SB 305:
The Separation of Oil from Gas for the Oil & Gas Production Tax

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Premise of the Bill

- Under current law oil and gas are taxed together
- Oil is worth much more than gas
- The combining mechanism materially reduces oil taxes even though oil operations are unaffected

Oil is Different than Gas

- Oil more geographically concentrated (fewer sellers: OPEC)
- Oil supplies more depleted
- Gas is more plentiful
- Oil has fewer substitutes
- Gas has more substitutes

BTU 10:1

West Coast ANS

- Market Price $80/bbl
- Less:
  - Shipping $2.07
  - TAPS $4.18
- Gross Value $73.75

North Slope Gas

- Market Price $6/mmbtu
- Less:
  - Tariff AK to AB $3.54
  - AB Hub $0.24
  - Tariff AB to L48 $0.85
- Gross Value $1.37/mmbtu
- BOE Basis (X 5.5) = $7.54
- On a straight BTU to BTU basis oil is worth nearly 10 X as much as gas

Some Things that have BTUs

- Oil
- Gas
- Coal
- Wood
- Asphalt
- Shoe Leather
- Rubber
- Coffee grounds
- Citrus rinds
- Corn cobs
- Dung

Mechanics of Current Tax

- 1) Oil gross value (market price less transport cost)
- 2) Gas gross value (market price less transport cost)
- 3) Oil + gas gross value gas = Combined gross value
- 4) Combined gross value – lease capital and operating costs = Combined oil & gas net value
- 5) Combined oil & gas net value / total oil & gas BOEs = p/BOE net value (see Slide #6)
- 6) Progressivity factor (based on per BOE net value) plus 25% base rate = tax rate
- 7) Single tax rate applied to combined oil & gas net value

Barrel of Oil Equivalents (BOEs):
Putting Oil & Gas on an Apples / Apples Basis

- 4.5 billion cubic feet per day (bcf/d) of natural gas
- A cubic foot of North Slope gas will have about 1,100 BTUs
- Natural gas is measured in millions of BTUs (mmbtu)
- 4.5 billion cubic feet per day will have 4.95 million mmbtu's (4.5 X 1,100)
- A barrel of oil has about 5,500 BTUs
- 4.5 billion cubic feet per day will have the BTU equivalence of 900,000 barrels of oil (BOEs) (4,950,000 / 5.5)
- If there are 500,000 barrels of oil, total BOEs will total 500,000 + 900,000 = 1,400,000

Progressivity Mechanics

- "Trigger" = $30 net / BOE value
- "Slope" = 0.4%*
- Progressivity surcharge = (Net per BOE value - $30) X .004
- Example: if net value = $50
  - Base tax rate = 25%
  - Progressivity = ($50 – $30) X .004 = 8%
  - Total tax of 33% on net value

* Slope changes to 0.1% after $92.50 net per BOE value

HOW GAS IMPACTS OIL TAXES

	Oil Alone (p/bbl)	Gas (p/mmbtu)	:	Combined Oil & Gas	
			:		
Market Price	$80.00	$6.00	:	Oil	
Transp cost	$5.00	$4.50	:	p/bbl net value	$55.00
Gross Value	$75.00	$1.50	:	Barrels (millions)	183
			:	Total oil net value ($mm)	$10,038
Costs	$20.00	$0.50	:	Gas	
			:	p/mmbtu net value	$1.00
Net (p/barrel or p/mmbtu)	$55.00	$1.00	:	mmbtu's (millions)	1,807
			:	Total gas net value ($mm)	$1,807
Base rate	25.00%		:		
Progressivity	10.00%		:	Total oil & gas net value	$11,844
Total tax rate	35.00%		:	Total BOEs	511
			:	Net value / BOE	$23.18
Daily bbls (oil) or mmbtu (gas)	500,000	4,950,000	:	NO PROGRESSIVITY!	
Daily BOEs	500,000	900,000	:		
Annual BOEs (millions)	183	329	:		

DEPARTMENT OF REVENUE EXAMPLES
FROM FEBRUARY 24, 2010 PRESENTATION
TO SENATE FINANCE
"Progressivity Profitability Parity Gas"

Oil Price	Gas Price	Oil Alone Progressivity Factor	Oil & Gas Combined Progressivity Factor	Reduction in Progressivity Factor	Oil Alone Tax ($billions)	Gas Alone Tax ($billions)	Total Tax if Taxed Separately ($billions)	Combined Tax ($billions)	Annual Tax Reduction from Combining ($billions)
$75	$8.00	5.38%	0.00%	5.38%	$1.7	$1.1	$2.8	$2.5	$0.3
$100	$8.00	15.38%	3.59%	11.79%	$4.0	$1.1	$5.1	$4.0	$1.1
$120	$8.00	23.38%	6.79%	16.59%	$6.4	$1.1	$7.5	$5.5	$2.0

How the Bill Works

- Under the current law there is a base tax rate of 25%
    - Plus progressivity based on the combined oil & gas net value / BOE
- The bill removes progressivity on gas
- Progressivity on oil continues to be calculated just on oil net value / barrel
- Exclusion of gas in the progressivity calculation does not reduce oil taxes