AOGA Position Paper: The Oil & Hazardous Substance Release Prevention and Response Fund

The Alaska Oil and Gas Association supports fair and equitable efforts to ensure the State of Alaska is financially prepared in the event of hazardous substance spills. The Oil and Hazardous Substance Release Response Fund, also known as the "470 Fund," is designated for this purpose. To pay for this fund, the state has collected a surcharge only on the oil and gas industry. If an incident occurs, the oil and gas industry also repays costs associated with response, as do some other industries. Still, the oil and gas industry is the only industry that has been assessed a specific surcharge/tax to pay for the purposes of this fund, even though the state utilizes the fund for a variety of other industries and individuals.

AOGA opposes any effort to increase the per-barrel surcharge dedicated to the 470 Fund without the State of Alaska first:

- *Broadening the contributing efforts of all industries that use the fund's services*
- *Implementing additional efficiencies within DEC*
- *Adopting policies to improve cost recovery efforts*

Because this issue is often revisited, we offer the following background information.

History of the 470 Fund

In short, the 470 Fund is a source of revenue that has been utilized for preventing and responding to the release of oil and other hazardous materials across the state.

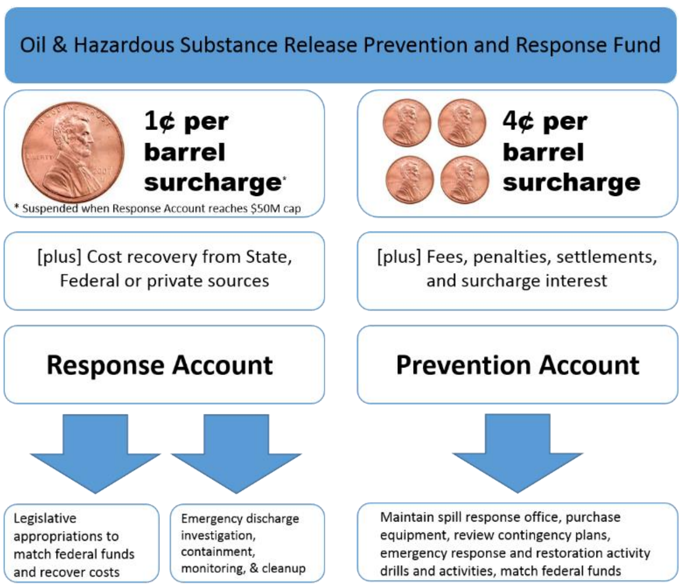
Alaska has had some sort of oil spill cleanup fund in place since 1976, when it was called the Coastal Protection Fund. The rationale for establishing such a fund was the imminent operation of the Trans-Alaska Pipeline System, then under construction. Over time, the Fund morphed into the Oil Spill Mitigation Account, then the Oil Spill Reserve Account, then, in 1986, into the Oil and Hazardous Substance Release Response Fund, or the "470 Fund", a reference to the bill number that created it.

In 1989, after the Exxon Valdez oil spill, lawmakers added a 5 cent per barrel surcharge to fund the account. Legislation also established a $50 million reserve account within the fund to be used for responses to oil and hazardous substance releases. The fund could be used to review oil discharge prevention and contingency plans, conduct drills and training, and verify financial responsibility.

Spill Response Drills, Alaska Clean Seas, 2015

In 1994, the Legislature again made a change, deciding to "split the nickel" by dedicating two cents of the per barrel levy to the new Response Account, and three cents to a Prevention Account. The fund was also renamed the Oil and Hazardous Substance Release Prevention and Response Fund, but is still commonly referred to as the 470 Fund.

In 2006, the Legislature split the nickel again, diverting four cents a barrel into the Prevention fund and one cent a barrel into the Response fund. The current funding mechanism for the state's prevention and response activities has remained unchanged since the 2006 amendments. Graphic A demonstrates how the fund currently operates.



Graphic A – Based on DEC Response Fund Diagram, 2010

What is the function of DEC's Spill Prevention and Response Division (SPAR)?

The stated legislative purpose for the 470 Fund is to ensure that Alaska is prepared for, and capable of responding to, spills of oil and other hazardous materials. Specifically, the fund pays for the Division of Spill Prevention and Response (SPAR) to conduct three main activities: prevention, initial response and contaminated site cleanup. SPAR's prevention efforts include reviewing discharge prevention and contingency plans; conducting training, response drills, inspections, and tests; and, verifying an organization's proof of financial responsibility to clean up spills.

SPAR's response account is used to finance the response to a release or threatened release that poses an imminent and substantial threat to public health or welfare, or to the environment. The response division investigates, evaluates, contains, cleans, monitors and assesses releases, and recovers the cost to the State of Alaska when the response account is used.

SPAR is also brought in to assist the cleanup process planning and mitigation of contaminated sites. These sites may be schools, tank farms, parks or any other site where contamination has gone underground and affected groundwater and soil. This is generally a lengthy and complex process, including monitoring existing sites to verify they are not spreading, working with responsible parties to clean up contamination, and partnering with potential buyers to encourage reuse and redevelopment.

Why is the per barrel surcharge being revisited now?

As oil production has declined over the years, so has revenue resulting from the per barrel surcharge. Simply put, fewer barrels equals less revenue. In fact, according to the Alaska Department of Environmental Conservation, the fund is predicted to run a deficit by the end of FY15. DEC is projecting a $1.9 million shortfall in FY16, assuming the receipt of a $5 million settlement. Current projections show DEC will face an approximate $7 million shortfall in FY17 (Source: DEC Prevention Account Revenues, Expenditures, and Balance Projection, 12/22/14).

AOGA's history with the 470 Fund

AOGA has been engaged in the policy decisions surrounding the 470 Fund since its inception in 1989. In 1994, AOGA supported the legislation that split the initial surcharge into two separate accounts, one for response and one for prevention. AOGA did not oppose the modification to the surcharge in 2006 because the total taxable amount remained at 5 cents per barrel.

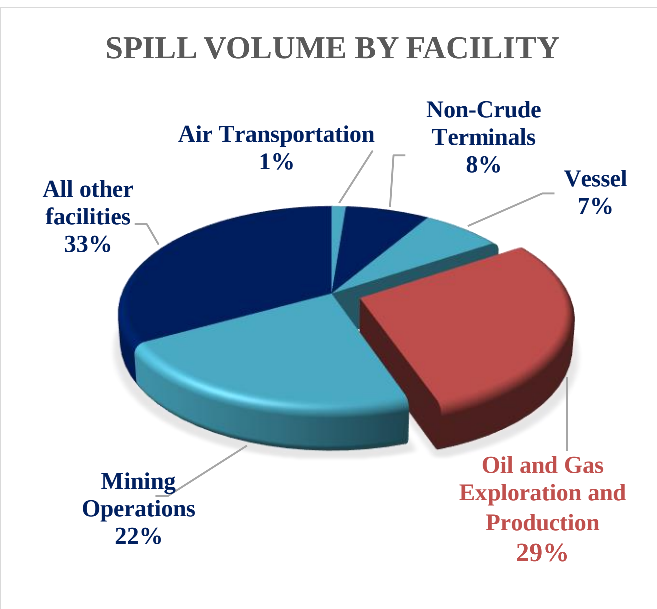
How has the fund been used?

This is an important question given that only the oil and gas industry pays a dedicated tax to the 470 Fund.

Despite the stated purpose of cleaning up and preventing spills, the fund has historically been appropriated to non-spill projects such as campgrounds, state airports, tank farm remediation, privately owned greenhouses and new ferries. According to DEC, these types of expenditures are no longer being made, but the corpus of the fund may have been unnecessarily reduced during years when these types of appropriations were authorized.

More importantly, withdrawals from the fund are made mostly on behalf of non-oil and gas industries.

Although oil and gas production accounted for 100 percent of the fund's dedicated funding, the DEC annual reports show that, over the last five years, oil production and exploration and natural gas production altogether amount to less than 29% of total spill volume. (Source: Annual Summary of Oil and Hazardous Substance Releases, FY10- FY14). Mining operations accounted for approximately 22% of spills, followed by vessels, air transportation, maintenance yard/shops, canneries, gas stations, non-crude terminals and a variety of other facilities.



Source: Annual Summary of Oil and Hazardous Substance Spills, FY10-FY14

In FY12, the area of Alaska with the greatest volume of discharge was Bristol Bay, an area with no oil and gas activity. (Source: DEC, Annual Summary of Oil & Hazardous Substance Spills, October 2012). In that same year, of the Top 10 Releases reported by DEC, only three were related to oil and gas industry activity. The others included tank farms, ocean vessels, seafood plant spills, and an antifreeze spill at the University of Alaska Fairbanks.

DEC's FY14 total budget was $23.8 million. Of that, $5.3 million went to spill prevention and preparedness, and $6.7 million was dedicated to the response program. A large portion was dedicated to mitigation efforts for contaminated sites which, DEC has stated, are not related to the oil and gas industry. Federal funding accounts for approximately two-thirds ($5 million) of the $8.5 million a year contaminated sites budget, however DEC relies on revenue from the response account, funded solely by the oil and gas industry, to cover the difference. (Source: 2013-2014 Biennial Report on the Oil & Hazardous Substance Release Prevention & Response Fund).

Why does AOGA oppose a per barrel surcharge increase?

Since 1989, the oil and gas industry has contributed more than $350 million to the 470 Fund.

Everyone should pay their fair share. If policy makers decide to increase funding for the 470 Fund, revenues should be collected from all parties that utilize the functions of the SPAR Division. It does not make sense, nor is it just, to place the sole burden of maintaining or increasing funding to an account on a single industry when that industry is a minority utilizer of the funds.

In short, AOGA endorses the same position as the Oil and Gas Transition Team for the Walker/Mallott administration, which advocated for the State to utilize other revenue sources before increasing the surcharge on the oil and gas industry. This would then be a true "user pays" model and become a funding formula that recognizes all users of the fund.

Additionally, AOGA advocates for SPAR to continue to identify efficiencies internally and for the State to adopt other policies to assist the state in recovering costs from other users who are not currently reimbursing the State after a response.

Industry is prepared for a spill. The oil and gas industry is prepared with robust response capabilities in the event an industry-related spill occurs. Companies that engage in or intend to undertake oil and gas exploration, development, production, or pipeline transport activities are required by federal and state regulations to have current contingency plans in place, have spill response equipment available and exercise both plan and equipment regularly. The annual cost for each operator to purchase and maintain equipment and carry out oil spill response drills ranges from $1.8-8 million annually.

In addition, oil and gas companies belong to not-for-profit spill response cooperatives, such as Cook Inlet Spill Prevention and Response, Inc. (CISPRI) and Alaska Clean Seas (ACS). These are full-response organizations that provide the personnel, material, equipment, and training to members for responding to oil spill. Membership fees start at $500,000 for producers, and $100,000 for non-producers, with a $20,000-50,000 annual fee. Daily exercise or development fees range from $1,250-2,500.

Spill Response Equipment, Alaska Clean Seas, 2015

In the event that SPAR responds to an oil industry spill, DEC almost always recovers the full cost of the response. The same cannot be said for all facilities. In FY14, SPAR billed more than $3 million to various industries and recovered one-third of that amount. To strengthen the State of Alaska's oil spill preparedness and response, there must be an effort to recover more than 30 percent of the state's spending.

Taxes deter investment. Unilaterally raising taxes on one industry to offset problems associated with declining production is ill-advised. Since oil tax reform passed, Alaska's opportunity to realize more oil production is closer than ever before. The Alaska Department of Revenue now predicts increased oil production in the near-term, which could decrease the 470 Fund's liability in the next few years. (Source: 2014 Fall Revenue Sources Book). In the long term, the most fair and comprehensive solution for increasing revenue to the fund is to establish a funding model that taps into all of the various industries that use it. It also stands to reason that once an industry is compelled to pay a dedicated tax into the fund, that industry would then have additional incentive not to release hazardous substances, lest the fund's principal be reduced.

"AOGA realizes the State of Alaska must be prudent and prepare for hazardous spills of all kinds," says AOGA President and CEO Kara Moriarty. "With that in mind, policymakers should ask all industries that use the fund to share the burden of paying into it, and should look for operating efficiencies within DEC that could reduce costs. Lastly, prioritizing cost recovery efforts to collect funds that are already owed to the State is another common sense solution worth pursuing."

OIL & GAS: FUELING ALASKA'S ECONOMY

AOGA
Alaska Oil and Gas Association

The Alaska Oil and Gas Association (AOGA) is professional trade association whose mission is to foster the long-term viability of the oil and gas industry for the benefit of all Alaskans.