



Oil and Hazardous Substance Release Response Fund Report

The purpose, background, structure and administration of Alaska's Response Fund

**Fiscal Years
1995 to 2005**



MAY 2007

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administration of Alaska's Response Fund***

Fiscal Years 1995 to 2005

Alaska Department of Environmental Conservation,
Division of Spill Prevention and Response, Contaminated Sites Program

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SUMMARY

This report provides an overview of the purpose, background, structure and administration of the State of Alaska's Oil and Hazardous Substance Release Prevention and Response Fund (OHSRPRF) commonly known as the "Response Fund." Included in the Response Fund are a Response Account and a Prevention Account. The report also includes an analysis of the revenue and appropriations for each of these accounts.

The Fund's Prevention Account is used to pay the expenses of the State's spill prevention and response programs. The Response Account, which maintains a balance of \$50 million, is available for response to a release of oil or a hazardous substance that poses an imminent and substantial threat to the public health or welfare or to the environment. It can also be used when a release is declared a disaster emergency.

The precursor to today's Response Fund was the Coastal Protection Fund, first created in 1976, five years after the Department of Environmental Conservation came into being. The Fund has been changed and renamed several times by the Alaska Legislature. This report documents the evolution of the original Coastal Protection Fund to the current Oil and Hazardous Substance Release Prevention and Response Fund.

There have been several milestones during this evolution:

- In 1976 the "Tanker Safety Law" passed, establishing the Coastal Protection Fund for spill cleanup and imposing the payment of annual risk charges on oil shipping companies, determined by the safety features of their oil tankers.
- An Oil Spill Mitigation Account was established in 1977 to collect civil penalties for discharges of oil. The funds could be used to restore and enhance environments affected by oil pollution.
- In 1980 the Oil Spill Reserve Account replaced the Coastal Protection Fund after a U.S. Supreme Court decision in 1978 invalidated the Fund, declaring it pre-empted by the federal Ports and Waterways Safety Act, which precluded the collection of risk charges from oil companies. The Oil Spill Reserve Account maintained a cleanup fund through General Fund capital appropriation, and it also received deposits of costs recovered from responsible parties or from the federal government.
- In 1986 the Oil and Hazardous Substance Release Response Fund replaced the Oil Spill Reserve Account. This action broadened allowable uses to include cleanup of hazardous substance spills.
- In the wake of the *Exxon Valdez* disaster in 1989, the Alaska Legislature passed a number of bills increasing the funding sources and uses of the Response Fund. Most significant was a bill to levy a five-cent-per-barrel oil production severance tax, known as the "conservation surcharge." Legislation also established a \$50 million reserve account within the Fund to be used

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for responses to oil and hazardous substance releases. The Fund's monies could also be used to review oil discharge prevention and contingency plans, conduct drills and training, and verify financial responsibility.

- 1994 legislation divided the Response Fund into two accounts, and split the "nickel a barrel" surcharge. Two cents would go to the new Response Account and three cents to a Prevention Account. The Fund was renamed the Oil and Hazardous Substance Release Prevention and Response Fund.

In this report, financial data for the Response and Prevention accounts begins with Fiscal Year (FY) 95, starting July 1, 1994, and ends June 30, 2005. FY 95 was the first state fiscal year after the Alaska Legislature made significant changes in 1994 through Senate Bill 215.

The Response Fund has remained unchanged since the 1994 amendments, except for revising the annual reporting requirement to a biennial report.

The 1994 changes, which established both accounts and divided the five-cent conservation surcharge between the accounts, effectively reduced operating revenue for state spill prevention and response programs by 40%.

This reduction meant that the operational funding for the Division of Spill Prevention and Response would no longer be sustainable.

I. FUND OVERVIEW

A. Purpose of the Fund

The Legislature established the Response Fund to pay for the cost of responding to a release or threatened release of oil or hazardous substances and to pay the expenses of establishing and maintaining spill prevention and response programs that would mitigate oil and hazardous substance spills.



In 1976, a year before the startup of the Trans-Alaska pipeline, the state established its first fund for oil spill response, the Coastal Protection Fund.



Alaska law requires the oil industry to conduct periodic drills to demonstrate readiness to respond to a spill. The above 2004 drill in Valdez included tabletop exercises and tested equipment to use dispersants.



The Response Fund in part pays for DEC review of spill contingency plans. These plans were not required of railroads in 1999 when an Alaska Railroad freight train derailed, spilling about 120,000 gallons of jet fuel. After 2000, railroads, cruise ships, and similar carriers of fuel were brought under the oil spill safety net.



Response Action Contractors are registered and approved by DEC. The contractors hire spill response workers like this one at the *Kuroshima* spill, Dutch Harbor, 1997.

B. Background and Legislative History

In 1968, Atlantic Richfield completed its discovery well in the Prudhoe Bay oil field and Alaska was forever changed. By 1969, three major oil companies had applied to build a forty-eight inch pipeline to transport the newly found oil to an ice-free port in Southcentral Alaska. Also, in 1969 the National Environmental Policy Act (NEPA) became law. The U.S. Environmental Protection Agency was created in 1970, bringing a national policy and focus on environmental issues, including oil transportation.

The Trans-Alaska Pipeline generated more concern over the environment than any other single project in a time when the importance of environmental review was emerging with the advent of complex Environmental Impact Statements (EIS). Environmental issues became intertwined with Alaska's economic and social future.

Governmental approval of the pipeline was a long time coming. Preliminary stipulations for construction were issued, followed by an EIS. Passage of the Alaska Native Claims Settlement Act in 1971 removed one legal hurdle, and objections over the EIS were settled not by the courts but by the U.S. Congress, with passage of the Trans-Alaska Pipeline Act in 1973.

In 1971, through passage of Senate Bill 75, Governor William Egan elevated the responsibility for protecting Alaska's natural environment from a program within the Department of Health and Social Services to a new Department of Environmental Conservation. SB 75 also prohibited oil pollution and discharges of oil contaminated ballast water. It established pollution penalties, restoration damages, criminal violations, and enforcement authorities. In part, this significant change in state government was made in recognition of changes taking place in Alaska's economy and environmental issues associated with the production of North Slope crude oil, construction of the Trans-Alaska Pipeline System, and tanker transportation through Prince William Sound.

The department's prevention and response programs for oil and hazardous substances were first funded by water quality and coastal zone management programs and carried out under the federal Clean Water Act program. In the early years, the Alaska Legislature provided funding for the state's oversight of the oil and gas industry from the general fund.

Significant Response Fund Events

- 1968 Atlantic Richfield discovers oil in the Prudhoe Bay field.
- 1969 Three oil companies apply to build Trans-Alaska Pipeline.
- 1971 DEC created, with oil pollution statutes.
- 1976 Alaska enacts the "Tanker Safety Law" with the Coastal Protection Fund.
- 1977 June 22, operation of the trans-Alaska pipeline begins.

Oil Spill Mitigation Account established to hold penalties paid to the state.



- 1978 Federal courts strike down the Coastal Protection Fund and tanker risk charges.
- 1980 Oil Spill Reserve Account established, replacing Coastal Protection Fund for spill cleanup.

Preparedness requirements expanded to include offshore facilities and oil barges.
- 1985 Abandoned barrels found at Nikiski highlight need for hazardous substance spill response.

(Continued next page)

(Significant Response Fund Events, Continued)

- 1986 Legislation creates the Oil and Hazardous Substance Release Response Fund, making funds available for contaminated sites cleanup.
- 1987 CERCLA funds used to begin contaminated sites cleanup program. Other federal funding soon came for Department of Defense sites cleanup and leaking underground fuel storage tanks.
- 1989 March 24, grounding of the *Exxon-Valdez*.
- 1990 Legislature expands sources and uses of Response Fund, enacting a five-cent per barrel surcharge on oil produced.
- Storage Tank Assistance Fund established to help owners/operators of underground storage tanks meet a federal deadline for spill prevention measures or tank closure by 1998.
- 1991 DEC signs Memorandum of Agreement with Department of Defense for cooperative cleanup efforts for current and former military activities.
- 1993 Audit of DEC's policy issues concerning the Response Fund. Conducted by Legislative Budget and Audit while Fund changes were being considered.
- 1994 SB 215 divides Response Fund into two accounts: Response and Prevention. The five-cent surcharge is split, with three cents per barrel going to the Prevention Account, and the two-cent surcharge going to the Response account.
- SB 215 also renames the fund as the "Oil and Hazardous Substance Release Prevention and Response Fund."
- A second legislative audit conducted of accounting procedures and use of the Fund by other state agencies.

Coastal Protection Fund – 1976

In 1976, the Alaska Legislature passed Senate Bill 406, the "Tanker Safety Law," requiring large oil terminals and tank vessels operating in the state to provide DEC with adequate spill contingency plans and proof of financial responsibility to compensate for damages in the event of a spill. The law also established the Coastal Protection Fund, to be used for oil spill cleanup and fueled by an annual risk charge imposed on oil shipping companies. The charge was to be determined by the degree of spill risk posed by their equipment and operations, based on the safety design features of their oil tankers. The annual risk charge provisions were challenged and ultimately struck down in 1978.

The first challenge was brought by five oil companies in *Chevron U.S.A. v. Hammond*, and the U.S. District Court in 1978 found the Fund to be preempted by the federal Ports and Waterways Safety Act.¹ Prior to the District Court decision, the 1978 United States Supreme Court decision in *Ray v. Atlantic Richfield Co.* found parts of Washington state's tanker laws as preempted by federal law. The Coastal Protection Fund was also found to be invalid under the dedicated fund prohibition in the Alaska Constitution because the risk charges collected by the state were dedicated to the fund. The provisions for contingency plans and proof of financial responsibility were left intact.

Oil Spill Mitigation Account – 1977

Before these decisions were made, the Oil Spill Mitigation Account was established in 1977 to serve as a repository for civil penalties paid to the state for oil discharges. The paragraph, located in the section entitled, "Civil penalties for discharge of oil," provides that "penalties received by the state under this section shall be deposited in the General Fund and credited to a special account called the 'oil spill mitigation account.'" It allowed the legislature to annually appropriate money from the oil spill mitigation account in a sum equivalent to the amount of these penalties received for the calendar year preceding the legislative session in which the appropriation is made. The appropriated funds were to be used to restore and enhance environments affected by oil pollution, including aquaculture projects.

¹ *Chevron U.S.A. v. Hammond*, 1978 AMC 1697 (U.S. Dist. of Alaska).

Oil Spill Reserve Account – 1980

In response to the *Chevron v. Hammond* decision, the Alaska Legislature passed House Bill 205 in 1980 to replace the Coastal Protection Fund with an **Oil Spill Reserve Account**. HB 205 corrected the defects of the law creating the Coastal Protection Fund and maintained the legal integrity of the state’s program. The law recommended a cleanup fund be maintained through General Fund capital appropriations. The fiscal note for HB 205 stated that “It is recommended that the cleanup reserve be maintained by capital appropriation at the \$1 million level ... balance of the reserve should carry over from year to year ... costs recovered from spillers or from federal funds will be deposited in the General Fund...”² That same year the Legislature enacted a comprehensive re-write of the Alaska oil pollution statutes in AS 46.04. This 1980 legislation expanded the contingency plan and financial responsibility requirements to offshore exploration and production facilities, and oil barges.

The “470 Fund” – 1986

In 1985 DEC discovered high levels of trichloroethane released from 100 barrels abandoned near the Kenai Spur Highway at Nikiski. Legislation in 1986 replaced the Oil Spill Reserve Account with the **Oil and Hazardous Substance Release Response Fund** (OHSRRF, commonly known as the “470 Fund” after its enacting legislation, House Bill 470). This legislation made significant changes to the previous account by authorizing DEC to use the Fund for response to unpermitted releases of hazardous substances (i.e., hazardous waste sites). It also paved the way for the beginning of the state’s program to address historic contamination caused by oil and hazardous substances.

In 1987, EPA provided funding to Alaska through the federal Comprehensive Environmental Response Compensation and Liability Act (CERCLA) that allowed DEC to establish a permanent contaminated sites cleanup program. The fledgling program continued to mature with the addition of the Defense Environmental Restoration program in the late 1980s to address contaminated military sites, and the federal leaking underground storage tank program. Even though DEC’s contaminated sites program was funded by federal grants and general funds initially, Response Funds would be used in later years to help pay the state’s contribution.

Five-cent-per-barrel Surcharge, \$50 Million Reserve – 1989

After the *Exxon Valdez* oil spill disaster in March of 1989, the Alaska Legislature passed numerous bills concerning oil and hazardous substances and expanded both the sources of revenue for the Response Fund and the permissible uses of the Fund (See Table 2 for a summary of oil spill legislation.). Specifically, in Senate Bill 260 in 1989, the Legislature enacted a five-cent per barrel oil production severance tax known as the “conservation surcharge” to provide an independent state containment and cleanup capability for oil and hazardous substance releases of a magnitude that presents a grave and substantial threat to the economy and environment of the state. SB 260 provided the funding mechanism to establish and maintain a \$50 million reserve for responses to spills. The Fund prior to passage of the bill had not held much more than one million.

² SCS CSHB 205, 1980 (approved by the Governor: June 27, 1980)

House Bill 567 was enacted in 1990 to strengthen DEC's authority to require compliance with oil discharge contingency plans. Of particular significance was the requirement that contingency plan holders maintain sufficient resources to contain and remove, within the shortest possible time, a realistic maximum oil discharge.³ HB 567 required industry contingency plans to include prevention measures and added certification requirements for approved contingency plans. This legislation also clarified proof of financial responsibility, liability limits for tank vessels and oil barge operations, and DEC inspections of regulated industries. HB 567 established DEC participation in structural integrity of vessels, barges, pipelines, and facilities and expanded uses of the Response Fund to include:

- Review of oil discharge prevention and contingency plans.
- Training, response exercises, inspections and tests to verify inventories and ability of state, municipal, or parties required to have approved contingency plans.
- Verification of financial responsibility.

Also in 1990, House Bill 566 became law, mandating an "incident command system" requiring spill response to be directed cooperatively by the spiller, DEC and the appropriate federal agency. It also established the State Emergency Response Commission (SERC) in statute under DEC. The new commission had responsibility for establishing Local Emergency Planning Committees and for coordination, planning and oversight of local community contingency plans and other tasks related to oil and hazardous substance response planning. The law established response corps of trained volunteers and response depots of pre-staged equipment for oil and hazardous substance releases. Responsibility for these local resources was placed within the Department of Military and Veterans Affairs.

That same year the Legislature passed House Bill 220 to provide a proactive technical and educational assistance program to help owners and operators of underground storage tanks (UST) meet changing federal requirements. In 1984, amendments had been made to the federal Resource Conservation and Recovery Act (RCRA) to regulate certain underground storage tanks (primarily at gas stations) containing petroleum and hazardous substances. EPA established requirements for spill protection tank upgrades and closures with a 1998 deadline for compliance. HB 220 set up the Storage Tank Assistance Fund (STAF) to provide grants and loans to underground storage tank (UST) owners and operators for assessments, containment, corrective actions, and cleanup costs. HB 220 also included funding to cover the costs of administering the STAF and the tank cleanup loan program, including the costs of a Board of Storage Tank Assistance. In 2002, Senate Bill 153 placed an end date on the grant program of June 30, 2004, and created a revolving loan fund for UST cleanups. From 1991 through 2005, \$43.1 million of Response Funds were appropriated to the UST grant/revolving loan program to fund this work.

In July 1991, the Department of Environmental Conservation established the Spill Prevention and Response (SPAR) Division in order to streamline and focus state responsibility and authority for developing and managing the state's oil and hazardous substance release prevention and response programs.

Many stakeholders of the Fund have been monitoring its use since the surcharge on each taxable barrel of oil produced in the state went into effect. During the early-to-mid 1990s, some objected to the expanded use of the Fund and direct appropriations for specific projects because they were not consistent

³ Governor Steve Cowper letter of February 21, 1990 to Speaker of the House.

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with statutory intent. Others were concerned that these expanded uses would jeopardize the Fund's future ability to provide readily available funding to adequately protect public health and welfare and the environment from the release or threatened release of oil or a hazardous substance.

Oil and Hazardous Substance Release Prevention and Response Fund - 1994

In 1993, SB 215 was introduced by the Legislature to remove certain uses of the Response Fund, restrict the types of cleanups that the Response Fund could be used for, divide the Fund into two accounts, and divide the five-cent per barrel conservation surcharge between the two accounts.⁴ The original proposal for the so-called "split-of-the-nickel" was for three cents of the surcharge being deposited into a Response Account and two cents being deposited into a Prevention Account. Governor Walter Hickel's administration and the Department of Environmental Conservation opposed these changes in the Fund because it failed to provide for a ready source of cleanup funds for all types of spills and failed to provide adequate ongoing funding for core spill prevention and response activities.⁵

Eventually, SB 215 was amended to:

- (1) Allow cleanup of all types of oil and hazardous substance spills from both the Response and Prevention Accounts,
- (2) Provide funding of ongoing prevention and response activities through the Prevention Account funded by a three-cent per barrel conservation surcharge, and
- (3) Create a \$50 million Response Account funded by a two-cent per barrel conservation surcharge.

This split of the nickel essentially reduced available funding to operate spill prevention and response programs by 40%. The Legislature also divided the existing balance of the Response Fund (\$42,081,378) as well as the balance of the five-cent Surcharge Account between the Prevention and Response Accounts (see Table 1).

The Department had misgivings about the ability to maintain the Prevention Account as a long-term, viable funding source, given the Department of Revenue's estimates of the decline in the volume of oil production and the termination of the Exxon Valdez cost recovery settlement payments due to end in Fiscal Year (FY) 2003. In particular, the Department was concerned that the allowable uses of the Prevention Account were increased in the final House version of SB 215 by allowing funding for the Underground Storage Tank Assistance Fund to come from the Prevention Account.

The final version of SB 215 renamed the Response Fund to the "Oil and Hazardous Substance Release Prevention and Response Fund" (OHSRPRF) and provided for use of both the Response and Prevention Accounts for oil and hazardous substance cleanups. Use of the Response Account for spill cleanup without a legislative appropriation is authorized by AS 46.08.045. As was the case under prior law, if a release or threatened release poses an imminent and substantial threat to public health, or welfare, or the environment, DEC can access the Response Account. SB 215 required that when DEC accessed the

⁴ SB 215, Senator Miller introduced May 8, 1993.

⁵ Letter from Commissioner John Sandor to Sen. Mike Miller and Rep. Bill Williams, dated January 19, 1994; March 2, 1994, Testimony of Commissioner Sandor before the House Resource Committee Hearing on CS HB 238(RES); Letter to Sen. Drue Pearce and Sen. Steve Frank, Co-Chairs of Sen. Finance Committee from Bob Poe, Director of DEC's Division of Administrative Services, dated March 24, 1994.

Response Account, it must provide notification to the governor and the Legislative Budget and Audit Committee of the use of those funds. The Response Account can also be used for cleanup activities if the governor declares a disaster emergency under AS 26.23.020(c).

SB 215 became law without Governor Hickel's signature on October 2, 1994. Although Governor Hickel supported the so-called "3-2 split concept," he was concerned about two aspects of SB 215: (1) it allowed use of the prevention account for upgrading above-ground storage tanks without identifying other funding

alternatives, such as the private sector and federal government, and (2) it cast doubt on the state's ability to restore and enhance the environment in the aftermath of a spill.⁶

The changes effectively reduced the operating revenue for spill prevention and response programs by 40%. This reduction ensured that operational funds for the Division of Spill Prevention and Response would not be sustainable.

Also during the 1994 Session, the Alaska Legislature formalized the Alaska State Emergency Response Commission (SERC) as an "all hazards" Commission and transferred it from DEC to the Department of Military and Veterans' Affairs (DMVA) in Senate Bill 33. It also vested responsibility in DMVA to oversee the performance of local emergency planning committees (LEPCs) and to designate local emergency planning districts. The SERC and LEPC support staff were transferred from DEC to DMVA. Up to this point, the SERC and LEPCs had been under the purview of DEC, with funding provided from the Response Fund. SB 33 authorized DMVA's use of the Response Fund to pay for activities that were authorized uses of the Fund. SB 215, however, limited the amount of funds for LEPCs to not more than 3% of the estimated annual balance of the Prevention Account.

Table 2, page 9, is a chronological listing of significant legislation that has affected the Response Fund and state programs for prevention and response to oil and hazardous substance releases.

The Legislative Budget and Audit Division conducted two audits of the Response Fund during the 1993 and 1994 legislative sessions while SB 215 was under consideration. The objective of the 1993 audit⁷ was to review Department of Environmental Conservation policy issues relating to the Response Fund. The audit report noted concerns expressed by the oil industry that language in SB 260 (1989), which

**Table 1: Splitting of the Response Fund
~ Two accounts created in 1994 ~**

The net results of the passage of SB 215 and the initial funding of the two accounts effective during Fiscal Year 1995 were:

Prevention Account

\$ 5,000,000 from the Response Fund balance
\$15,540,000 from the Surcharge Account
 \$20,540,000 Total

Response Account

\$37,081,378 from the Response Fund balance
\$10,360,000 from the Surcharge Account
 \$47,441,378 Total

⁶ Senate Journal Text for SB 215 in the 18th Legislature, dated 07-15-1994.

⁷ January 10, 1994 Audit (Audit Control Number 18-4463-94)

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established the five-cent-per-barrel surcharge, indicated that the purpose of the surcharge was to have an independent spill containment capability in the event of *future discharges* (emphasis added). The audit ultimately determined that Alaska Statutes 46.08.040, “Purposes of the Fund”, is the overriding authority, and therefore, using the Fund for cleanup of historical contamination was appropriate. The audit also noted that although these uses were legal under the uses of the Fund set out in statute, a dichotomy existed between uses of the Fund and the origin of the major funding source (surcharge on taxable oil produced).

The objective of the 1994 audit⁸ was to review the accounting procedures and expenditures incurred against the Response Fund by agencies outside of DEC. This audit looked closely at the use of the Response Fund by other state agencies, the reimbursable services agreement (RSA) process to transfer those funds by DEC, and accountability by agencies for their uses of the Fund.

The second audit also noted concerns about the trend of using the Response Fund for a majority of funding for the State Emergency Response Committee (SERC) and Local Emergency Planning Committees (LEPCs) under their “all hazards” function. The audit report indicated that the Response Fund should be used to fund those activities only to the extent they address oil and hazardous substance issues.

There were no legislative changes made to Response Fund uses, revenue, or management from 1994 to 2005, although the annual Response Fund Report to the Legislature was changed to a biennial report in 1998 with the passage of HB 265. The structure of the Fund has remained unchanged since 1994 through 2005.

⁸ February 6, 1995 Audit (Audit Control Number 18-4499-95).

Table 2: Summary of Alaska’s Oil Legislation

| | | |
|-------------|----------------------------|--|
| 1971 | Senate Bill (SB) 75 | Created DEC; prohibited oil pollution and discharge of oil-contaminated ballast water; and established pollution penalties, restoration damages, criminal violations, and enforcement authorities. |
| 1972 | SB 374 | Established strict liability for the discharge of hazardous substances, including oil. |
| 1976 | SB 267 | Established oil and hazardous substances discharge reporting requirements, provided for injunctive relief, and amended civil assessment and compliance order authorities. |
| | SB 406 | Created the Coastal Protection Fund and provided for regulation of tank vessel traffic, oil terminal facilities, and marine carriers; issuance of certificates of risk avoidance, proof of financial responsibility; governor’s emergency powers; removal of prohibited oil discharges; and enforcement authorities. |
| 1980 | House Bill (HB) 205 | Enacted new oil pollution control statutes to replace provisions in SB 406 which were declared by the federal court to be preempted by federal laws. |
| 1984 | SB 503 | Enacted new hazardous waste requirements, including regulation, permitting, transportation, site selection, and penalty provisions. |
| 1986 | HB 470 | Established the Oil and Hazardous Substance Release Response Fund to provide a funding source for both oil and hazardous substance release responses. |
| 1988 | HB 548 | Made it a violation to fail to have the resources identified in a contingency plan and to fail to respond immediately with those resources in the event of a spill. |
| | HB 553 | Made a \$900,000 appropriation to DEC to inventory, inspect, assess, and clean up contaminated sites located within the Kenai Peninsula Borough. Additional appropriations ensued. |
| 1989 | SB 256 | Provided for the Department of Law to seek cost recovery at request of DEC; clarified municipal reimbursements from the Fund. |
| | HB 68 | Authorized DEC to use liens against property as security for state expenditures. |
| | SB 260 | Established nickel-per-barrel surcharge on regulated industry production and a \$50 million reserve for paying the costs of responses to oil and hazardous substance releases. |
| | SB 261 | Provided for DEC to prepare an annual State Master Plan and Regional Plans. |
| | SB 264 | Established (1) Response Office in DEC for catastrophic or declared emergency spills, (2) emergency response equipment depots in DEC’s Response Office, and (3) emergency response volunteer corps in DEC’s Response Office. Expanded uses of Response Fund to pay for Response Office, depots and corps. |
| | SB 271 | Clarified civil penalty for the unpermitted discharge of oil and the failure to implement an oil discharge contingency plan. |

(Table 2, continued: Summary of Alaska's Oil Legislation)

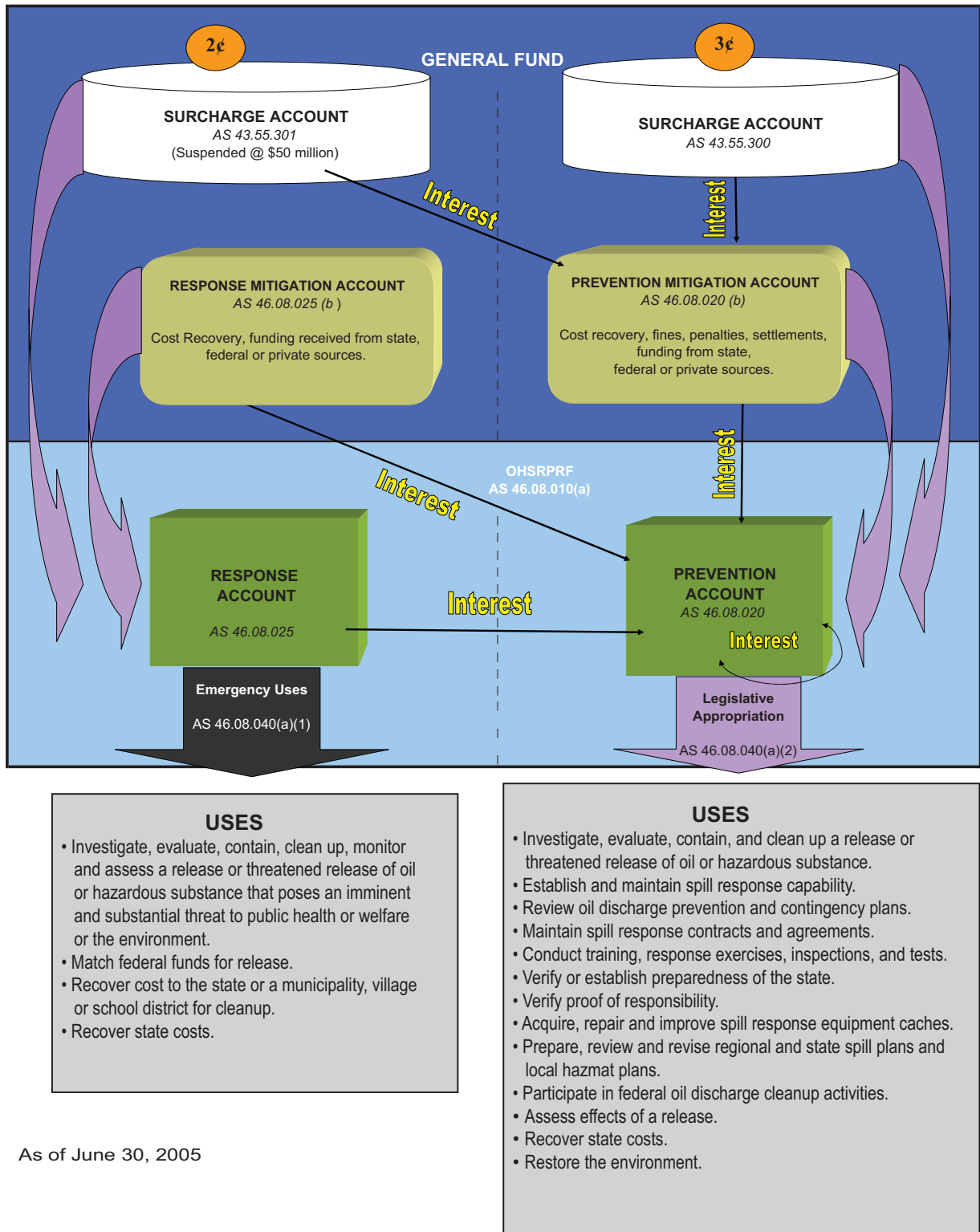
| | | |
|-------------|---------------|--|
| 1990 | HB 220 | Established the Board of Storage Tank Assistance to develop underground storage tank program regulations, tank cleanup program regulations and storage tank workers certification regulations. |
| | HB 315 | Categorized environmental crimes and determined appropriate level of criminal behavior for each. |
| | HB 316 | Established the level of criminal damages to be assessed in fines against organizations for damages caused by environmental crimes. |
| | HB 566 | Established the oil and hazardous substance response corps and response depots in the Department of Military and Veterans Affairs, the State Emergency Response Commission (SERC) in DEC; and oil spill response planning responsibility and the Oil & Hazardous Substance Spill Technology Review Council (under the SERC) in DEC. SERC was required to establish Local Emergency Planning Committees. HB 566 also established the incident command system (ICS) for response to spills. |
| | HB 567 | Required industry contingency plans to include prevention measures. Added certification requirements for approved contingency plans. Clarified proof of financial responsibility and liability limits for tank vessels and oil barge operations. Clarified DEC inspections of regulated industries. Established DEC participation in structural integrity of vessels, barges, pipelines, and facilities. Expanded uses of Response Fund to include: <ul style="list-style-type: none"> • Review of oil discharge prevention and contingency plans. • Conduct training, response exercises, inspections and tests to verify inventories and ability of state, municipal, or parties required to have approved contingency plans. • Verification of financial responsibility. |
| | HB 578 | Established Citizens Oversight Council and expanded uses of Response Fund to include Citizens Oversight Council costs. |
| 1991 | SB 165 | Expanded uses of Response Fund to include refurbishment or construction of marine response vessels. |
| | SB 25 | Expanded uses of Response Fund to municipal grants. |
| | HB 194 | Required the Board of Marine Pilots to cooperate with DEC in the review and approval of training programs for pilots of tankers. |
| | HB 196 | Required the Citizens Oversight Council to submit a report on whether state laws for response action contractor civil liability and vessel contingency plan requirements should be amended. |
| | SB 263 | Provided a one-year delay to June 1, 1992 for compliance of non-crude oil operations with the financial responsibilities in AS 46.04.040. Authorized DEC to issue interim approval for contingency plan amendments that substantially comply with the requirements of Chapter 191, SLA 90. |
| 1992 | SB 540 | Required DEC to (1) develop regulations governing the registration and approval of oil spill primary action contractors, and (2) collect fees in the amount necessary to cover costs of this program. |

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(Table 2, continued: Summary of Alaska's Oil Legislation)

| | | |
|-------------|---------------|--|
| 1994 | SB 215 | Divided the Response Fund into two accounts and restricted uses of the Fund. Transferred SERC responsibility to the Department of Military and Veterans Affairs. Provided that not more than 3% of the estimated annual balance of the Prevention Account may be used to pay for costs incurred by local emergency planning committees. The Response Fund is renamed the "Oil and Hazardous Substance Release Prevention and Response Fund." |
| | SB 33 | Established the Alaska State Emergency Response Commission as "all-hazards" and transferred it to the Department of Military and Veterans' Affairs, along with its associated duties with local emergency planning districts and local emergency planning committees. |
| 1998 | HB 265 | Changed the Response Fund Annual Report to the Governor and Legislature to a biennial report. |
| 2000 | HB 273 | Established contingency plan and proof of financial responsibility requirements for non-tank vessels over 400 gross tons and railroads. Created a Task Force on Motorized Transportation to develop regulations. |
| 2002 | SB 16 | Modified statutes based on recommendations of the Task Force on Motorized Transportation concerning requirements for non-tank vessels and railroads. |
| | SB 343 | Clarified best available technology requirements for oil discharge and prevention contingency plans. |
| 2003 | HB 59 | Provided for regulation of drug labs. |
| | SB 74 | Provided for contingency plan renewal extension. |
| 2005 | HB 197 | Exempted certain natural gas exploration and production facilities for oil discharge prevention and contingency plans and proof of financial responsibility. |

Figure 1: Oil & Hazardous Substance Release Prevention & Response Fund — 2005



C. Structure of the Response Fund in 2005

The Fund consists of two accounts from which spill response activities are financed: (1) the Response Account and (2) the Prevention Account. As revenues are collected for deposit into the Response and Prevention Accounts, they are held in sub-accounts within the general fund. These sub-accounts include the two-cent and three-cent Surcharge Accounts, the Response Mitigation Account, and the Prevention Mitigation Account.

Each fiscal year, through the legislative budget process, revenues held in the various sub-accounts are appropriated to the Response and Prevention Accounts. Interest earned on the various accounts is deposited as outlined in statute. Figure 1 on page 12 shows the sources of funding, the flow of revenue among the accounts, and the uses of each account.

The Response Account

This account is a \$50 million reserve that is readily available to the DEC Commissioner to pay for expenses incurred by DEC during a response to a release or threatened release of oil or hazardous substances when the governor declares a disaster. Money from the Response Account may also be used without a disaster declaration to address a release or threatened release of oil or a hazardous substance that poses an imminent and substantial threat to the public health or welfare, or to the environment. However, since money spent from the Response Account has not been appropriated through the legislative process, DEC must notify the Governor's Office and the Legislative Budget and Audit Committee within 120 hours of accessing the account for emergency responses to spills that have not been declared a disaster. Authorized uses of the Response Account are described in the caption under Response Account in Figure 1, previous page.

The Response Account is funded by:

- Two cents per barrel conservation surcharge on crude oil production.
- Cost Recovery.
- State, federal or private sources.

Table 3, next page, summarizes the funding mechanisms for the Response Account.

Table 3: Summary of Funding Mechanisms for Response Account

| Revenue Categories | Source | Explanation |
|---|--|--|
| Surcharge | \$.02 per barrel conservation surcharge on crude oil produced in Alaska. | Annual estimated balance of deposits into the General Fund of the proceeds of the oil conservation surcharge levied by AS 43.55.201. The surcharge is suspended when the Account reaches \$50 million and is reinstated if the balance falls below that threshold. |
| Cost Recovery (State costs, and other funds) | All direct and indirect state costs. | Money recovered or otherwise received from parties responsible for the containment and cleanup of oil or a hazardous substance at a site for which the state expended money from the Response Account. |
| | Funds from state, federal or private sources. | Money received from other state sources, from federal or other sources, or from a private donor. |

The Prevention Account

This account, under AS 46.08.040 (a)(2), is used to pay the operating expenses associated with maintaining a spill prevention and response office. Prevention and preparedness activities include review of oil spill contingency plans, verifying proof of financial responsibility, conducting training and response exercises, and inspections. It is also used for cleanup of contaminated sites, and for all oil and hazardous substance releases not covered by the Response Account.

The Prevention Account is funded by

- Surcharge of three cents per barrel conservation surcharge on crude oil production.
- Cost Recovery.
- Interest earned income
- Fines, penalties, and settlements.

Money appropriated for operating and capital expenses, and not spent, lapses back into the Prevention Account and remains available for appropriation in successive fiscal years.

A complete list of the authorized uses of the Prevention Account are described in Figure 1, page 12.

Appropriations to DEC and other state agencies by the Legislature come from the Prevention Account to fund the operating and capital expenses of the state’s oil and hazardous substance spill prevention and response programs. Table 4 summarizes all funding mechanisms for the Prevention Account.

Table 4: Summary of Funding Mechanisms for Prevention Account

| Revenue Categories | Source | Explanation |
|---|---|---|
| Surcharge | Three-cent-per-barrel conservation surcharge on crude oil produced in Alaska. | Annual estimated balance of deposits into the General Fund of the proceeds of the oil conservation levied by AS 43.55.300. |
| Cost Recovery (State costs, and other funds) | All direct and indirect state Costs. | Recovery of all costs incurred by the state in the cleanup or containment of released oil or hazardous substances. |
| | Civil Penalties for discharges of non-crude oil. | Recovery of penalties under AS 46.03.758 (dollar per gallon fines for non-crude oil). |
| | Civil Penalties for discharges of crude oil. | Recovery of penalties under AS 46.03.759. |
| | Civil action for pollution damages. | Recovery of fines under AS 46.03.759, costs associated with abatement, containment or removal, restoration of the environment, costs for emergency first response, incidental administrative costs, economic savings, reasonable costs incurred by the state in detection, investigation and attempted correction, and liquidated damages for environmental effects. |
| | Attorney fees and costs. | Recovery of full reasonable attorney fees and costs |
| | Restoration. | Recovery of costs for restoration of the environment to its condition before injury. |
| | Criminal penalties. | Recovery of costs under AS 46.03.790. |
| | Damages. | Recovery of costs in an amount equal to injury to or loss of persons or property, loss of income, loss of the means to produce an income, or loss of an economic benefit. |
| | Funds from state, federal, private, or other sources. | Including federal cost recovery from the Oil Spill Liability Trust Fund, deposits made for specific projects such as the reserve pit closeout funded by industry, funds from private sources, such as the Charter Agreement, which reimburses the state for specific projects or funds from other state agencies, such as the receipt of TAPL funds to conduct specific cleanups. |
| Interest Earned | Prevention Account interest. | Interest earned from the balance in the Prevention Account. |
| | Prevention Mitigation Account interest. | Interest earned from the balance in the Prevention Mitigation Account. |
| | Response Account interest. | Interest earned from the balance in the Response Account. |
| | Response Mitigation Account interest. | Interest earned from the balance in the Response Mitigation Account. |
| | Two-cent Surcharge Account interest. | Interest earned on the balance of the program receipts account (<u>AS 37.05.142</u>) maintained from the proceeds of the two-cent-per-barrel surcharge. |
| | Three-cent Surcharge Account interest. | Interest earned on the balance of program receipts account (<u>AS 37.05.142</u>) maintained from the proceeds of the three-cent-per-barrel surcharge. |

D. Administration of the Fund

Administration of the Response Fund is the responsibility of the DEC Commissioner. The Fund requires oversight to ensure monies used by DEC are appropriately spent and documented using accepted accounting practices, that cost recovery is pursued, that recovered money is appropriately accounted for, and that reporting requirements are met. Oversight is performed under the direction of the Director of the Spill Prevention and Response (SPAR) Division and governed by the authorized uses of the Fund (AS 46.08.040).

HB 470, passed in 1986, addressed administration of the Fund. By providing DEC the responsibility to administer the Fund, the Legislature intended to meet the need for DEC to have “readily available funding necessary to contain and cleanup releases” of oil and hazardous substances that pose a direct threat to the public health, environment, and economy of the state.⁹ DEC was required to follow administrative requirements, issue regulations for administering the Fund, and make fiscal reports to the governor and legislature. The Commissioner of the Department of Administration is assigned responsibility for tracking and reporting on the Response Account balance, and suspending or activating the two-cent surcharge. The Department of Revenue is responsible for investing the money held in the various accounts within the Fund for purposes of earning interest income.

Each year, prior to developing the annual budget request to fund essential state core spill prevention and response priorities, DEC estimates both the near and long-term Prevention Account balance. Projecting the Prevention Account balance is a critical step in monitoring the long term health of the Fund and the programs it supports. It has also been used to calculate the amount of available funding (3% of the Prevention Account balance) eligible for appropriation to Local Emergency Planning Commissions for specific regional spill prevention and response planning activities. At the beginning of each fiscal year, DEC calculates the following year’s Prevention Account balance using the current Account balance, adding projected income, and subtracting the current year’s appropriations. This provides all parties a balance upon which to plan the next year’s budget request, using the most current information available.

DEC must maintain accounting records that show the income and expenses of the Fund. Since the 1994 changes in SB 215, DEC’s role as Response Fund administrator changed from strict accountability for how all state agencies receiving Response Funds use those funds, to those agencies being responsible for accounting for their uses and reporting to DEC.

A biennial report must be made available to the Legislature following the convening of each first regular session by the DEC Commissioner.¹⁰ The report must include the following information, as well as other information considered significant by the DEC Commissioner:

- Amount of money expended for the preceding two fiscal years.
- Amount and source of money received and recovered for the preceding two fiscal years.

⁹ Representative Mike Davis November 12, 1985 Sponsor letter to the Legislature

¹⁰ The last annual report was submitted to the first session of the 21st Legislature in January 2000 for Fiscal Year 1999. Subsequent reports were changed to biennial by the Legislature.

Oil and Hazardous Substance Release Response Fund Report, Fiscal Years 1995 to 2005

- Summary of municipal participation in DEC's responses that were paid by the Fund.
- Detailed summary of DEC response activities paid for by the Fund during the proceeding two fiscal years.
- Projected cost to DEC for the next two fiscal years of monitoring, operating, and maintaining sites where response has been completed or is expected to be continued for the next two fiscal years.
- Number of sites that are included in DEC's contaminated sites database.
- A prioritized listing of those sites, both statewide and by community, based on immediate and long-term threats to the public health or welfare or to the environment.

II. RESPONSE ACCOUNT

A. Revenue

At the time of the creation of the Response Account (SB 215, 1994), the Legislature divided the existing balance of the Response Fund (\$42,081,378) between the two accounts, depositing \$37,081,378 into the Response Account. In addition, the “nickel-per-barrel” surcharge account balance (\$25,900,000) was split, with 40% (\$10,360,000) deposited into the Response Account. The starting balance of the Response Account on July 1, 1994, was \$47,441,378.

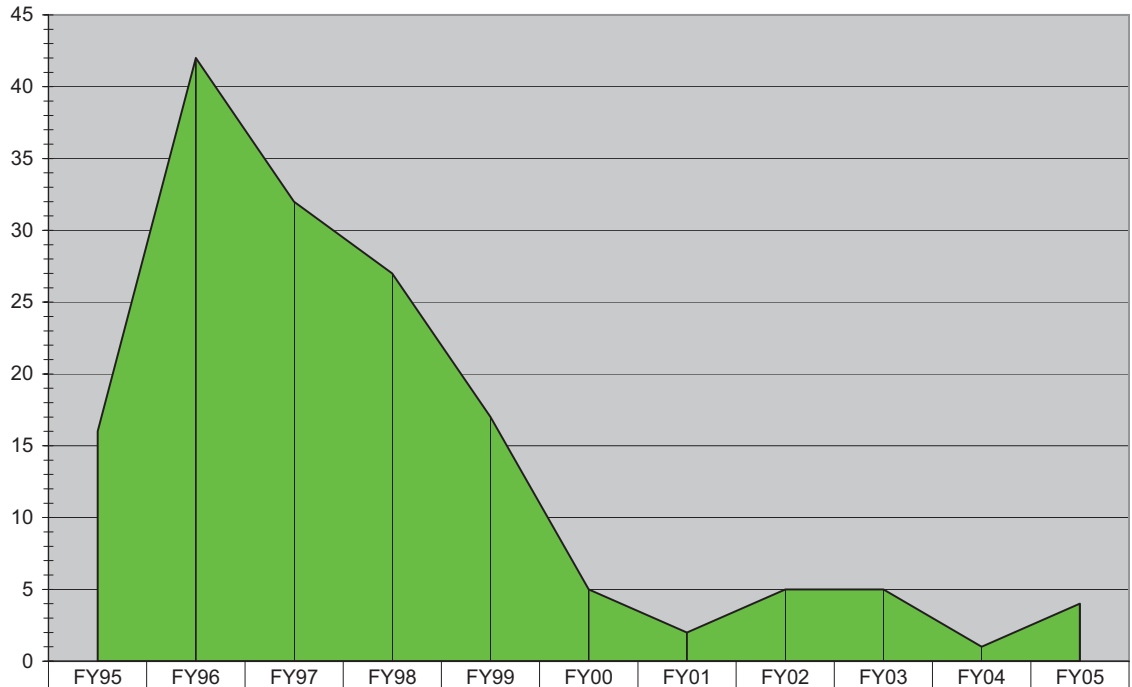
The two-cent surcharge is suspended when the combined balances of the following accounts equal or exceed \$50 million: the Surcharge Account, the Response Mitigation Account¹¹, and the unreserved and unobligated balance of the Response Account. Within 30 days of the end of each calendar quarter, the Commissioner of the Department of Administration determines the Response Account balance and files a report. Suspension of the surcharge begins on the first day of the calendar quarter following the determination that the balance equals or exceeds \$50 million. The \$50 million balance was exceeded in December 1994 and the surcharge has been suspended since April 1995.

The Response Account has remained above \$50 million since the two-cent surcharge was suspended in 1995. The Account has been accessed several times since 1995, causing fluctuations in the balance, however, cost recovery efforts have generally been successful and always timely enough to prevent the account from dipping below the \$50 million cap.

Revenue collected during a fiscal year is held in either the surcharge account or the response mitigation account and transferred to the Response Account through legislative appropriation language the following fiscal year (FY). In other words, revenue collected and held in FY 94 would not be in the Response Account, and available for use, until FY 95. Revenues reflected in Figure 3 are shown for the fiscal year the money was available for use, rather than the fiscal year that the money was collected.

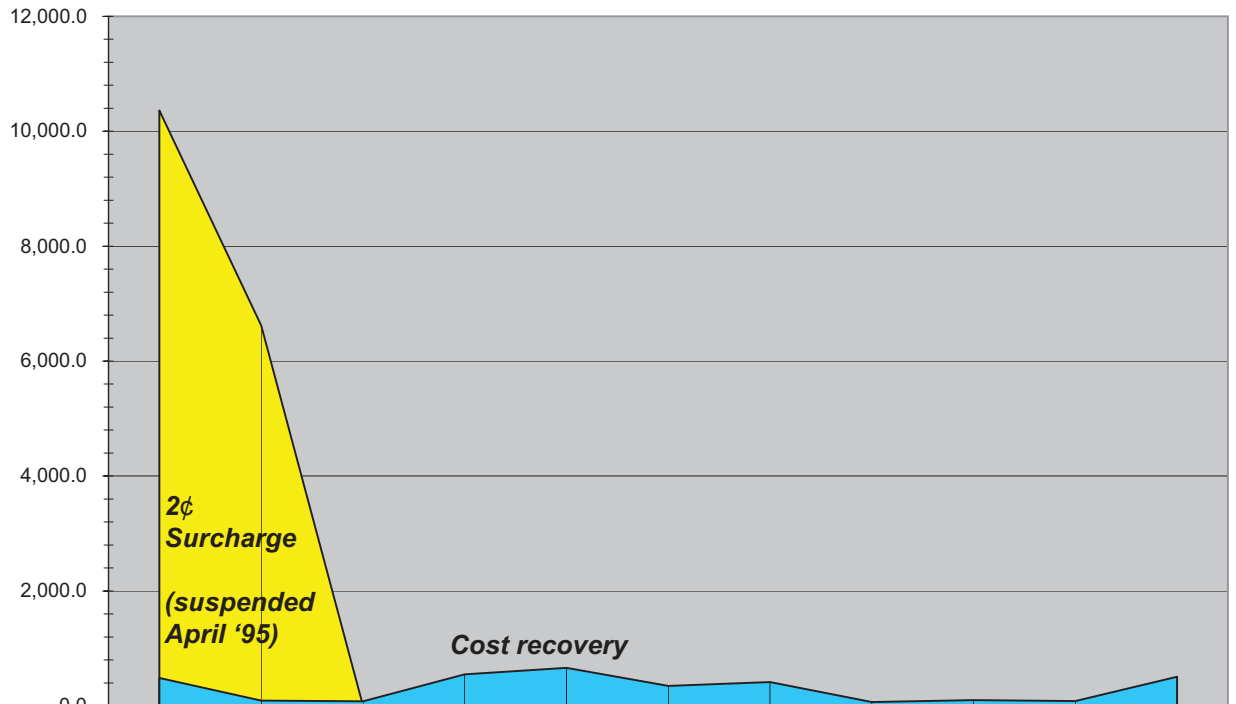
¹¹ See Figure 1, page 12.

Figure 2: Number of Times the Response Account Has Been Accessed by Fiscal Year



| | | | | | | | | | | | |
|--|----|----|----|----|----|---|---|---|---|---|---|
| Response Account Access - Number of Times per Year | 16 | 42 | 32 | 27 | 17 | 5 | 2 | 5 | 5 | 1 | 4 |
|--|----|----|----|----|----|---|---|---|---|---|---|

Figure 3: Response Account Revenue (\$Thousands)



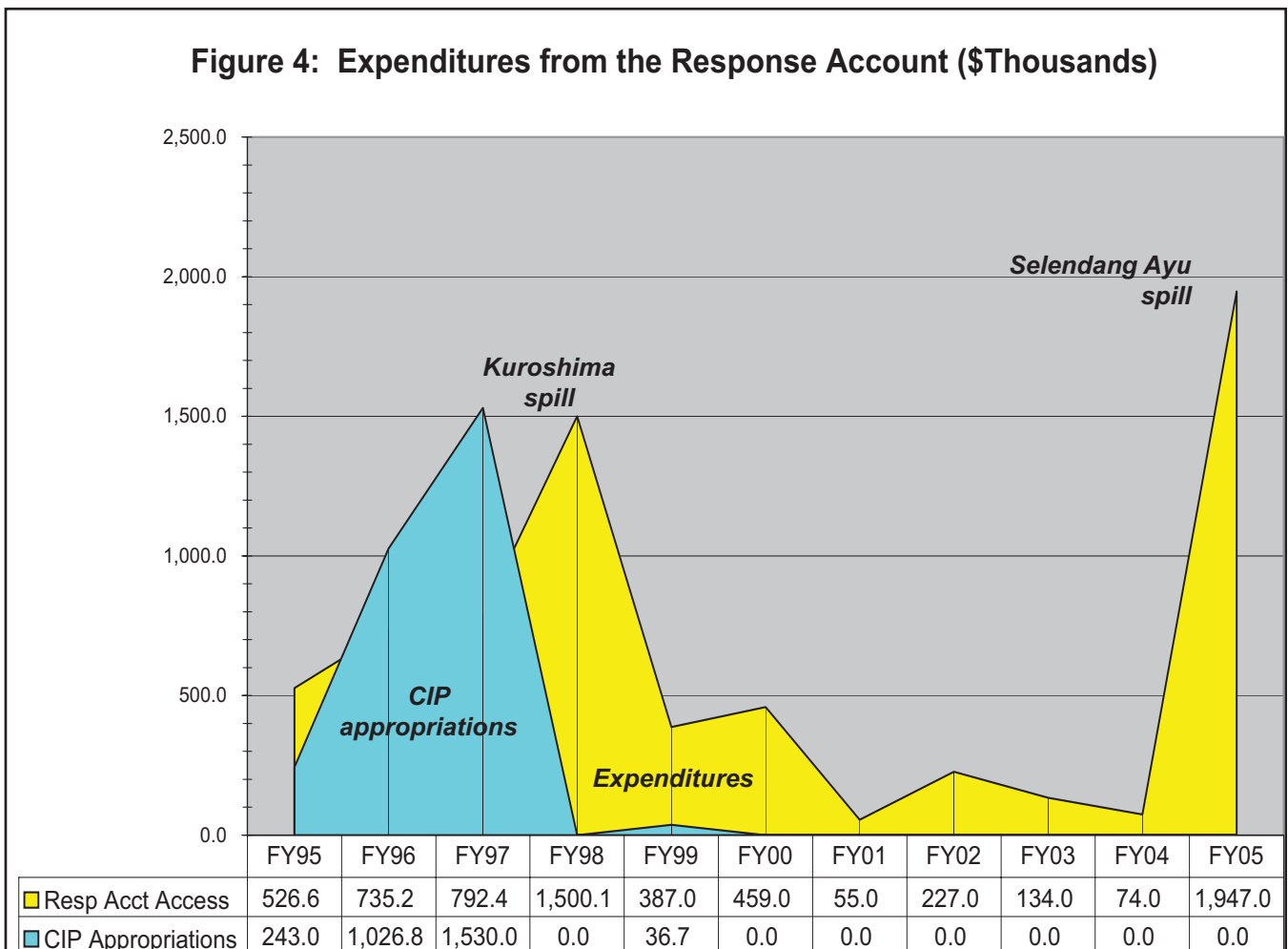
| | | | | | | | | | | | |
|------------------|----------|---------|------|-------|-------|-------|-------|------|------|------|-------|
| 2-Cent Surcharge | 10,360.0 | 6,619.3 | | | | | | | | | |
| Cost Recovery | 487.3 | 91.3 | 79.4 | 548.7 | 663.7 | 347.3 | 416.6 | 67.7 | 98.7 | 82.0 | 505.5 |

B. Expenditures

Expenditures vary according to spill incident circumstances (e.g., product and amount spilled, contaminated resources, restoration). Since 1995, DEC has carefully considered each funding request for its appropriateness for emergency funding prior to accessing the Response Account for an incident. The Response Account has been accessed primarily for imminent and substantial spills. In addition to accessing the account for emergency spills, the Response Account was used during the mid to late 1990s to fund several CIP budget appropriations to agencies other than DEC for various cleanup projects around the state.

By law, the account balance is to be maintained at \$50 million. This amount provides adequate funds for the initial cost of a state response to a major oil spill until more money is provided.

Figure 4 illustrates the appropriations for CIP budgets and expenditures for emergency response to spills. The spike that occurred in FY 1998 was due to the grounding of the freighter *Kuroshima*, and the spike in FY 2005 is due to the grounding of the cargo ship *Selendang Ayu*.



III. PREVENTION ACCOUNT

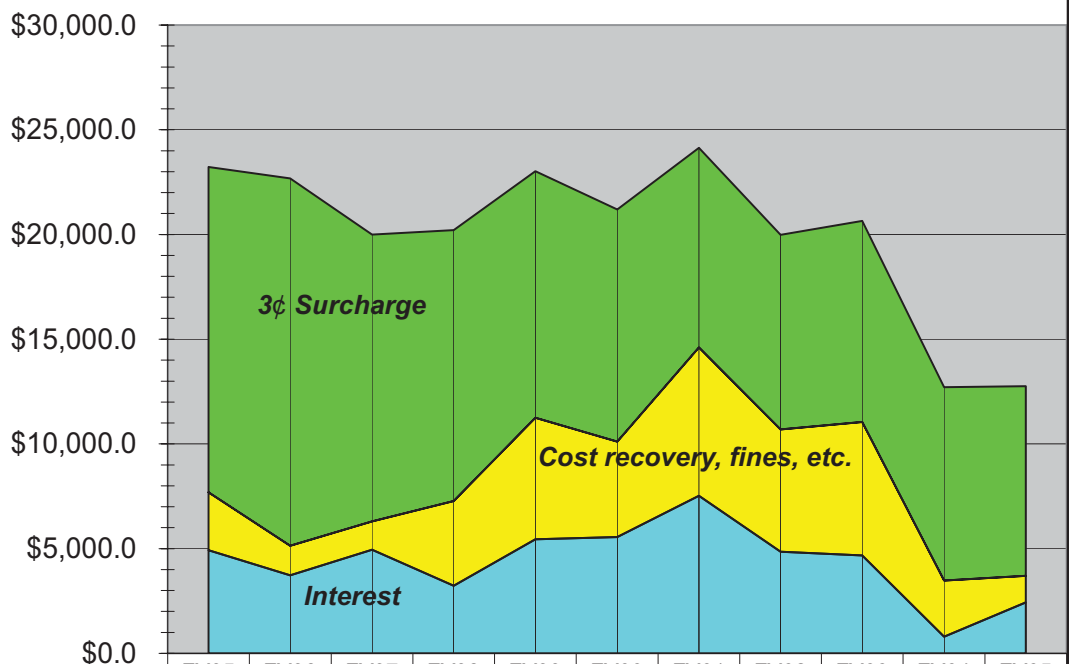
A. Revenue

The Prevention Account is funded by:

- 1) the three-cent per barrel conservation surcharge,
- 2) cost recovery (including fines and penalties imposed on persons as the result of a release or threatened release of oil or a hazardous substance), and
- 3) interest earned income (interest earned on the balance of the Response Fund and prevention account cost recoveries).

At the time of the creation of the Prevention Account (SB 215, 1994), the Legislature divided the existing balance of the Response Fund (\$42,081,378) between the two accounts, depositing \$5,000,000 into the Prevention Account. In addition, the surcharge account balance (\$25,900,000) was split, with 60% (\$15,540,000) deposited into the Prevention Account. The starting balance of the Prevention Account on July 1, 1994, was \$20,540,000. This split of the nickel essentially reduced available funding to operate spill prevention and response programs by 40%.

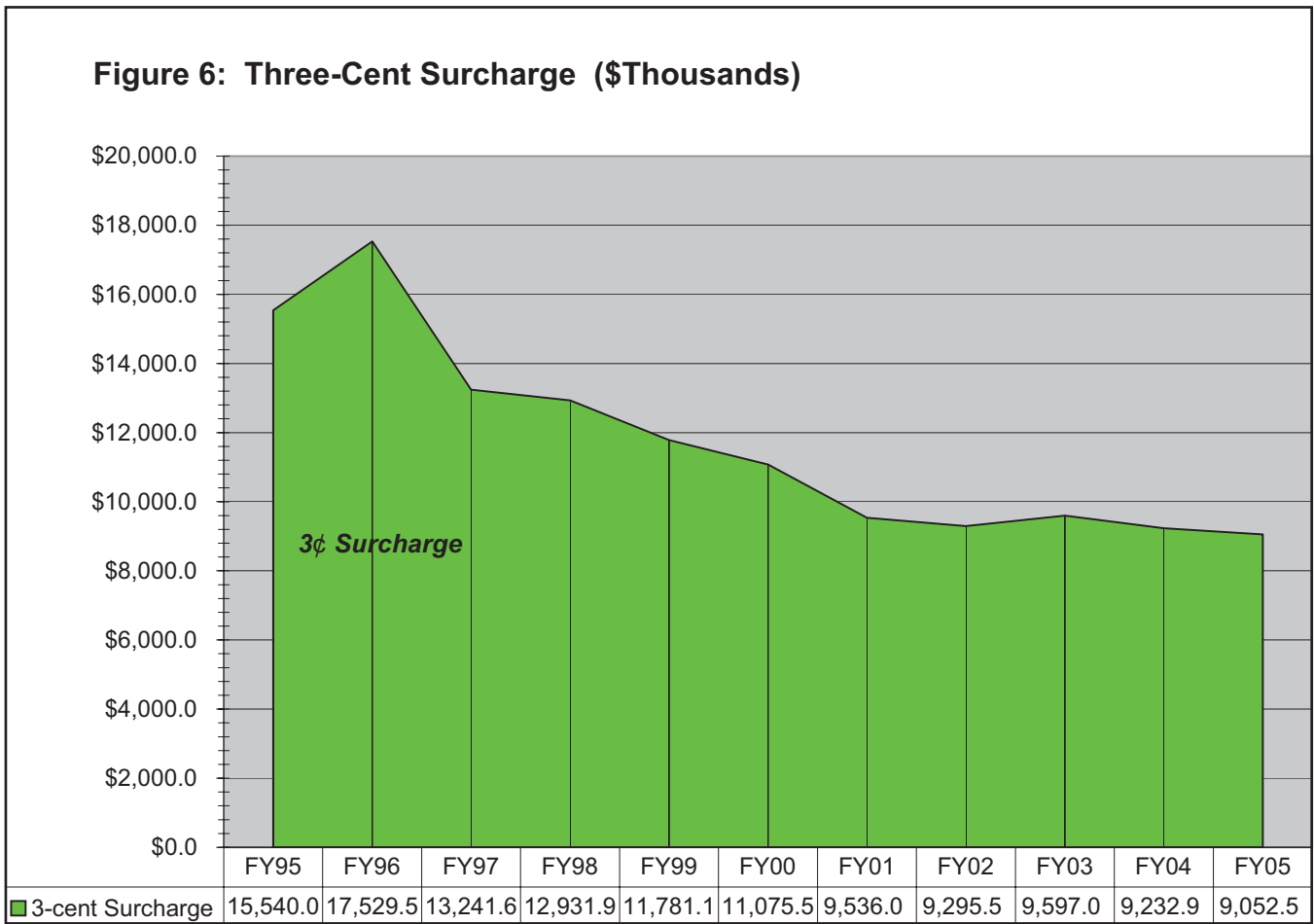
Figure 5: Prevention Account All Revenues (\$Thousands)



| | FY95 | FY96 | FY97 | FY98 | FY99 | FY00 | FY01 | FY02 | FY03 | FY04 | FY05 |
|---|----------|----------|----------|----------|----------|----------|---------|---------|---------|---------|---------|
| ■ 3-cent Surcharge | 15,540.0 | 17,529.0 | 13,698.0 | 12,931.0 | 11,781.0 | 11,075.0 | 9,536.0 | 9,295.5 | 9,597.0 | 9,232.9 | 9,052.5 |
| ■ Cost Recovery, Fines, Settlements, Misc | 2,768.5 | 1,422.4 | 1,351.7 | 4,048.3 | 5,799.0 | 4,559.3 | 7,082.8 | 5,835.0 | 6,372.9 | 2,680.8 | 1,274.8 |
| ■ Interest | 4,919.0 | 3,721.9 | 4,949.9 | 3,228.1 | 5,445.2 | 5,554.6 | 7,523.1 | 4,859.1 | 4,678.4 | 791.9 | 2,428.4 |

1. Three-Cent Surcharge

The largest source of recurring revenue to the prevention account has been the three-cent surcharge per barrel of crude oil produced. As shown in the graph below, the amount of revenue received from the surcharge peaked in FY 1996 at over \$13 million and has been gradually declining ever since. In FY 2005 the amount of revenue was the lowest ever received, at just over \$9 million, and is projected to decline further in future years as the level of oil production decreases.



2. Cost Recovery (state costs, fines, penalties, damages and other funds)

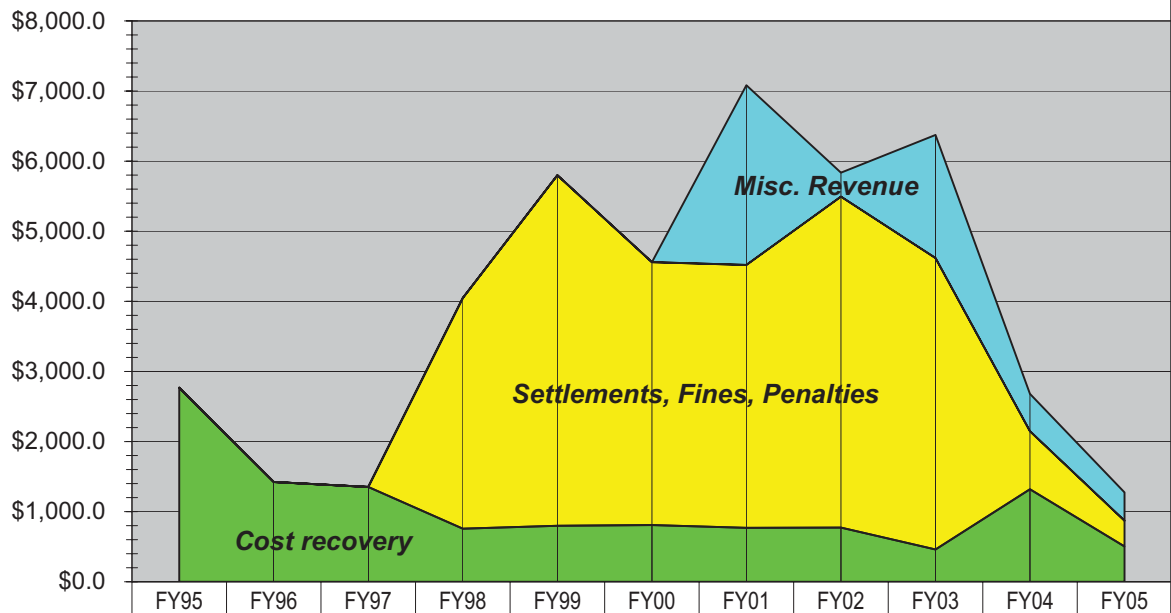
Parties responsible for the release of oil and hazardous substances are liable for costs associated with response and/or cleanup. The state attempts to recover all its oversight costs from all responsible parties when one or more can be identified. Revenue is also received from fines, penalties, and settlements.

In 1998 the Prevention Account received its first of six installments of the settlement payment resulting from the *Exxon Valdez* oil spill. The average annual payment of \$3.9 million ended in 2003, causing a significant decline in settlement income.

Other funds can come from a variety of places including fees, and federal and private sources.

These revenue sources are non-recurring in nature, and the amounts tend to fluctuate greatly from year to year, making it difficult to make reliable, long-term revenue projections.

Figure 7: Cost Recovery, Settlements, Fines, Penalties and Miscellaneous Revenue (\$Thousands)



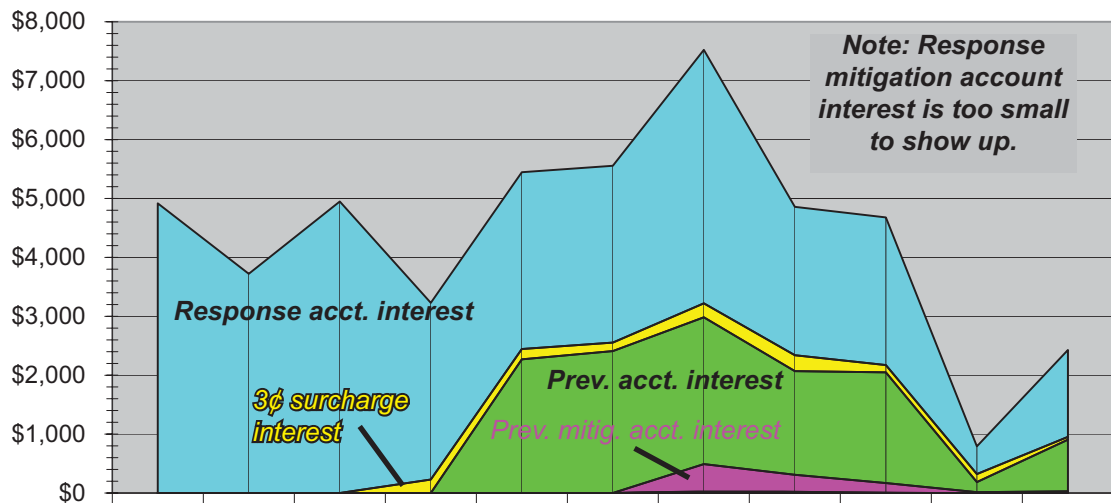
| | | | | | | | | | | | |
|-------------------------------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|-------|
| Misc. Revenue | | | | | | | 2,563.8 | 342.1 | 1,756.0 | 533.0 | 403.7 |
| Settlements, Fines, Penalties | | | | 3,291.4 | 5,000.0 | 3,750.0 | 3,750.0 | 4,719.8 | 4,155.7 | 827.6 | 366.6 |
| Cost Recovery | 2,768.5 | 1,422.4 | 1,351.7 | 756.9 | 799.0 | 809.3 | 769.0 | 773.1 | 461.2 | 1,320.2 | 504.5 |

Note: Revenue amounts derived from cost recovery, fines, penalties, settlements, and miscellaneous are not available by those specific categories for Fiscal Years 1995 through 1997. All revenue collected for those years is shown as Cost Recovery.

3. Interest Earned

All monies held in the various accounts that make up the Response Fund are invested, with returns being deposited into the Prevention Account. Historically, investment income has been a substantial contributor to the balance of the prevention account, averaging roughly \$5.3 million per year between 1995 and 2003. Investment income peaked in 2001 at \$7.5 million, but in 2004 investments only earned just under \$800 thousand. In Fiscal Year 2005, investment income rebounded slightly, to earn about \$2.4 million; however, a return to the previous average of \$5.3 million is not expected. The Department of Revenue serves as the Fund’s investment manager.

Figure 8: Investment Income (\$Thousands)



| | FY95 | FY96 | FY97 | FY98 | FY99 | FY00 | FY01 | FY02 | FY03 | FY04 | FY05 |
|--|---------|---------|---------|---------|---------|---------|---------|---------|---------|-------|---------|
| Response Account Interest | 4,919.0 | 3,721.9 | 4,949.9 | 3,000.0 | 3,000.0 | 3,000.0 | 4,303.8 | 2,519.5 | 2,505.5 | 470.6 | 1,475.5 |
| 3-Cent Surcharge Interest | | | | 228.1 | 176.9 | 145.1 | 237.1 | 271.5 | 123.7 | 135.8 | 46.3 |
| Prevention Account Interest | | | | | 2,268.3 | 2,409.5 | 2,490.5 | 1,758.6 | 1,880.7 | 172.4 | 877.8 |
| Prevention Mitigation Account Interest | | | | | | | 467.9 | 289.9 | 166.3 | 13.5 | 23.1 |
| Response Mitigation Account Interest | | | | | | | 23.8 | 19.6 | 2.2 | 0.0 | 5.7 |

Note: Revenue amounts derived from interest income is not available by specific categories for Fiscal Years 1995 through 1997. All interest income revenue collected for those years is shown as Response Account interest.

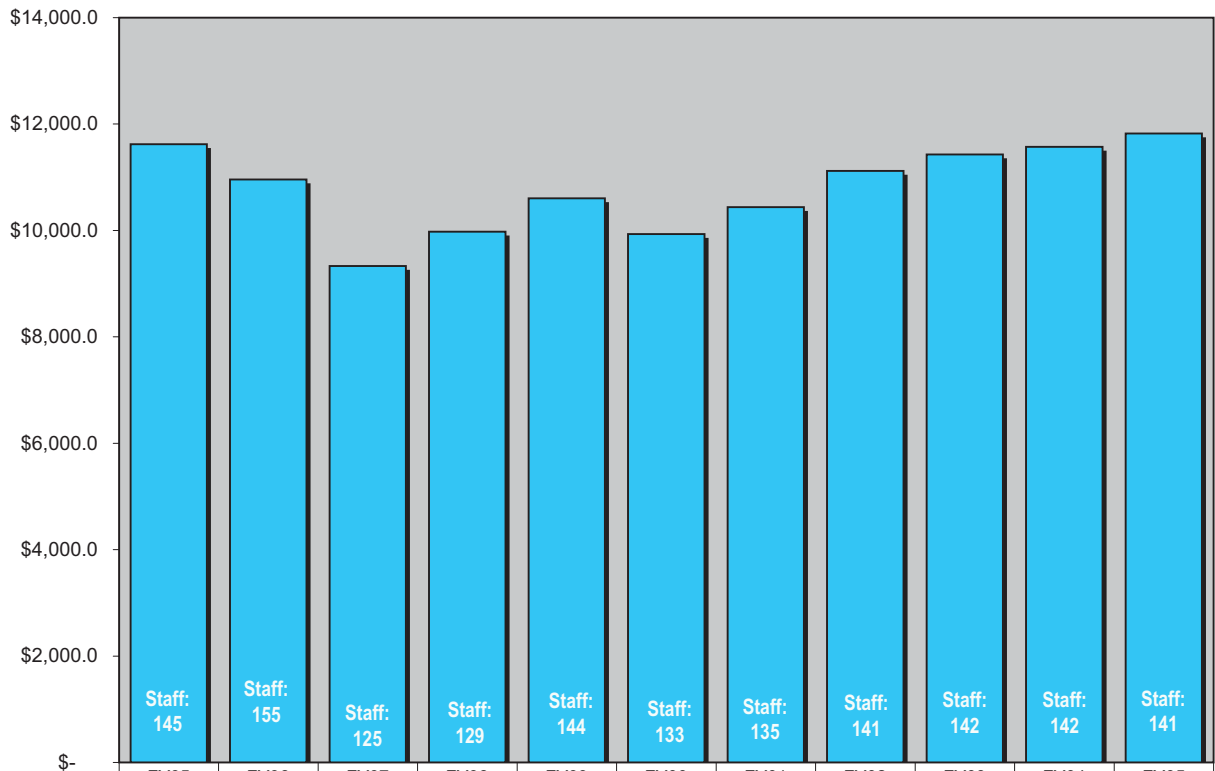
B. Appropriations

Under AS 46.08.040, the prevention account may be used for: 1) various general operating expenses such as maintaining a response office; 2) activities associated with investigating, evaluating, and responding to spills of oil and hazardous substances; 3) prevention activities; 4) match for federal grants; and 5) other purposes. The Response Fund portion of the SPAR Division's annual Operating budget, portions of other divisions' Operating budgets, and Capital Improvement Project budgets are appropriated by the legislature from the prevention account balance.

SPAR Operating Appropriations

Although SPAR Operating appropriations from the prevention account have fluctuated since 1995, they have always stayed within the total revenue available in the account. In FY 1995, SPAR's Response Fund appropriation was \$11,620.4 million. Ten years later, in FY 2005, SPAR's Response Fund appropriation was \$11,821.8 million, an increase of 1.7% over a decade.

Figure 9: SPAR Division Operating Appropriations (\$Thousands)



Alaska Department of Environmental Conservation

Other Operating Appropriations

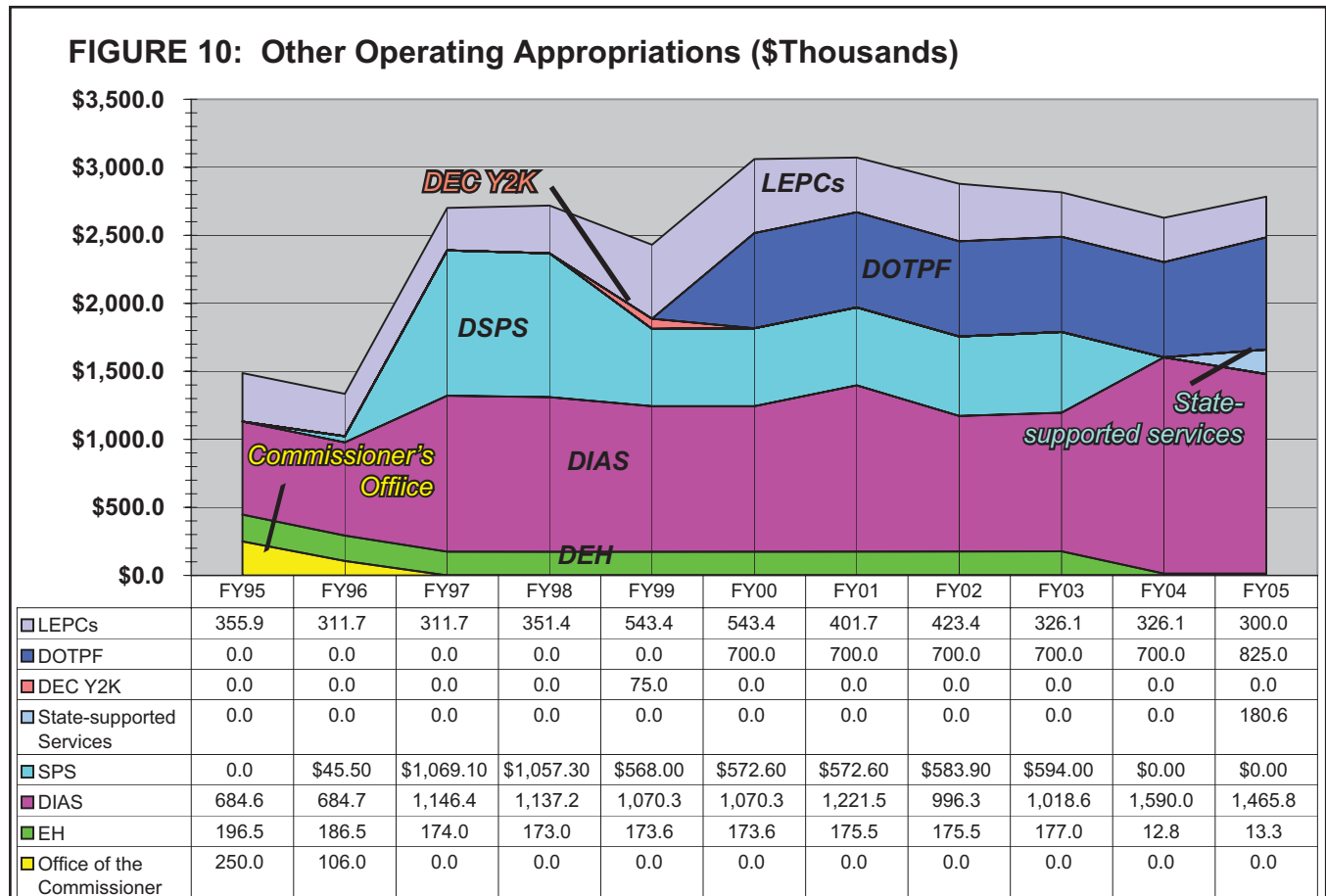
Other divisions within DEC and other departments also receive appropriations of the Response Fund in their Operating budgets. In FY 1995, the total amount of money appropriated to divisions other than SPAR and other state agencies was \$1,487.0 million. In FY 2005, the amount of the Response Fund appropriated to non-SPAR entities totaled \$2,784.7 million, an increase of 87.3% over a decade.

Those other agencies, as listed in Figure 10 below, include:

- Local Emergency Planning Commissions (LEPCs).
- Alaska Department of Transportation and Public Facilities (DOTPF).
- DEC's Year 2000 (Y2K) effort.
- other state-supported services.

Other units within the department have included:

- Division of Information and Administrative Services (DIAS).
- Division of Environmental Health (DEH).
- Commissioner's Office.
- Division of Statewide Public Services (DSPS), in existence from 1996 to 2003.



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