

# Judge Gleason's Decision: An Alternate Perspective

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*August 9, 2012*

# Disclaimers

- The opinions expressed here are entirely my own; not speaking on behalf of any client
- Not involved in the case, but monitored the case and have studied the decision closely because of its potential impact on Alaska
- Not here to challenge or dispute the logic or conclusion of the opinion

# Agenda

- Background
- What the decision says
- What the decision doesn't say
- The implications for the future

# Background of the Case

- State court dispute over the valuation of TAPS for property tax purposes
- Parties: Alyeska v. the North Slope Borough, Fairbanks North Star Borough and Valdez (and the Alaska Dep't of Revenue)
- Life of TAPS is relevant to TAPS economic value and accumulated depreciation
- Decision subject to appeal to the Alaska Supreme Court

# What the Decision Says

- Judge Gleason found that the value of TAPS for property tax purposes was \$8.94 B (2007), \$9.64 (2008), \$9.24 (2009)
- In the course of determining those values, concluded that “the life of TAPS based on its proven reserves and incorporating its minimum capacity throughput limitations as of ... 2007, 2008 and 2009 is at least until 2065.”
- Based on her conclusion that TAPS can continue to accommodate flows as low as 70,000 bbl/d

# What the Decision Doesn't Say

- The decision doesn't say anything about current or reasonably foreseeable production levels
  - The decision simply says that the production tail will continue longer
- The decision also doesn't say anything about the effect of declining production on the state's economic well being
  - The decision doesn't speak to state revenue

# The Implications

- Joe Balash has it right ...
  - “Deputy Natural Resources Commissioner Joe Balash said *a 300,000-barrel a day throughput scenario ... would be a ‘disaster,’* because at that level, the state budget would be in a ‘dire deficit.’”
    - Becky Borher (AP), Fairbanks Daily News-Miner, Jan. 8, 2012 (17 paragraphs into the story).
- To paraphrase James Carville from the 1992 Presidential campaign
  - In Alaska, “It’s the production rate ...”
  - ... not the reserve life

# Current ANS Production Forecast

**Figure 4-11. Alaska North Slope Production, FY 2011 and Forecasted FY 2012-2021<sup>(1)</sup> (million barrels per day)**

Fiscal Year	Currently Producing	Percent Change from Prior Yr.	Under Development	Under Evaluation	Total ANS	Percent Change from Prior Yr.
2011	0.603	(6.3%)	0.000	0.000	0.603	(6.3%)
2012	0.548	(9.1%)	0.026	0.001	0.574	(4.7%)
2013	0.485	(11.6%)	0.069	0.001	0.555	(3.3%)
2014	0.451	(6.9%)	0.099	0.010	0.561	1.0%
2015	0.406	(10.0%)	0.115	0.017	0.538	(4.1%)
2016	0.369	(9.1%)	0.151	0.029	0.550	2.1%
2017	0.336	(9.1%)	0.179	0.034	0.549	(0.1%)
2018	0.307	(8.5%)	0.171	0.066	0.544	(0.9%)
2019	0.282	(8.1%)	0.166	0.066	0.515	(5.4%)
2020	0.262	(7.4%)	0.164	0.061	0.486	(5.6%)
2021	0.241	(7.7%)	0.161	0.056	0.458	(5.8%)

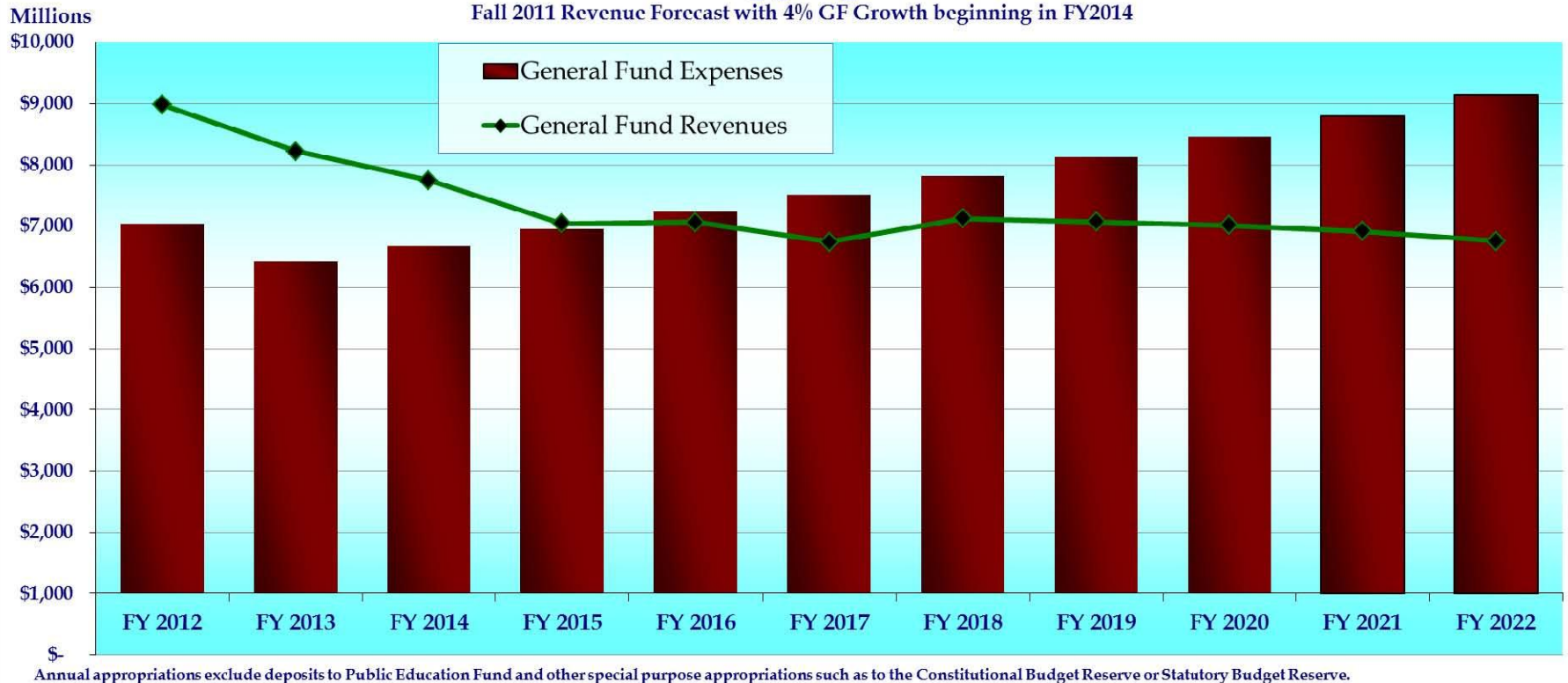
<sup>(1)</sup> Some of the oil forecasted in the Under Development and Under Evaluation categories are from new projects in fields currently producing.



# Scenario 3: Governor's FY2013 Budget with 4% Annual GF Expenditure Growth beginning in FY2014

## GF Revenue versus Appropriations FY12 to FY22

Fall 2011 Revenue Forecast with 4% GF Growth beginning in FY2014



**Source: Office of Management and Budget FY2013 10-Year  
Plan (p. 13)**

# Scenario 3: Governor's FY2013 Budget with 4% Annual GF Expenditure Growth beginning in FY2014

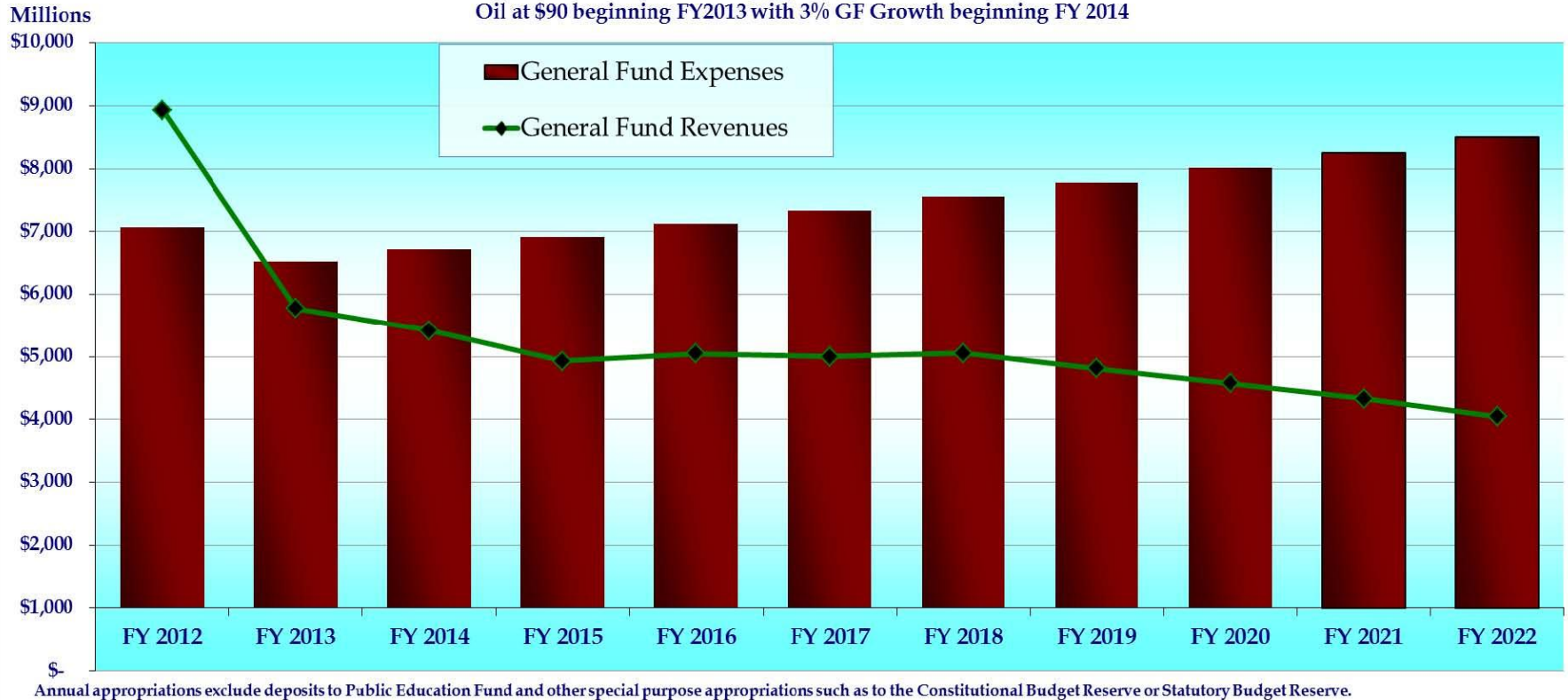
Oil Price & Production	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21	FY22
Fall 2011 forecast ANS West Coast (\$/bbl.)	\$108.98	\$109.47	\$109.08	\$108.75	\$107.79	\$106.05	\$108.76	\$111.54	\$114.39	\$117.31	\$120.31
Fall 2011 forecast ANS production (mmbbl./day)	0.574	0.555	0.561	0.538	0.550	0.549	0.544	0.515	0.486	0.458	0.432
Revenue vs. Spending (\$millions)											
General Fund Revenues <sup>1/</sup>	\$8,981.8	\$8,217.7	\$7,742.8	\$7,043.4	\$7,065.5	\$6,738.9	\$7,125.0	\$7,070.4	\$7,012.1	\$6,917.5	\$6,757.0
General Fund Expenses	\$7,041.8	\$6,430.2	\$6,687.4	\$6,954.9	\$7,233.1	\$7,522.4	\$7,823.3	\$8,136.3	\$8,461.7	\$8,800.2	\$9,152.2
Budget Surplus/Shortfall	\$1,940.0	\$1,787.5	\$1,055.4	\$88.5	\$167.6	\$783.5	\$698.3	\$1,065.9	\$1,449.6	\$1,882.7	\$2,395.2
Reserve Balances (\$millions)											
CBRF Main Account Balance End of Year	\$5,408.7	\$5,615.9	\$5,830.2	\$6,051.9	\$6,281.3	\$6,518.6	\$6,764.1	\$7,018.0	\$7,280.8	\$7,552.6	\$6,703.9
CBRF Subaccount Balance End of Year	\$4,972.2	\$5,323.6	\$5,700.0	\$6,102.9	\$6,534.4	\$6,996.3	\$7,490.9	\$8,020.4	\$8,587.4	\$9,194.5	\$9,844.4
CBRF Total	\$10,380.9	\$10,939.5	\$11,530.2	\$12,154.8	\$12,815.6	\$13,514.9	\$14,254.9	\$15,038.4	\$15,868.2	\$16,747.0	\$16,548.3
Statutory Budget Reserve Balance	\$4,402.1	\$6,189.5	\$7,245.0	\$7,333.5	\$7,165.9	\$6,382.4	\$5,684.1	\$4,618.2	\$3,168.6	\$1,285.9	\$0.0
TOTAL RESERVES	\$14,783.0	\$17,129.1	\$18,775.2	\$19,488.3	\$19,981.6	\$19,897.3	\$19,939.0	\$19,656.6	\$19,036.7	\$18,033.0	\$16,548.3

Source: Office of Management and Budget FY2013 10-Year  
Plan (p. 14)

# Scenario 2: Revenue@\$90 oil FY2013 Governor's Budget plus 3% Annual Growth beginning FY2014

## GF Revenue versus Appropriations FY12 to FY22

Oil at \$90 beginning FY2013 with 3% GF Growth beginning FY 2014



**Source: Office of Management and Budget FY2013 10-Year  
Plan (p. 11)**

# Scenario 2: Revenue@\$90 oil FY2013

## Governor's Budget plus 3% Annual Growth beginning FY2014

Oil Price & Production	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21	FY22
Fall 2011 forecast ANS West Coast (\$/bbl)	\$108.98	\$90.00	\$90.00	\$90.00	\$90.00	\$90.00	\$90.00	\$90.00	\$90.00	\$90.00	\$90.00
Fall 2011 forecast ANS production (mmbbl./day)	0.574	0.555	0.561	0.538	0.550	0.549	0.544	0.515	0.486	0.458	0.432
Revenue vs. Spending (\$millions)											
General Fund Revenues <sup>1/</sup>	\$8,981.8	\$5,775.3	\$5,414.2	\$4,926.1	\$5,049.8	\$5,001.6	\$5,056.2	\$4,807.1	\$4,574.3	\$4,331.3	\$4,041.2
General Fund Expenses	\$7,041.8	\$6,430.2	\$6,623.1	\$6,821.8	\$7,026.5	\$7,237.2	\$7,454.4	\$7,678.0	\$7,908.3	\$8,145.6	\$8,390.0
Budget Surplus/Shortfall	\$1,940.0	\$654.9	\$1,208.9	\$1,895.7	\$1,976.6	\$2,235.7	\$2,398.2	\$2,870.9	\$3,334.1	\$3,814.3	\$4,348.7
Reserve Balances (\$millions)											
CBRF Main Account Balance End of Year	\$5,408.7	\$5,615.9	\$5,830.2	\$6,051.9	\$4,922.3	\$2,835.4	\$510.9	\$0.0	\$0.0	\$0.0	\$0.0
CBRF Subaccount Balance End of Year	\$4,972.2	\$5,323.6	\$5,700.0	\$6,102.9	\$6,534.4	\$6,996.3	\$7,490.9	\$5,801.2	\$2,771.7	\$0.0	\$0.0
CBRF Total	\$10,380.9	\$10,939.5	\$11,530.2	\$12,154.8	\$11,456.7	\$9,831.7	\$8,001.8	\$5,599.7	\$2,771.7	\$0.0	\$0.0
Statutory Budget Reserve Balance	\$4,402.1	\$3,747.2	\$2,538.2	\$642.5	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
TOTAL RESERVES	\$14,783.0	\$14,686.7	\$14,068.4	\$12,797.4	\$11,456.7	\$9,831.7	\$8,001.8	\$5,599.7	\$2,771.7	\$0.0	\$0.0

Source: Office of Management and Budget FY2013 10-Year Plan (p. 12)



... maybe even  
Scenario 2 is  
too optimistic



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## Shell sees oil lows of \$70 in 2012 volatility

Oil giant reports 54% jump in 2011 profits despite tough final quarter

BY EMILY GOSDEN, THE TELEGRAPH FEBRUARY 2, 2012

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Shell's chief executive, Peter Voser, outlined an aggressive long-term growth strategy, focused on "upstream" exploration and production. He said the strategy would help Shell ride out volatility and increase cash flow by up to 50pc over the next four years. It would spend



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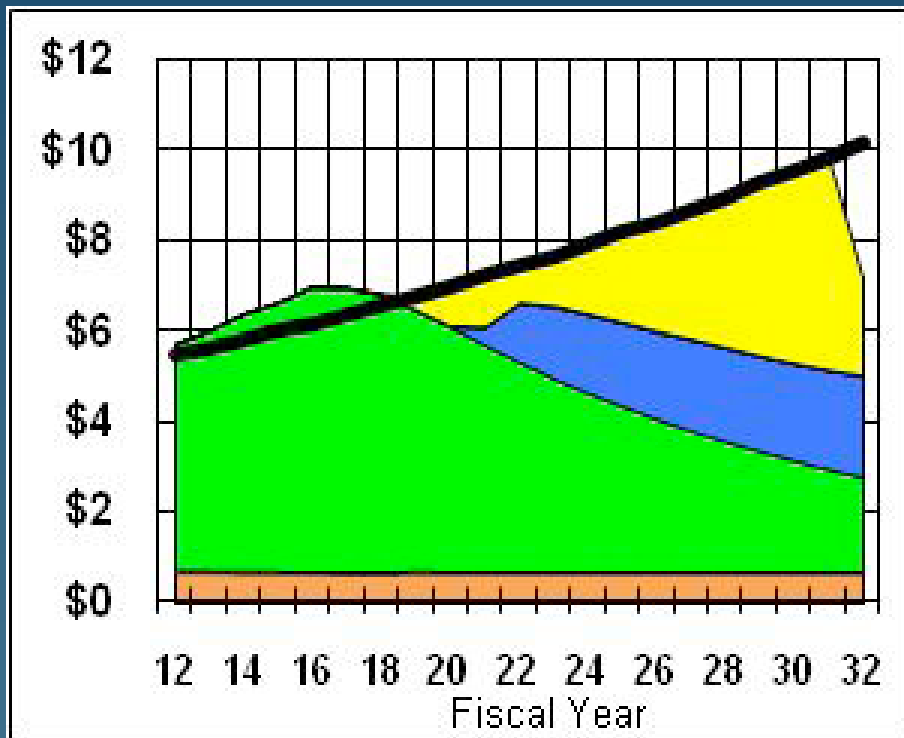
# Another perspective ...

- The Administration's 10-year forecast only goes out to 2022
- Last year, Scott Goldsmith of UAA's Institute of Social and Economic Research (ISER) extended last year's forecast on out another ten years ...

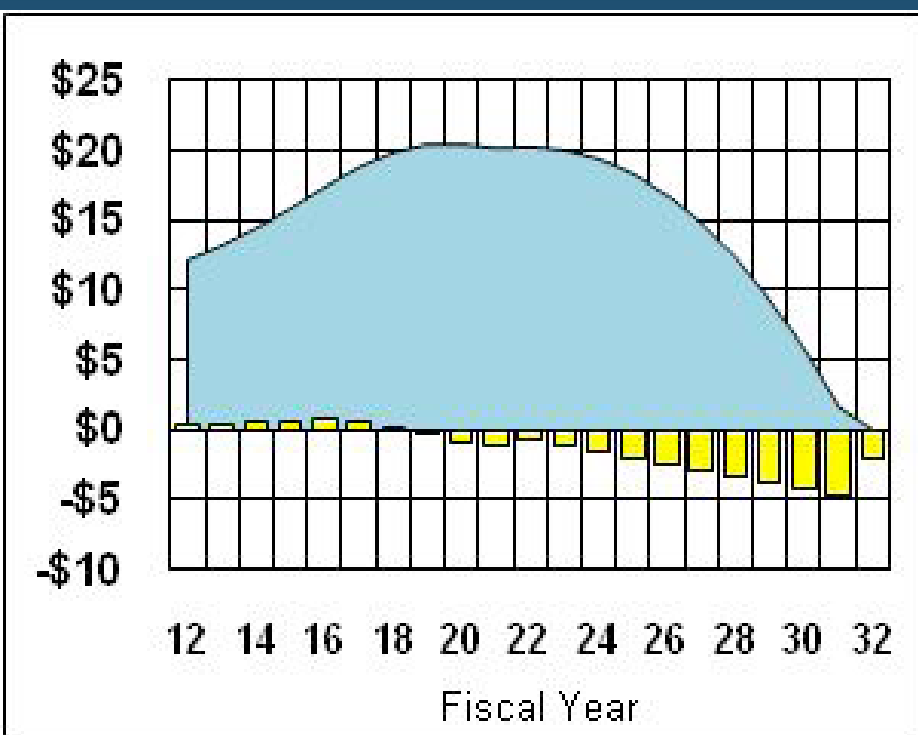
# OMB FISCAL PLAN—EXTENDED

(2012 Billion \$, includes gas monetization)

## GF Projection



## Financial Reserve

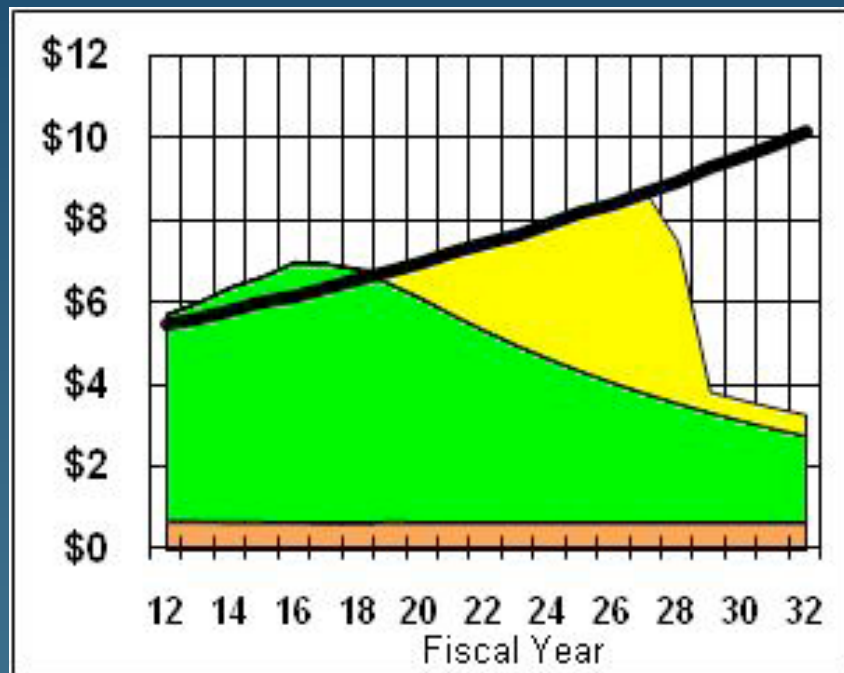


**Source: *Revising the State Fiscal Plan to Account for Petroleum Wealth*,  
Web Note No. 9, Institute of Social and Economic Research  
University of Alaska Anchorage by Scott Goldsmith (p. 5, 2011)**

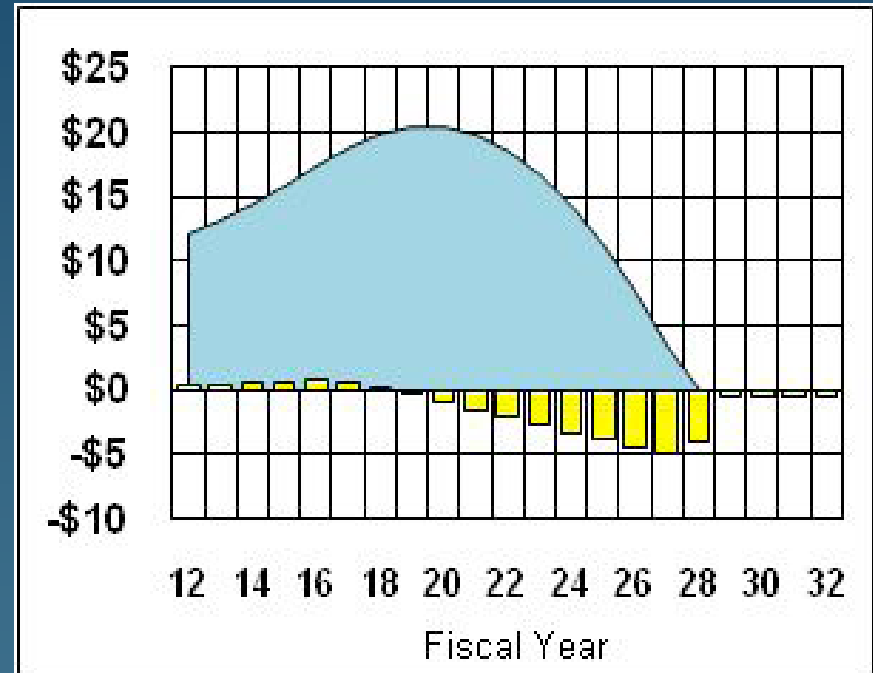
# OMB FISCAL PLAN—EXTENDED

(2012 Billion \$, no gas)

## GF Projection



## Financial Reserve



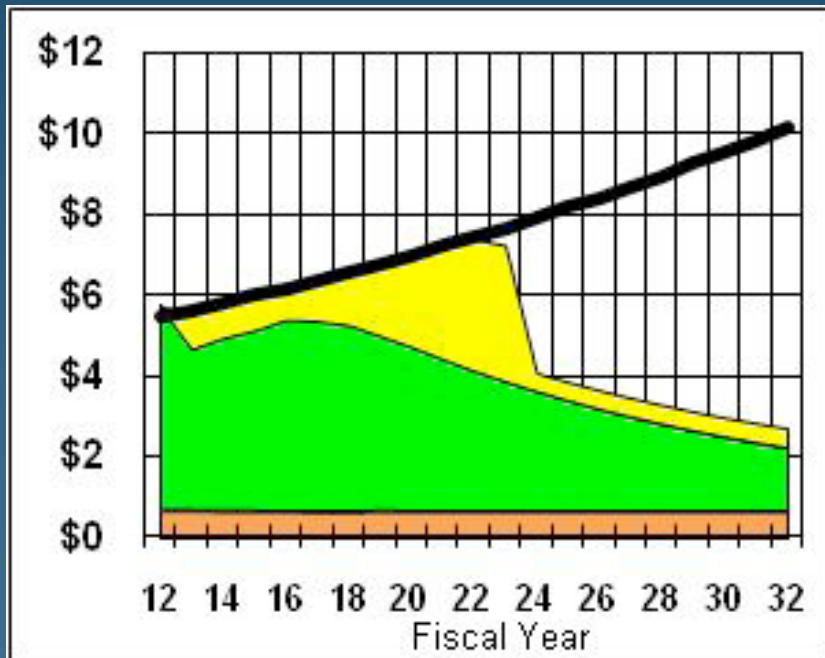
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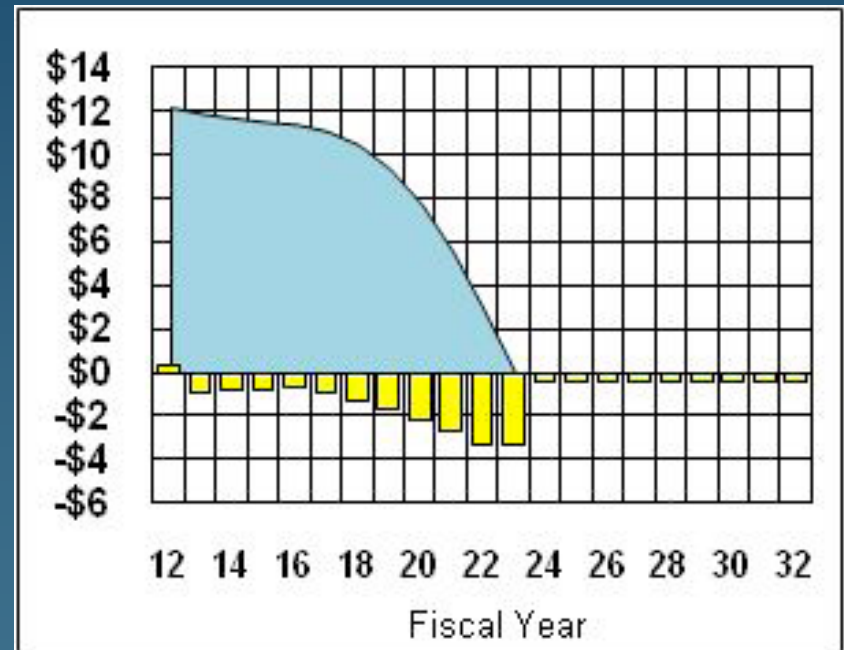
# OMB FISCAL PLAN—EXTENDED

(2012 Billion \$, no gas/75% of oil price)

## GF Projection



## Financial Reserve



**Source:** *Revising the State Fiscal Plan to Account for Petroleum Wealth, Web Note No. 9, Institute of Social and Economic Research University of Alaska Anchorage by Scott Goldsmith (p. 5, 2011)*

# Other Consequences of the Decision

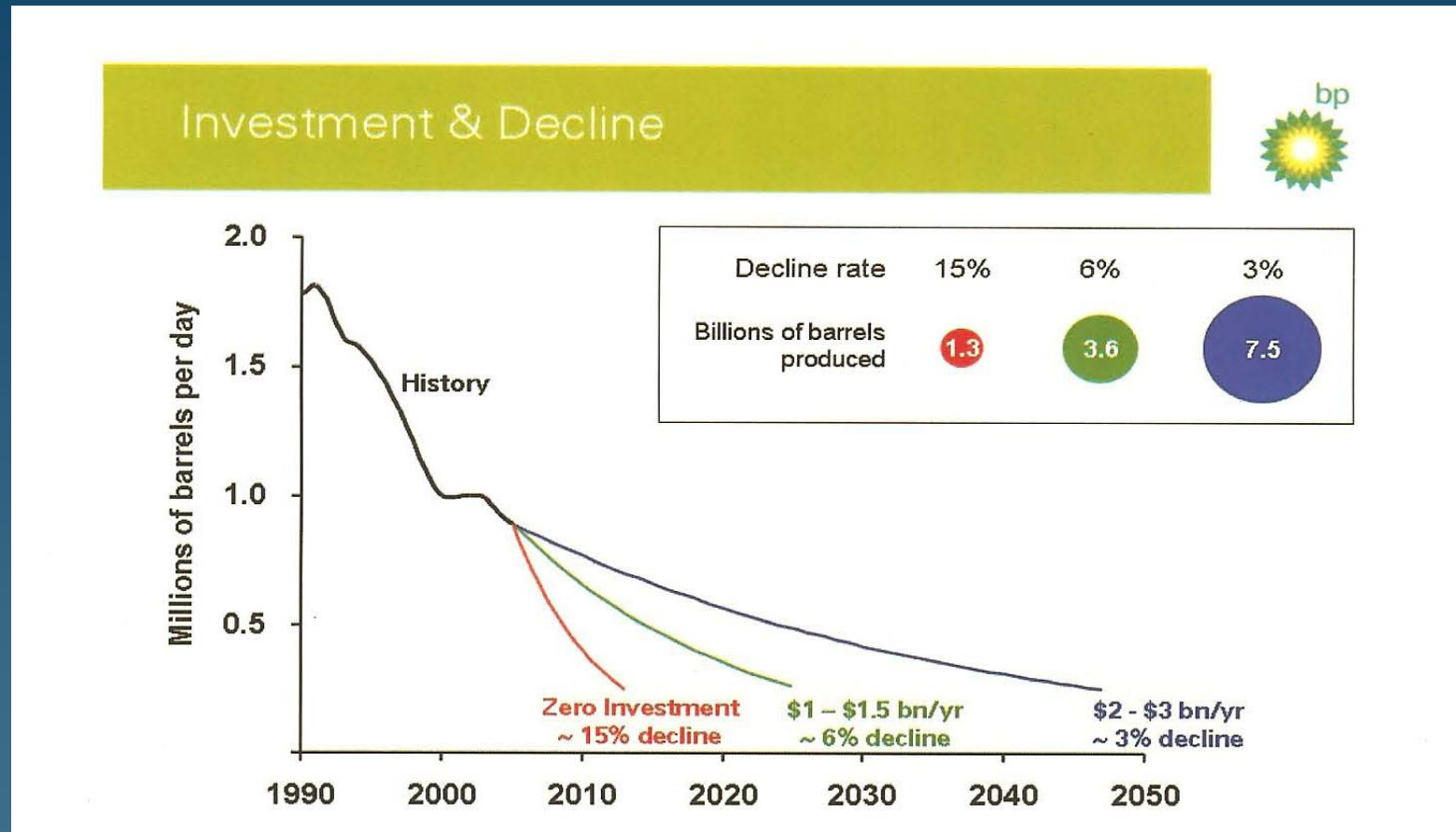
- Increases TAPS rates
  - Roughly 25% of current TAPS rates are to recover ad valorem taxes; increased taxes, increased rates
- Decision disproportionately benefits NSB, Fairbanks and Valdez; hurts State
  - Increased TAPS rates reduce royalty and production taxes
- Significant additional tax hike on industry
  - Reinforces perception of unpredictable and litigious Alaska business environment

# Conclusion

- Judge Gleason's Decision ...
  - ... says nothing about which decline curve Alaska is on
  - ... at most, the decision merely says that the tail end of the decline curve may be extended longer than some have previously forecast
- In short, the person that turns the lights off on Alaska's economy can stay a few more years, but the remainder will have left long before

# Back Up Slides

# Alaska's Three Alternative Futures

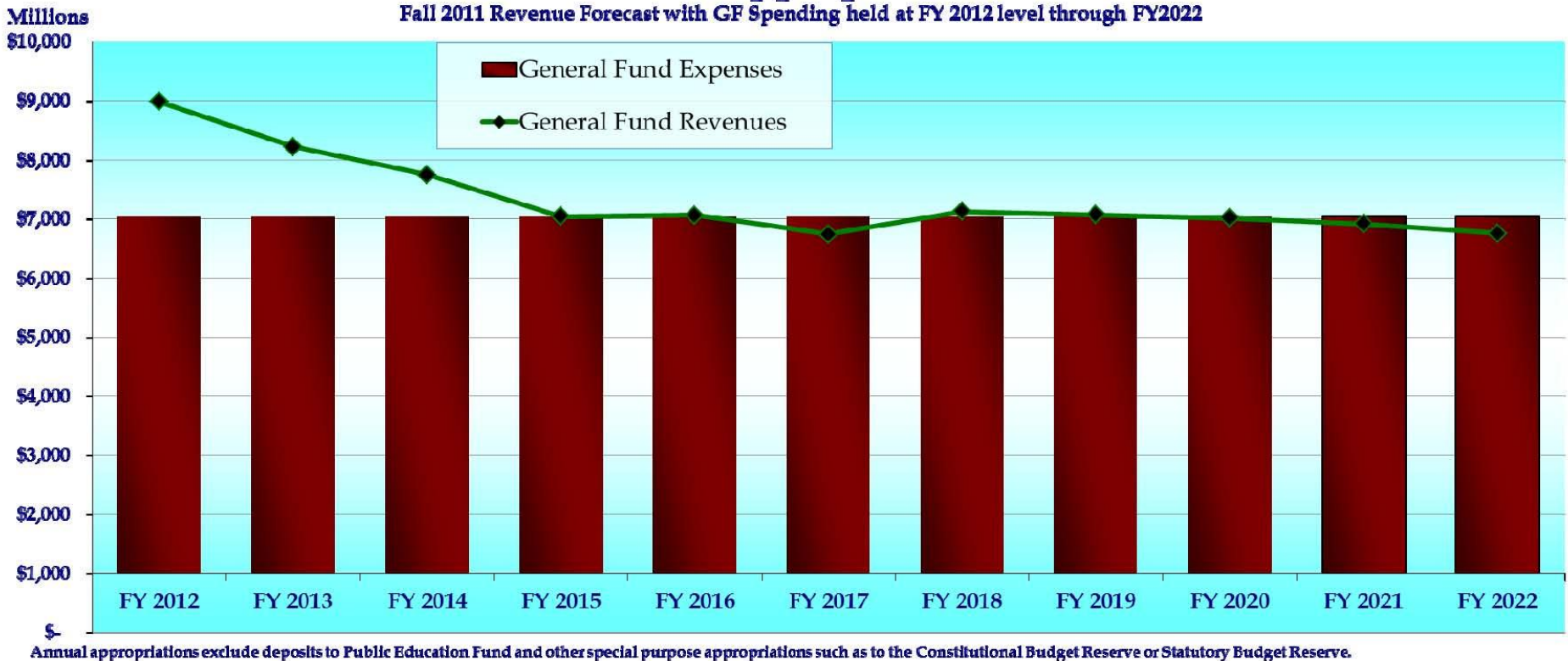


**Source:** BP Presentation on Proposed PPT  
(Alaska State Legislature House & Senate Resources  
Committees 2006)

# Scenario 1: General Fund Spending held at FY2012 level (\$7.0 billion) through FY2022

## GF Revenue versus Appropriations FY12 to FY22

Fall 2011 Revenue Forecast with GF Spending held at FY 2012 level through FY2022



Source: Office of Management and Budget FY2013  
10-Year Plan (p. 9)

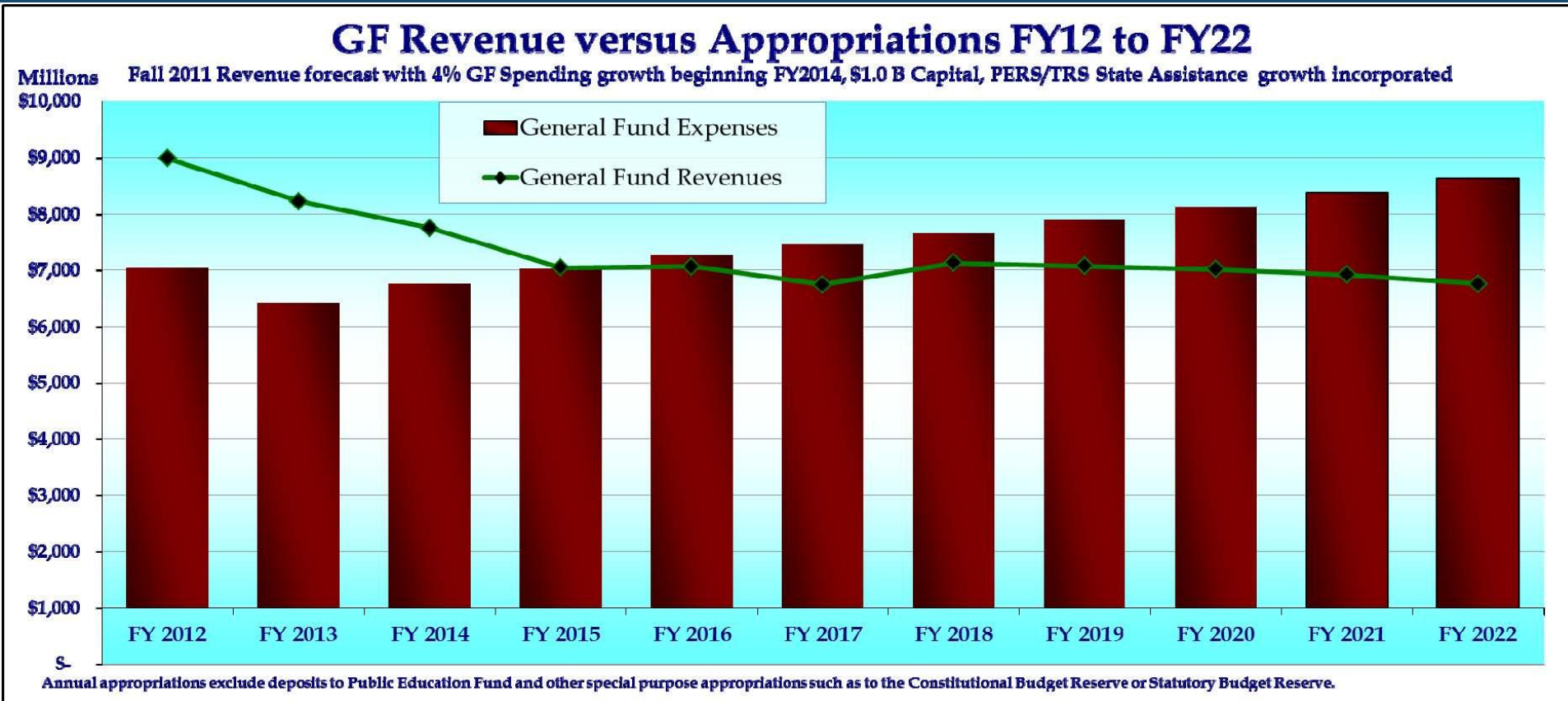
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Fall 2011 forecast ANS production (mmbbl./day)	0.574	0.555	0.561	0.538	0.550	0.549	0.544	0.515	0.486	0.458	0.432
Revenue vs. Spending (\$millions)											
General Fund Revenues <sup>1/</sup>	\$8,981.8	\$8,217.7	\$7,742.8	\$7,043.4	\$7,065.5	\$6,738.9	\$7,125.0	\$7,070.4	\$7,012.1	\$6,917.5	\$6,757.0
General Fund Expenses	\$7,041.8	\$7,041.8	\$7,041.8	\$7,041.8	\$7,041.8	\$7,041.8	\$7,041.8	\$7,041.8	\$7,041.8	\$7,041.8	\$7,041.8
Budget Surplus/Shortfall	\$1,940.0	\$1,175.9	\$701.0	\$1.6	\$23.7	\$302.9	\$83.2	\$28.6	\$29.7	\$124.3	\$284.8
Reserve Balances (\$millions)											
CBRF Main Account Balance End of Year	\$5,408.7	\$5,615.9	\$5,830.2	\$6,051.9	\$6,281.3	\$6,518.6	\$6,764.1	\$7,018.0	\$7,280.8	\$7,552.6	\$7,833.8
CBRF Subaccount Balance End of Year	\$4,972.2	\$5,323.6	\$5,700.0	\$6,102.9	\$6,534.4	\$6,996.3	\$7,490.9	\$8,020.4	\$8,587.4	\$9,194.5	\$9,844.4
CBRF Total	\$10,380.9	\$10,939.5	\$11,530.2	\$12,154.8	\$12,815.6	\$13,514.9	\$14,254.9	\$15,038.4	\$15,868.2	\$16,747.0	\$17,678.2
Statutory Budget Reserve Balance	\$4,402.1	\$5,577.9	\$6,279.0	\$6,280.6	\$6,304.3	\$6,001.5	\$6,084.7	\$6,113.2	\$6,083.5	\$5,959.2	\$5,674.4
TOTAL RESERVES	\$14,783.0	\$16,517.5	\$17,809.2	\$18,435.5	\$19,120.0	\$19,516.3	\$20,339.6	\$21,151.7	\$21,951.7	\$22,706.3	\$23,352.6

Source: Office of Management and Budget FY2013  
10-Year Plan (p. 10)



# Scenario 4: FY2013 Governor's Budget with 4% Annual Agency Growth, Capital at \$1.0 B, PERS/TRS



Source: Office of Management and Budget FY2013 10-Year Plan (p. 15)



# Scenario 4: FY2013 Governor's Budget with 4% Annual Agency Growth, Capital at \$1.0 B, PERS/TRS

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General Fund Expenses	\$7,041.8	\$6,430.2	\$6,763.6	\$7,029.2	\$7,271.3	\$7,463.1	\$7,663.3	\$7,890.1	\$8,129.3	\$8,378.4	\$8,639.7
Budget Surplus/Shortfall	\$1,940.0	\$1,787.5	\$979.2	\$14.2	\$205.8	\$724.2	\$538.3	\$819.7	\$1,117.2	\$1,460.9	\$1,882.7
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Statutory Budget Reserve Balance	\$4,402.1	\$6,189.5	\$7,168.8	\$7,183.0	\$6,977.3	\$6,253.0	\$5,714.7	\$4,895.0	\$3,777.8	\$2,316.9	\$434.2
TOTAL RESERVES	\$14,783.0	\$17,129.1	\$18,699.0	\$19,337.9	\$19,792.9	\$19,767.9	\$19,969.6	\$19,933.4	\$19,646.0	\$19,064.0	\$18,112.4

Source: Office of Management and Budget FY2013 10-Year  
Plan (p. 16)