out its version of SB 305. The committee bill replaced the Senate's 22.5/25 proposal with the governor's original 20/20 plan. On May 7, the full House began debate on the legislation. What ensued was two days of legislative wrangling over tax rate percentage points, with so many amendments, and amendments to amendments, that sometimes legislators did not know what they were voting on.

The first amendment on the tax rate would have moved the rate from 20 percent to 22.5 percent. The maker of the amendment, Rep. Mike Kelly, R-Fairbanks, joked that he was "getting strong hind legs – I'm learning I get to walk with three lobbyists hanging off each leg." An amendment to the first amendment would have raised the rate to 25 percent. Both failed.[75]

The next amendment was to raise the tax rate to 21.5 percent. To the surprise of many watching the debate, the amendment passed on a vote of 21 to 19. Almost immediately, there was a call for an "at-ease," where legislators are free to converse with each other, leave the floor to confer with whoever may be in the hall outside the House chamber doors, and make or take phone calls. On this particular day, the hall was filled with Murkowski administration staff, senators opposed to a higher tax rate, and oil company lobbyists.

Upon coming back to order, Rep. Pete Kott, R-Eagle River, moved to rescind the prior action adopting the amendment to raise the tax rate to 21.5 percent. The motion passed. The amendment to raise the tax rate was back before the body. This time it failed on a vote of 20 to

20. Speaker John Harris, R-Valdez, and Rep. Bruce Weyhrauch, R-Juneau, changed their votes from yes to no. Rep. Peggy Wilson, R-Wrangell, changed her vote from no to yes.[76]

When another amendment passed to raise the rate to 22.5 percent, the action was again rescinded. And so it went with more amendments, each adjusting the tax rate up or down by just a few percentage points.[77]

The biggest drama occurred when two Democratic minority members offered an amendment to set a minimum tax floor to protect state revenue during times of low oil prices. Majority member Rep. Weyhrauch spoke in support of the amendment and it passed on a vote of 23 to 17. An "at ease" was called. Upon reconvening, Weyhrauch moved to rescind the action to adopt the amendment, angrily declaring that he had learned the proposed minimum tax would hurt small independent operators.[78]

Minority Leader Rep. Ethan Berkowitz, D-Anchorage, then spoke out. He decried the phone calls being taken on the House floor, and the lobbyists in the hallway and in the gallery telling legislators how to vote. He said, "You know Mr. Speaker, you got a telephone call. I walked out into the hallway, surrounded by dozens of lobbyists. All screaming about the great injustice we've done to them ... But this is our floor. Our floor. No telephone call is supposed to change what we're doing. No lobbyist is supposed to peer over the railing and tell us to change our mind. Never should happen ... Our obligation is to the people of the State of Alaska. Our obligation is constitutional and is to get the maximum benefit from our oil, and our gas. That's what we swore an oath to do. We did not swear an oath to increase profitability for companies headquartered in Houston, and London, and elsewhere around the globe. So, others may want to compromise. I say enough."[79]

The House ultimately settled on a 21.5 percent tax rate and 20 percent tax credit with a progressivity provision, a minimum tax floor, and a reduced tax rate for the Cook Inlet region. On a 10 to 10 vote, the Senate failed to concur in the House amendments to SB 305 and the bill died at the conclusion of the regular session on May 9, 2006.

Following the end of the 2006 regular session, the gas line contract negotiated between Governor Murkowski and the producers was revealed. Many legislators found the provisions unacceptable, particularly locking in oil taxes. Ultimately, the legislature failed to approve the contract. However, work continued on the PPT legislation.

The final PPT passed on August 10, 2006 during a third special session. The legislation that became law established a base tax rate of 22.5 percent; a 20 percent tax credit for qualified capital expenditures and carried-forward annual losses; a .25 percent progressivity factor triggered when a taxpayer's net profits exceeded $40 per barrel; a minimum tax of not less than 4 percent of the gross value at the point of production; a small producer credit up to $12 million; a $6 million credit applicable to regions outside Cook Inlet and the North Slope; a transitional investment credit for costs incurred in the five years before the new production tax took effect; and companies producing less than 50,000 barrels per day could qualify for a cash refund of qualified capital expenditures and annual loss credits if they met certain conditions.[80]

The PPT was a fundamental shift in the state's relationship with the oil and gas industry. Either through reduced tax revenue or direct cash payments from the state, Alaska became the single largest indirect investor in new oil and gas projects, sharing in the risks of the companies' investment decisions, though not the actual decision-making.

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During the May 7th debate on SB 305, a large man with an imposing presence took a front row seat in the House gallery. The man was Bill Allen, CEO and founder of VECO. Having the natural gas pipeline contract between the state and oil and gas producers was important to Allen because VECO stood to profit from contracts for pipeline construction activities. Getting the PPT through the legislature with the 20/20 proposal intact was essential to getting the gas line contract finalized and Allen was there to make sure it happened.

As Alaskans later learned, it turned out Allen was not taking any chances in getting a production tax acceptable to the oil companies. Starting in 2005, the FBI secretly recorded conservations between Allen, Representatives Kott, Weyhrauch and Vic Kohring, R-Wasilla, and Rick Smith, VECO's Vice President for Government Relations. Videos later made public showed Allen using his influence and money to enlist the three legislators' support for maintaining the 20/20 PPT proposal, particularly to keep the tax rate at 20 percent.

According to the FBI Kott/Weyhrauch indictment, on January 8, 2006, the day before the start of the legislative session, Kott left Allen a phone message saying, "Things start tomorrow. I just wanted to get what our instructions are." Later conversations that took place throughout the session included discussions about how Allen could provide monetary support to Kott and the tactics Kott was using to influence legislators' votes on the oil tax legislation.[81]

Meanwhile, Rep. Weyhrauch was having his own conversations with Allen. On May 4, 2006, Weyhrauch, a lawyer, offered to provide legal services to VECO. That same day, in a taped conversation, Allen and Smith discussed whether VECO should hire Weyhrauch, and that they believed his job solicitation was connected to whether or not Weyhrauch would support VECO's preferred version of the PPT.

On May 7, Weyhrauch changed his yes vote on raising the tax rate to 21.5 percent to no after Kott's motion to rescind passed and the amendment was back before the body. Recorded conversations between Kott and Allen later that day reveal that Weyhrauch switched his vote after receiving instructions from Kott and Allen to make the change. On May 9, Allen told Smith they would need to give Weyhrauch some contract legal work if the 20 percent PPT bill passed the legislature.

Conversations and meetings between Allen, Smith, Kott, and Weyhrauch continued through the first and second special sessions. At one point, Allen gave Kott $1,000 in cash. Later VECO covered the costs of a poll conducted for Kott's reelection campaign and paid Kott a fraudulently inflated invoice on behalf of Kott's hardwood flooring business. Allen and Smith continued leading Weyrauch to believe they would provide him with contract work in exchange for his support of the 20 percent tax rate.

Kott and Weyhrauch were not the only ones acting on Allen's behalf. In a March 30, 2006 surveillance video, Rep. Kohring begins a conversation with Allen asking for Allen's help dealing with a $17,000 credit card debt. Allen agrees to try to figure out something that won't be linked to him or VECO. This is followed by Allen giving Kohring hundred dollar bills for Kohring to pass on to Kohring's daughter. Kohring accepts each bill with a polite thank you. In the end, he commits to making every effort to keep lobbying his colleagues for the governor's 20/20 plan.[82]

There were senators involved as well. In December 2008, Senator John Cowdery, R-Anchorage, pled guilty to conspiring to bribe another Alaska senator. Cowdery admitted that he and Allen met a state senator on June 25, 2006 at an Anchorage restaurant to offer the other senator $10,000 in campaign contributions. The offer was conditioned on the other senator's support for the PPT legislation as supported by Allen. The senator declined.[83]

Senator Ben Stevens, R-Anchorage, Senate President during the PPT debate, was also implicated. Though not charged with any crime, Stevens was a participant or referenced in recorded conversations with Bill Allen about retaining the 20/20 proposal. During Kohring's trial, Rick Smith testified that $250,000 in consulting fees that VECO paid Stevens was a bribe. And in 2010, the Alaska Dispatch News posted a reenactment of a June 5, 2006 phone call between Stevens and Allen where Allen blatantly recruited Stevens to work for VECO, and Stevens and Allen discussed Allen's hold over Kott and Weyhrauch.[84]

In May 2007, Allen and Smith pled guilty to bribing Alaska lawmakers in exchange for favorable votes. Kott, Kohring, and Weyhrauch pled not guilty to charges of bribery, conspiracy, and extortion. In the fall of 2007, juries found Kott and Kohring guilty. Kott was sentenced to six years in prison and Kohring to three and a half years. In March 2011, their convictions were vacated and the cases remanded for new trials because the prosecution had suppressed information that may have helped their defense. Later that year, they both agreed to plead guilty in exchange for being sentenced to time served and conditions on their release. Also in 2011, federal prosecutors dropped the four felony charges against Weyhrauch in return for his agreement to plead guilty to a single misdemeanor in state court.[85]

Through 2006 and into 2007, oil prices were approaching $90 per barrel. North Slope production was around 740,000 barrels of oil per day and continued to have a six percent annual decline rate.

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The 2006 primary election saw the defeat of Governor Murkowski to a relative newcomer, former Wasilla mayor Sarah Palin. Palin ran on an anti-corruption/anti-corporate platform and won the general election against former governor Tony Knowles. In 2007, Palin initiated a review of the PPT tax structure. The administration found that the cost analysis on which the PPT was based had failed to adequately predict the capital and operating costs the state's oil producers would deduct from their taxes. The higher costs and other factors resulted in an $800 million gap in anticipated revenue.[86]

The cost and revenue disparity, and the corruption scandal, led Governor Palin to introduce Alaska's Clear and Equitable Share Act (ACES). The bill raised the base tax rate from 22.5 percent to 25 percent and maintained the generous tax credits enacted under the PPT. It provided additional incentives to small producers and explorers by creating a fund for oil and gas credit cash purchases and eliminating the $25 million annual cap on cash purchases established by the PPT.[87]

Representatives for the major oil producers all opposed ACES. They generally said that, while they considered the existing PPT tax rate to be too high, making changes to the tax structure would create fiscal instability that would affect their decision-making. The producers contended that ACES would discourage investment in both the legacy fields and exploration and development of new fields. A BP representative summed it up this way: "This is about investment, to stem decline. The barrels are getting harder; technology is needed, more investment is needed. Economics will get worse if the tax increases..."[88]

Smaller independent companies testified in support of leaving the PPT in place and maintaining a stable tax policy. Though they appreciated new provisions that favored new entrants and smaller companies, it was their preference that the PPT be left alone.

The political climate in the October 2007 special session on ACES was far different from the 2006 PPT sessions. In September 2007, Rep. Kott was found guilty of corruption and sentenced to six years in prison. Rep. Kohring's trial was ongoing and grainy black-and-white FBI surveillance videos of VECO's Bill Allen handing him hundred dollar bills were in the news. And Palin, maintaining her anti-corruption and anti-corporate policy, had a 90 percent approval rating.

There was also a change in the Senate. After the 2006 election, Senate President Ben Stevens, along with his ties to VECO, was gone. All nine Democratic senators and six of the eleven Republicans put aside their differences and formed the Senate Bipartisan Working Group. From 2006 through 2012, the Working Group had a moderating influence on legislative decision-making.

ACES passed both the House and Senate with relatively little drama. The final bill increased revenue to the state almost four times more than Governor Palin's original proposal. Among other changes, the bill raised the progressivity factor to capture more revenue for the state at high oil prices. In making the amendment to increase the progressivity factor, Rep. Mike Kelly explained that it was about getting the state value for the product and resources and rebuilding the trust of the people of Alaska.[89]

Oil and gas companies were not pleased with the outcome of ACES, often saying that the progressivity factor took too large a bite out of company profits at high oil prices. From 2007 until 2012, they maintained those objections, except in 2009 when oil prices plummeted and the production tax rate decreased. The state's lower tax helped buffer the companies from losses elsewhere. After 2009, as prices began climbing into the $100 range, oil and gas companies renewed their complaints about ACES.

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In 2009, Lieutenant Governor Sean Parnell succeeded Governor Palin when she resigned in July of that year. Upon taking office, Governor Parnell maintained support for the oil and gas production tax system overall, including the progressivity provision, saying the administration's discussions with oil companies failed to produce evidence that changes were necessary. "I'm not interested in changing progressivity so [the companies] can take that money and invest it somewhere else," Parnell said. "If they're willing to invest it here, I'm open to considering it, but I'm standing up for Alaskans in this, not some other country."[90]

In 2011, following his election in the fall of 2010, Governor Parnell reversed his support for ACES. He soon put forward legislation that proposed changing the tax system in a way that would reduce state revenue at high oil prices. The House Republican majority was amenable to the governor's proposal. House Speaker Mike Chenault, R-Nikiski, said that "a number of us feel and have felt since ACES was passed that it is an unfair tax and that needs to be addressed."[91]

Over the objections of minority Democrats, the House passed a version of the governor's proposal that was estimated to reduce revenue to the state by $5.6 billion for the first five years if there was no new production. If oil production rose five percent from the forecasts, the reduction in revenue to the state would be $4.9 billion over the same period. The Senate Bipartisan Working Group did not take up the legislation passed by the House out of concern the state would lose too much revenue and get too little in return. ACES remained in effect through 2012.[92]

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The start of the 2013 legislative session marked another change in Alaskan politics. The PPT corruption scandal was mostly forgotten. Two sitting senators were actively employed by ConocoPhillips. Governor Parnell also once worked for Conoco. House Speaker Mike Chenault was a former owner of an oil field service company. Several other legislators were married to oil and gas industry employees. Republicans held majorities in both the House and the Senate; the Senate Bipartisan Working Group was no more.

With a legislative majority supportive of his policies, Governor Parnell introduced a new oil and gas production tax bill, SB 21. The legislation proposed a 25 percent flat tax rate, eliminated progressivity, eliminated the 20 percent qualified capital expenditure credit for North Slope projects, amended other credits to be carried forward to when there was production, retained the ACES minimum tax floor, and provided for a gross value reduction that allowed twenty percent of "new oil" to be tax-free indefinitely.

At the time of SB 21's introduction, oil prices were around $90 per barrel. North Slope production was around 534,000 barrels per day and the decline rate continued to average six percent per year. In a new development, Lower 48 oil production was booming with the advent of fracking technology.

The administration's stated impetus for the tax changes was a desire to arrest the decline in oil production and get more oil flowing in the Trans-Alaska Pipeline System. Parnell administration officials felt Alaska was lagging behind other oil states like Texas and North Dakota where new unconventional and shale oil plays were increasing production exponentially. The officials saw Alaska's production tax structure as a barrier to making Alaska more competitive and increasing North Slope oil production, particularly ACES' high progressive tax rate at high oil prices.

The administration was also concerned that the state's investment-based tax credits were costing the state billions and not leading to more production. The state had paid out almost $6 billion in tax credits to date. Almost $1 billion of those credits went to companies that had no production, and no tax liability to apply the credits against. As the state analyzed what it was getting for the $6 billion, they found no direct connection to future production.[93]

The oil and gas companies generally supported SB 21, especially the elimination of the ACES progressivity provision. While supportive of the gross value reduction, major producers were concerned that it applied only to new production. The companies wanted the same or a similar incentive to apply to the old giants Prudhoe Bay and Kuparuk as well. They emphasized that the legacy fields were key to offsetting the North Slope decline in oil production and had the greatest investment opportunities. Large and small companies sought continuing incentives for both new and old fields, and supported extending existing incentives for small producers and exploration activities.[94]

Opponents of SB 21 argued that with the loss of a progressive tax rate, the state stood to lose billions in potential revenue when oil prices were high, as they were at the time; they described the legislation as a "giveaway" both because of the loss of progressivity and because as lower-taxed new oil replaced old oil production, the state's share of the profits would decrease indefinitely into the future. New oil included oil from fields created after 2003. Over time, an increasing percentage of oil would qualify for the new oil tax breaks that would be applied for the life of oil recovery.

During both the House and Senate debates on SB 21, legislators offered multiple amendments in an attempt to address concerns raised by the legislation. All failed, largely along Republican majority/Democratic minority lines.

The final version of SB 21 passed on April 14, 2013. The legislation eliminated the ACES' progressivity provision and the North Slope qualified capital expenditure credits. It included a gross value reduction where twenty to thirty percent of new oil on the North Slope would be tax-free indefinitely. To provide a mildly progressive tax structure, SB 21 added a $5 per barrel credit for new oil in combination with a higher tax rate of 35 percent. This created a sort of reverse progressivity; as oil prices decreased, the tax reduction would increase.

Because it was not practical to apply the gross value reduction to existing fields, SB 21 added a North Slope sliding-scale per barrel credit that applied to production from fields that did not qualify for new oil incentives. For each barrel of oil produced from these fields, the producing companies qualified for a tax reduction ranging from $8 per barrel when the gross value of oil was $80 or less, to $1 per barrel between $140 and $149 gross value, and zero after that. Like the $5 credit, the sliding-scale tax reduction added a progressive element to the tax structure. Application of the reduction meant that the 35 percent tax rate would be reached only at very high oil prices starting around $160 per barrel.

In 2013, public dissatisfaction over the new tax system prompted a citizens' referendum to repeal SB 21 and return to ACES in its entirety. The proponents of the referendum gathered approximately 50,000 signatures from around the state, 20,000 more than required.

Supporters of the referendum argued that SB 21 gave away billions to the oil industry at high oil prices, and that since the generous tax credits did not require instate investment, companies would spend their extra profits elsewhere. They contended that ACES had worked to increase oil industry investment in Alaska. Opponents to the referendum argued that SB 21 was working to increase Alaska investment and would increase state revenue over the long term by increasing production.

The vote yes campaign raised $650,000 in support of their efforts. Though an impressive amount, they were overwhelmed by the $20 million raised by those against the referendum. BP, ExxonMobil and ConocoPhillips contributed a combined $10 million to the Vote No campaign.

Ballot Measure 1 was on the August 19, 2014 primary ballot. The measure failed by a vote of 99,855 (52.7%) against the repeal of SB 21 and 89,608 (47.3%) voting for the repeal.

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The 2014 general election brought yet another notable change to Alaska politics. Bill Walker, a Republican turned Independent, won the governorship with Byron Mallott, a long-time Democrat, running with him as lieutenant governor. Both supported ACES over SB 21. As a lawyer in private practice, Walker had a history of representing community and public interests in litigation against the state and oil and gas companies.

With the defeat of the referendum to repeal SB 21, Governor Walker committed to honoring the public's vote and leaving the oil and gas production tax system intact. This resolve was almost immediately challenged when, in 2015, oil prices dropped from over $100 per barrel to below $40 per barrel. In the face of a $4 billion deficit, the state could no longer afford all the tax credit incentives offered as part of Alaska's oil and gas production tax.

Tax credits were a critical component of the PPT introduced in 2006. The credits were intended to encourage investment in the exploration and development of new, smaller conventional oil fields and development of technically challenged unconventional oil, such as heavy oil, in the old larger fields. Over the years, as oil production on the North Slope declined and Cook Inlet oil and gas exploration stagnated, more incentives were added to the tax structure and existing tax credits increased. High oil prices allowed the addition of new tax credits without consideration of their cumulative impact to the state's production tax revenue, particularly when oil prices were low.

The biggest hit to the state treasury in 2015 was a tax credit purchase program first established in 2006 under the PPT. Because explorers and small producers would not produce enough oil or gas to have much of a tax liability against which to apply their tax credits, the PPT legislation allowed certain tax credits to be transferred and traded on the open market. Since the market was limited to the three major oil producers, independent companies were concerned they would not receive full value for their credits. They asked the legislature to establish a purchase program under the PPT where the state would pay cash for their credits upfront.

Senators at the time were skeptical about the cash purchase idea. Senator Con Bundy, R-Anchorage, said that he "cringed at the thought of the newspaper headlines were the State to write huge checks to the oil and gas industry." The Senate version of the PPT that was transmitted to the House for consideration during the 2006 regular session did not include a cash for credit purchase provision.[95]

During House Finance Committee consideration of the Senate version of the PPT legislation, committee member Rep. Mike Hawker, R-Anchorage, proposed inserting the cash purchase provision into the House Finance version of the bill. Murkowski administration officials cautioned that if oil prices fell, the state would be on the hook not only for decreasing revenues, but also for the purchase of tax credits. The officials urged serious consideration of the possibility that oil prices could fall fast with an equally swift decline in revenue. Rep. Hawker countered that was an unlikely scenario and that he did not think the state exposure would be that great. He emphasized the benefit to those making investments.[96]

The final PPT legislation ended up including a provision for the state to provide for the purchase of certain tax credits. Because legislators and administration officials worried about the potential impact to state revenue should oil prices drop, purchases were limited to companies producing not more than 50,000 barrels of oil per day and there was a $25 million cap per company. In addition, an applicant was required to incur a qualified capital expenditure or be the successful bidder for a state oil and gas lease within 24 months after applying for a transferable tax credit certificate. The purchase payment could not exceed the total of the expenditures or bid.

In 2007, ACES established an oil and gas tax credit fund as a way for the state to purchase qualifying credits more efficiently. The amount of money available to the fund was based on a percentage of production tax revenue. The $25 million cap established under the PPT was repealed because small producers found the cap to be too low. In response to legislators' questions regarding what would happen to the fund if oil prices dropped, an administration official explained that regulations would determine how to allocate payments when there was an insufficient fund balance. He said, "a long period of low prices could lead to insufficient money in the fund after lots of credits have been paid out, and the legislature might choose to not spend the money on credits." He stated that remaining credits not purchased by the state could either be carried forward or transferred to another taxpayer who had sufficient tax liability.[97]

2010 saw a further easing of restrictions on the cash purchase program with the repeal of the investment requirement to qualify for state purchase of credits. Also in 2010, the legislature added new tax credits that could be purchased by the state.

In 2013, an amendment to a fish tax bill allowed for the assignment of purchasable production tax credits to a third-party assignee. This meant companies could use their tax credits as collateral for loans or sell credits to a bank or investment institution; the state would then pay cash directly to the institution holding the credits. Testimony indicates legislators believed the amendment applied only to areas outside the North Slope, and only to gas. However, the language that passed had no limiting language and applied statewide for any activity. That the amendment was offered at 1:00 a.m. three days before the end of the legislative session may account for the confusion.[98]

The estimated amount needed for state purchase of tax credits grew from $180 million in 2009 to $700 million in 2015. As oil prices plummeted, fears of the state writing multi-million dollar checks to oil and gas companies while public services were being cut were realized. The state was receiving less in oil and gas production tax revenue than the amount needed to purchase credits.

In 2015, in response to the budget crisis, Governor Walker vetoed $200 million of the $700 million credit purchase appropriation for fiscal year 2016. For the fiscal year 2017 budget, he vetoed $430 million, leaving the $30 million required by the funding formula for the oil and gas tax credit fund. Under the law, available funds would be allocated among credit purchase applicants.

In 2016, the administration introduced a bill to modify tax credit programs and help ease the pressure on future state budgets. Even stalwart supporters of SB 21 recognized the need for change. The legislation, HB 247, passed the legislature near the end of the 2016 legislative session. HB 247 phased out Cook Inlet tax credits by 2018; halved credits for the region outside Cook Inlet and the North Slope; placed an annual cap on purchasable tax credits up to $70 million; and set time limits on how long new oil would qualify for a gross value reduction.

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In 2017, for the first time in twenty-four years, Democrats were in a leadership role in the House. Three Republicans and two Independents joined seventeen Democrats to form a majority coalition. The Senate remained in Republican control, with a majority of fourteen Republicans plus one Democrat.

The primary aim of the House coalition was to find a way to deal with the state's fiscal crisis, including addressing remaining oil production tax issues, particularly the problem of purchasable tax credits. Around $900 million in tax credit purchase applications were pending with the potential for billions more to accumulate in coming years.

Usually, the governor introduces major oil tax legislation. However, while Governor Walker was open to changes to the oil tax structure, his administration was concentrating its efforts on a fiscal plan. This left it to the legislature to decide what, if any changes to introduce.

The task of developing a bill fell to the House Resources Committee chaired by Reps. Geran Tarr and Andy Josephson, both Anchorage Democrats. Over the protests of Republican minority members, the chairs introduced HB 111 as a House Resources Committee bill on February 8, 2017. Among other things, the bill eliminated state purchase of tax credits.[99]

On April 11, 2017, following weeks of hearings, the House passed a bill that fundamentally restructured the SB 21 production tax structure. Among other things, the final House version of HB 111 eliminated North Slope purchasable annual loss credits; allowed annual losses to carry forward to when there was taxable production; increased publicly available taxpayer information; repealed the sliding scale per barrel credit; lowered the tax rate from 35 percent to 25 percent in conjunction with getting rid of the sliding scale credit; and added a supplemental tax bracket that would increase the tax rate by 15 percent at higher oil prices.

Oil and gas companies universally criticized the legislation. The major producers, ExxonMobil, BP, and ConocoPhillips, argued that the sliding scale per barrel credit was an integral part of the tax system, that SB 21 was working to stimulate investment, and that HB 111 would discourage future exploration and production.[100]

Independent explorers and developers felt they would be particularly hard hit by the loss of cash payments for annual loss credits. Annual losses are lease expenditures that would be deductible against a taxpayer's tax obligation except when the deduction would cause the tax to be less than zero. Generally, under a net profit system, unused deductions are carried forward to when there is taxable production. Unique to Alaska, a percentage of unused deductions could be converted to an annual loss credit and purchased by the state. This allowed small companies to benefit from allowable deductions immediately and not have to wait until they had commercial production. It also put the state in the position of paying for credits accrued on projects that ultimately went bankrupt or came up with a dry hole.

The House's goals for the oil tax revision were to enhance and protect state revenue and move toward a simpler, more self-adjusting tax system. When the Senate took up the House proposal, there was agreement on eliminating the purchasable tax credits. However, the goals announced by Senate Resource chair Cathy Giessel, R-Anchorage, were to minimize changes to the existing tax system as much as possible, and reduce the existing purchasable credit backlog. The final legislation passed by the Senate rejected almost all of the House provisions and concentrated on eliminating purchasable credits and establishing alternate means for companies to recoup value from their existing purchasable tax credits.

The Senate passed their version of HB 111 on May 15, 2017 on a vote of 14 to 5. The session ended two days later without any reconciliation between the House and Senate bill versions. Another attempt failed during a special session that started immediately after the regular session and ended June 16.

Governor Walker called a second special session starting as soon as the first special session ended, this time with a focus on the oil tax legislation. It took a month, but there was finally success near the end of the 30-days allotted for the special session. Though it meant giving up many of their proposed changes to the SB 21 tax system, the House majority agreed to a compromise brokered by Representatives Tarr and Josephson and Senator Giessel.

The final legislation repealed the annual loss credits statewide; limited state payments for purchasable tax credits to credits issued for work performed before July 1, 2017; and allowed taxpayers with outstanding purchasable tax credits to use the credits to satisfy other tax obligations. In place of the annual loss credits, HB 111 allowed companies operating outside Cook Inlet to carry forward 100 percent of their annual losses to when the company has production – the value of the annual loss would decrease in value by 10 percent, starting after the tenth year on non-producing leases and the seventh year on producing leases.

HB 111 left intact the sliding-scale per barrel credit that mainly benefitted the major producers, and the gross value reduction and $5 per barrel credit for qualified new oil. These and other SB 21 provisions remained issues for the House majority. As part of the compromise, provision was made for a legislative working group to analyze and review the state's oil and gas tax structure and develop terms for a comprehensive fiscal regime. The compromise legislation passed with 33 legislators voting yes in the House and 18 yeas in the Senate. It was a breakthrough in a year when state and national politics seemed hopelessly mired in partisan politics.

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In 2019, seventy years after Governor Gruening instituted Alaska's first comprehensive tax system, Alaska is once again on the brink of financial disaster. Like in territorial days, Alaska currently lacks a state income tax. The income tax first instituted in 1949 was repealed in 1980 because of the influx of oil money. Since then, funding for state government services and infrastructure remains largely dependent on revenue from the oil and gas production tax and lease royalties. The result is state budgets as volatile as oil prices.

Though oil prices in 2019 are higher than the big dive in 2015, they remain in the $60 range and the state is taking in less revenue than needed to fund state public services. To close a $1.6 billion deficit and make good on a campaign promise to pay Alaskans full dividends from the Permanent Fund, the state's oil revenue savings account, Alaska's new governor, Michael Dunleavy, proposed massive cuts to public service funding. Were the legislature to adopt Dunleavy's proposed budget, there would be devastating reductions in health care services and public education, several University of Alaska campuses might have to close and the state ferry system could be shut down completely. Rural areas would be hit hardest with even fewer public safety officers, higher energy costs, and an end to local oil and gas property taxes.

Public outcry over the governor's proposed budget includes calls for changes to the state's oil and gas production tax. There remains the belief that the system enacted under the Parnell administration in 2013 has short-changed Alaska. With oil prices remaining low, major oil producers can claim the maximum tax reduction of $8 per barrel produced under the sliding-scale credit for the large legacy fields and pay an effective tax rate at or near the minimum four percent gross value tax. New fields benefit from the gross value reduction and $5 per barrel credit for qualified new oil. Still lacking is quantifiable evidence that tax incentives induce additional oil production from existing fields or new exploration and production.

Purchasable tax credits continue to loom as an issue. As of January 30, 2019, the total of requested tax credits for purchase was around $837 million. In 2018, the legislature approved $100 million in payments. Governor Dunleavy's proposed budget included another $254 million in credit payments to be split between the current fiscal year and the next that begins July 1.

That oil tax reductions remain in place and that the state could pay out hundreds of millions to oil companies or lending institutions while public services are gutted is fueling the ire of many Alaskans. Whether that results in another round of changes to Alaska's oil and gas production tax remains to be seen…

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All of the Northern Alaskan oil development to date, which has included some of the largest resource discoveries in North America, has occurred on state and native lands surrounded by vast expanses of Federal properties.Â As it did a quarter century ago, Northern Alaska today offers the U.S. an opportunity to stabilize or even increase domestic oil supply. Exploiting that opportunity then proved an extraordinarily valuable contribution to enhancing the security of U.S. supply in the past. Given the prospects for future world supply, the value of the opportunity today is as great if not greater than it was then.