

Alaska Oil and Gas Association



121 W. Fireweed Lane, Suite 207
Anchorage, Alaska 99503-2035
Phone: (907) 272-1481 Fax: (907) 279-8114
Kara Moriarty, President/CEO

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Representatives Nageak and Talerico
House Resources Committee Co-Chairs
Alaska State Legislature
Juneau, AK 99801

Dear Representatives,

Thank you for allowing the Alaska Oil and Gas Association (AOGA) to respond to questions during testimony on May 28, 2016. I do have unanimous consent from our diverse membership to share the following thoughts and suggestions.

Before I discuss the follow-up, I would like to reiterate a few points that were made during the public hearing. While we appreciate the notion of an expanded loan program could be a tool in the state's tool box to attract industry investment to Alaska, we strongly urge members of the committee to recognize that a loan program should not be considered a replacement to the current system of refundable tax credits. The benefit to the state is greater with the current system versus the benefit of a loan program. The reason we suggest this is because some in industry leverage refundable credits to attract private capital and loans, which generate a much greater overall level of capital available to move projects forward.

Furthermore, we wish to take the opportunity to remind the Committee that in order to qualify for a refundable credit that a company must first invest its own capital in exploration, development and production type activities. After its initial investment into the Alaska economy, the company must then apply for its credit certificate and undergo extensive auditing by the Department of Revenue before a certificate is issued. Credits are not "free money".

While this proposed loan program does provide for some level of support for above ground infrastructure, the overall tax policy and current suite of tax credits provide a critical level of support for activities that include both exploration and drilling activities, activities that support a path to more production.

AOGA discussed our concern with the definition of "proven reserves" and we were asked to provide the definition utilized by the Securities and Exchange

Commission (SEC). The definition is attached, along with an amendment for your consideration to amend HB 246 and adopt the SEC definition.

AOGA was also asked to provide feedback on AIDEA's proposals addressing seven concerns that have been brought forward on HB 246 during the Committee's deliberations.

Concern 1 It is prudent not to use one term — “reserves” — in two very different contexts. AIDEA's fix is to say “financial reserves” when they are talking about a borrower's financial strength, and “proved reserves” to describe the resource that the borrower is looking at. Better would be to use “financial resources” or “creditworthiness” for the financial side, which avoids using “reserves” at all in that financial-strength context.

Concern 2 AIDEA's language about not taking on any responsibility for dismantlement, removal or remediation obligations is a good idea.

Concern 3 AOGA's proposal to adopt the SEC definition is superior because it includes, among other things, the concept of “commercially recoverable” that AIDEA has raised as an omission. AIDEA's loan-to-value “fix” for the concern isn't really a fix when a borrower is free to write whatever “value” it wants for its so-called “reserves.” The SEC's “focus more on the economics of production” is exactly what AIDEA – as a lender – needs to look at, versus a company's claim as to what may exist.

Concern 4 AIDEA's answer to this concern would allow financing of the 30” “ASAP” line that the Alaska Gasline Development Corporation was considering under AS 31.25.005(4).

Concern 5 AIDEA proposes letting its Board shift the money around between gas-pipeline uses and other uses without limitation. As a matter of public policy, it's better to have the people's elected representatives — the Legislature — allocate the money for one purpose or the other.

Concern 6 AOGA has no comment to offer here.

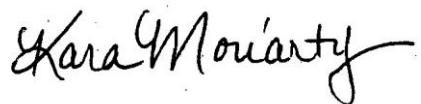
Concern 7 It is a good idea to set limits on AIDEA loan participation above which legislative approval would be required. AOGA would add that Sections 10 and 11 would allow not only allow AIDEA to make a loan or a loan guarantee, Section 10 would also allow AIDEA to purchase or acquire gas reserves, a gas lease or become a working interest owner in a gas lease. This is inconsistent with AIDEA's response to Concern 2 that it would not become liable for dismantlement, removal and restoration costs. Before acting on HB 246 the Legislature should fully understand this provision and the nature and size of the risks that may be involved for AIDEA to have this ability.

One additional concern that we would like to note is in Section 12 of the Bill, which says if any participant in an oil and gas field applies for a loan, then not only must

it agree to forgo all tax credits as part of the application, but all the other participants also have agree to forgo all tax credits as well. This provision would make it more difficult for the loan applicant to get approval, which in turn will affect timing, capital costs, etc.

In closing, in today's difficult financial times it is our opinion that the last thing the State should consider at this critical juncture is to replace a successful program of tax credit incentives with an overly complicated loan program fraught with many unknowns, and to have a state agency with less oil and gas expertise assume a greater role in creating incentives for the industry than the Department of Natural Resources or Department of Revenue.

Sincerely,



Kara Moriarty
President/CEO

Attachments: SEC Definition
 AOGA Suggested Amendment for "proved reserves"