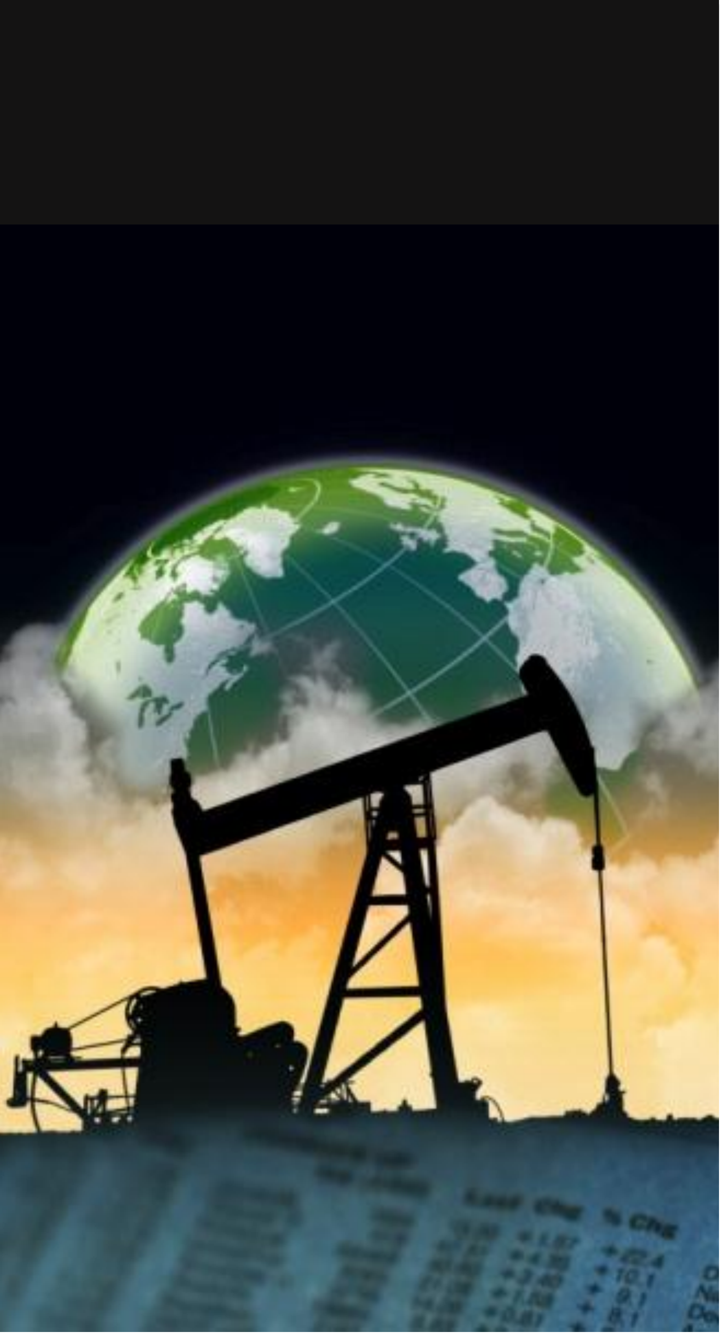


Senate Resources Committee

Alaska Fiscal System Discussion Slides

February 22 2013

Janak Mayer
Manager, Upstream
PFC Energy

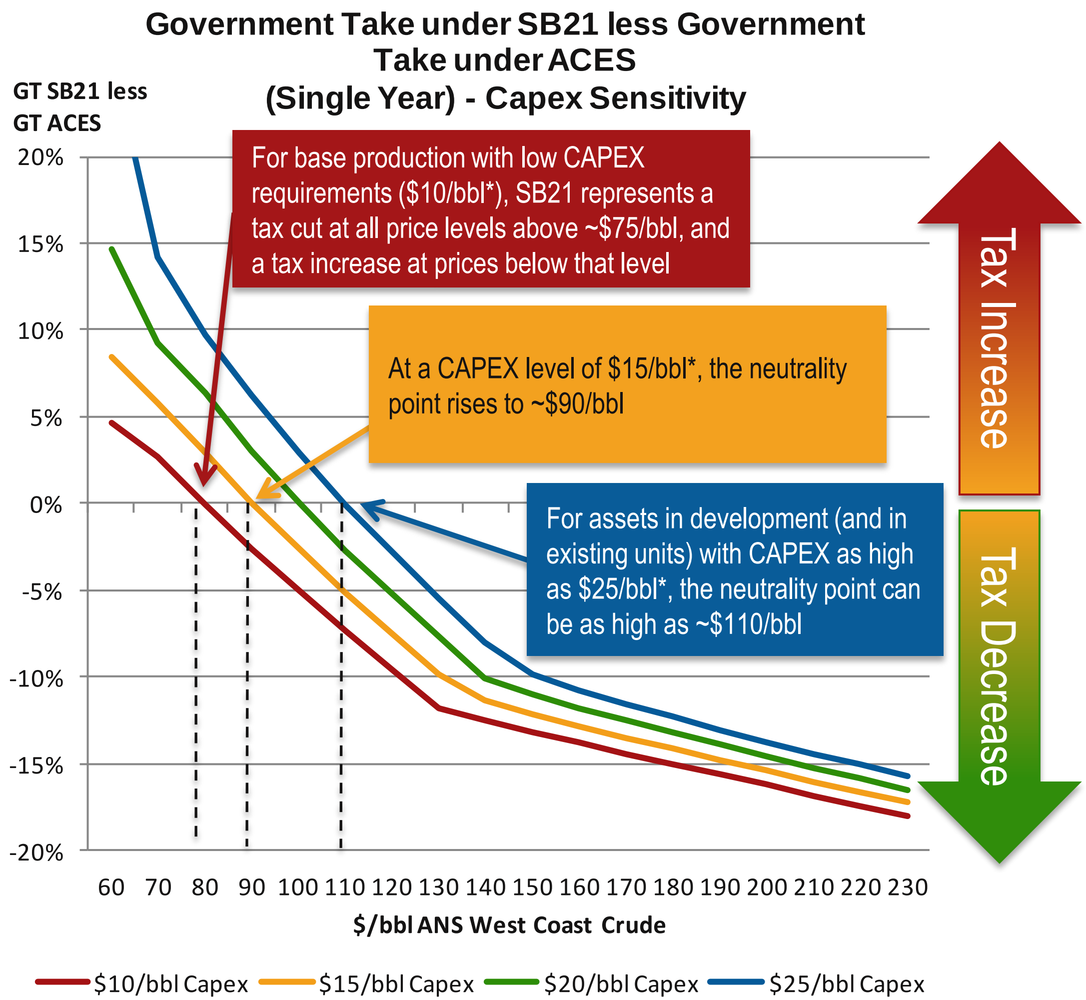
Requested Analysis:

Letter of Intent recommendation for evaluation point 3 – impact of continuing capital credits for well expenditures

Impact of combining well credits with bracketed progressivity

Impact of instead using a 35% base rate tax, combined with a production-based credit of $5/taxable bbl, claimable only in year of production

Government Take under SB21/HB72 and ACES – Capex Sensitivity

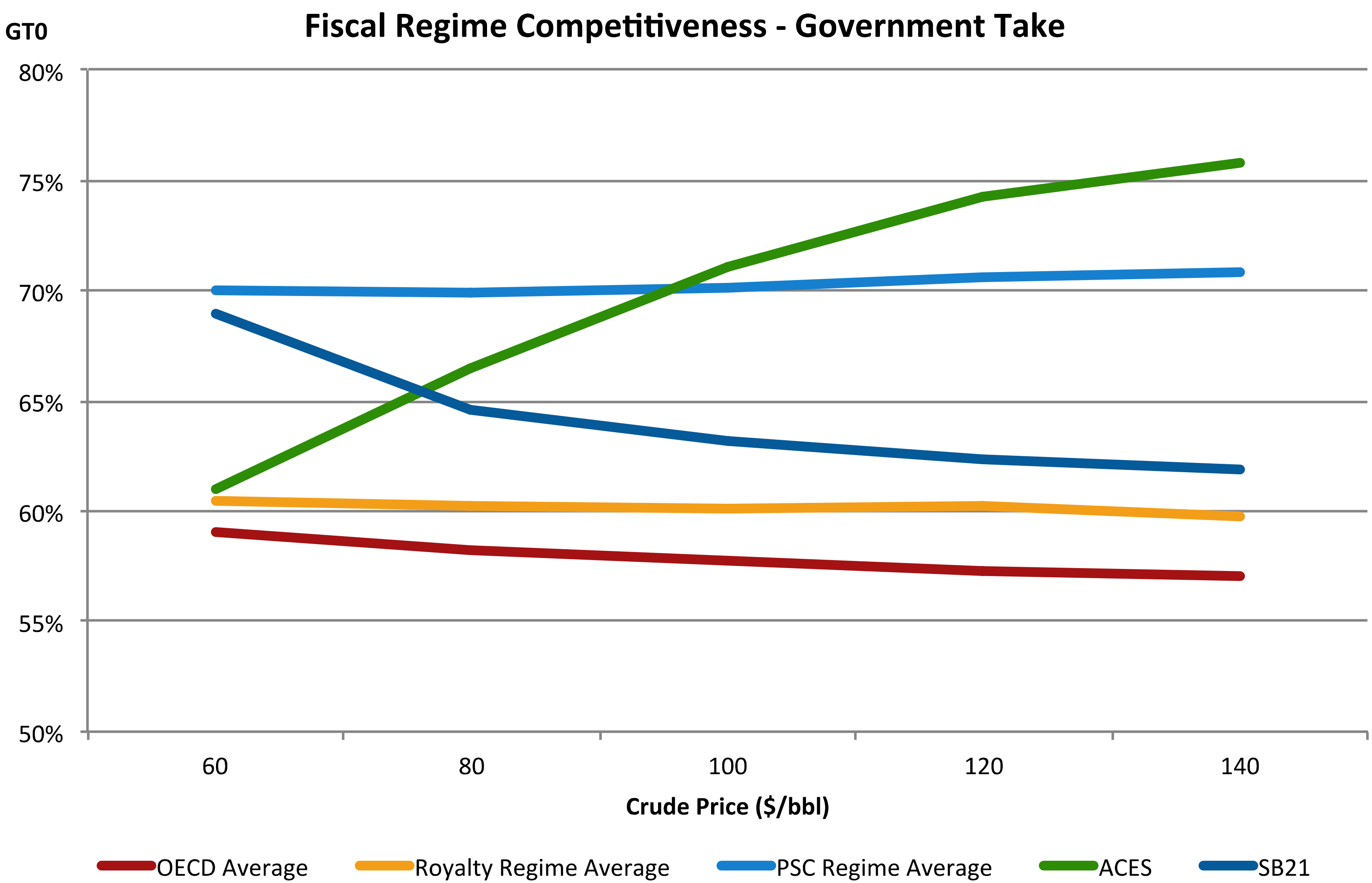


** All CAPEX figures are in gross bbl terms ($15 per gross bbl is roughly equivalent to DOR 2014 average North Slope forecast of $19.6 per bbl net of royalty, when adjusted for gross/net and for capital expenditures by non-taxable entities)*

- •As noted in PFC Energy testimony on 1/31/13, at low oil prices, Relative Government Take under SB 21 is higher than under ACES, due to the impact of low or no progressivity, combined with the elimination of the 20% capital credit under SB 21
- •The **oil price level** at which this occurs is highly **sensitive to annual levels of capital spending**, since CAPEX both reduces the oil price level at which progressivity kicks in under ACES, and determines the size of the available capital credit under ACES
- •Looking at a **single year of production** also slightly raises this neutrality point, since over many years, inflation reduces the real price level at which progressivity starts under ACES
- •For mature, producing assets with a low ongoing CAPEX requirement ($10/bbl), SB21 represents a **reduction in government take at prices above ~$75**, however for capital intensive new developments in existing units, that neutrality **point can be as high as $110/bbl**
- •It is thus important to understand that one impact of the removal of the 20% capital credit under SB 21 is that for companies with high development costs relative to overall production, it **can represent a tax increase at current prices**

PFC Energy

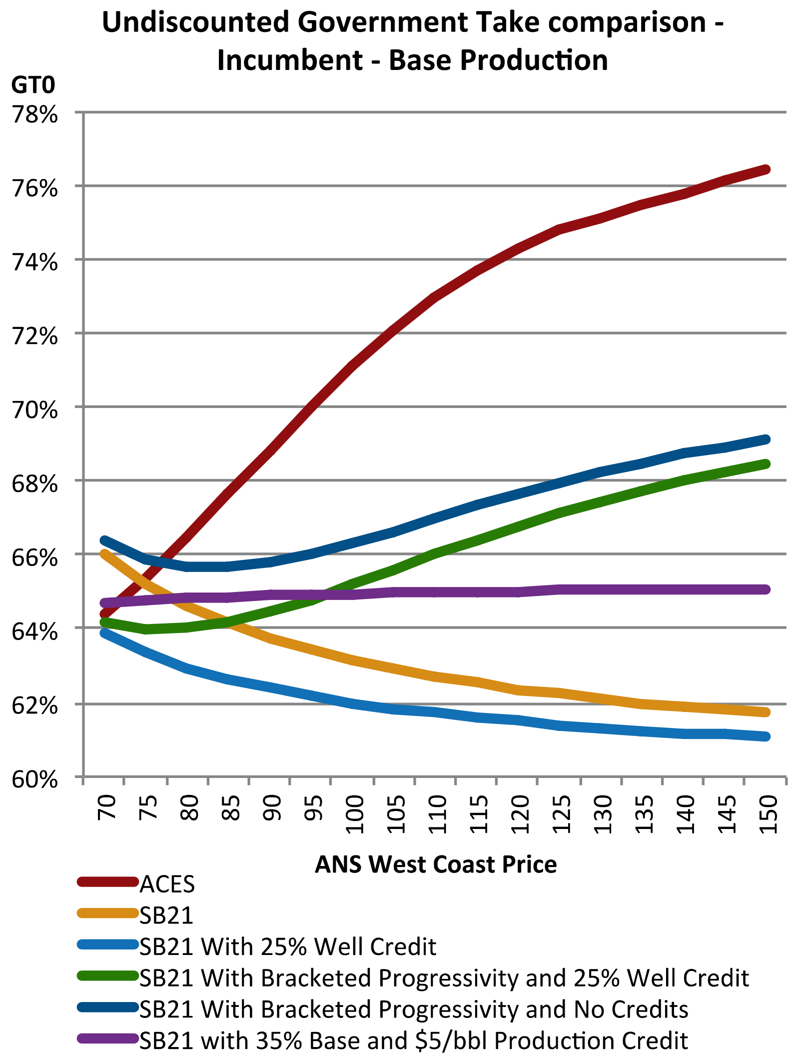
Fiscal Regime Competitiveness

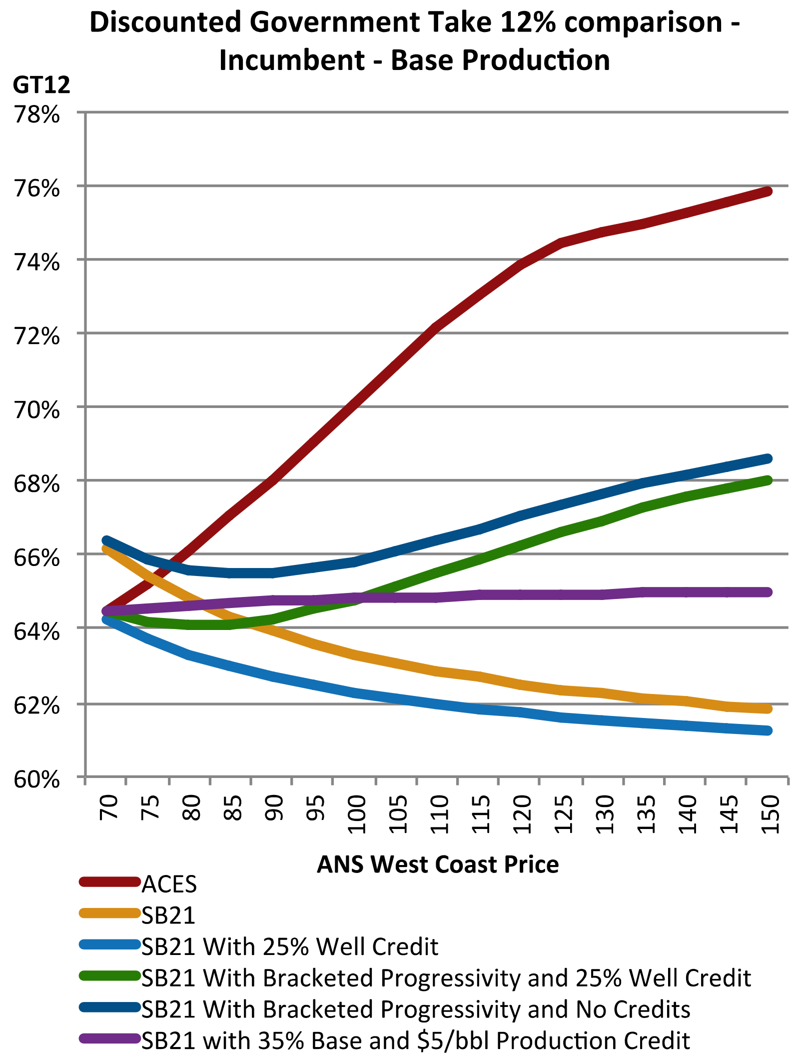


Assumptions

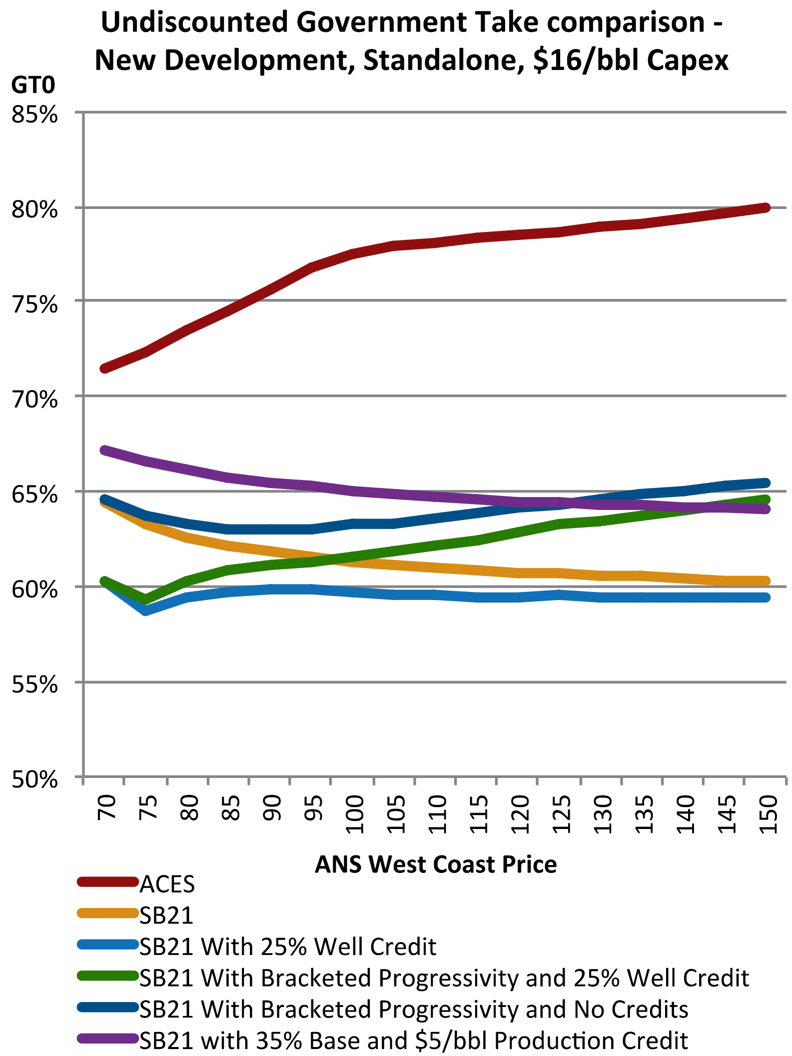
- Well Credit
  - 50% of capex qualifies, credit level 25%
- Bracketed progressivity
  - Thresholds and rates as under HB110:
    - Base tax 25%
    - <$30 PTV/bbl, 0% progressivity
    - $30-$42.5, 2.5% progressivity
    - $42.5-$55 – 7.5% progressivity
    - $55-$67.5 – 12.5% progressivity
    - $67.5-$80 – 17.5% progressivity
    - $80-$92.50 – 22.5% progressivity
    - >$92.50 PTV/bbl – 25% progressivity

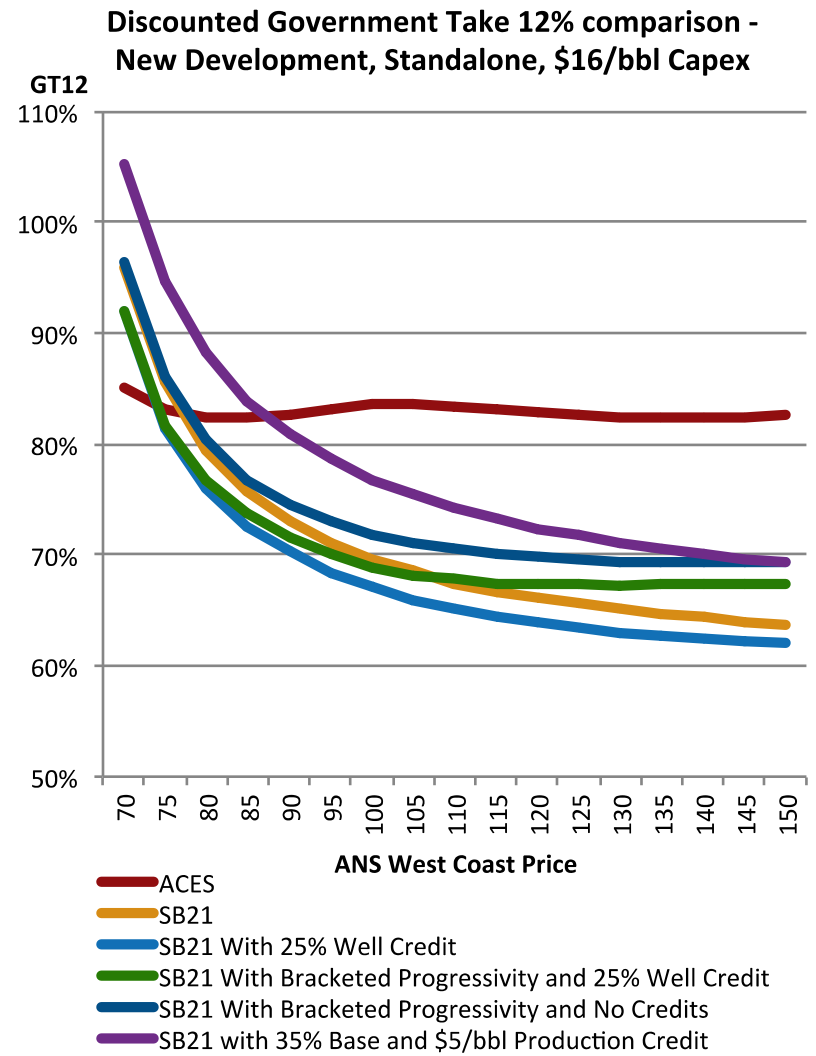
Government Take Comparison
Incumbent, Base Production



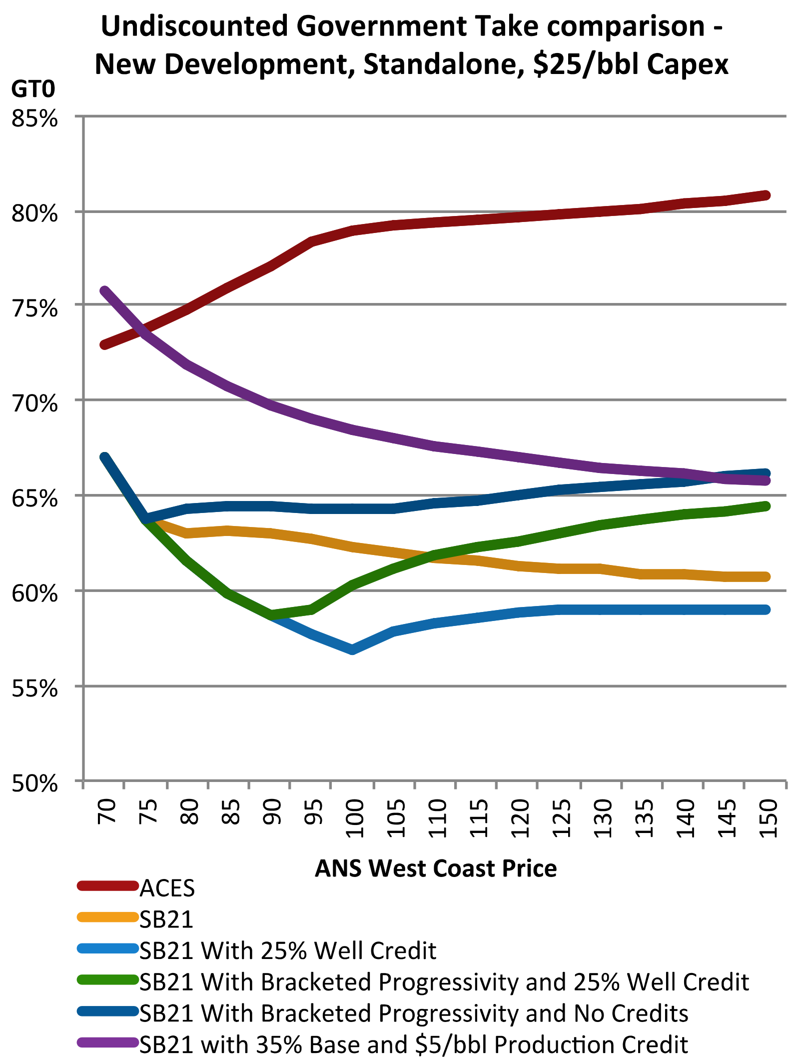


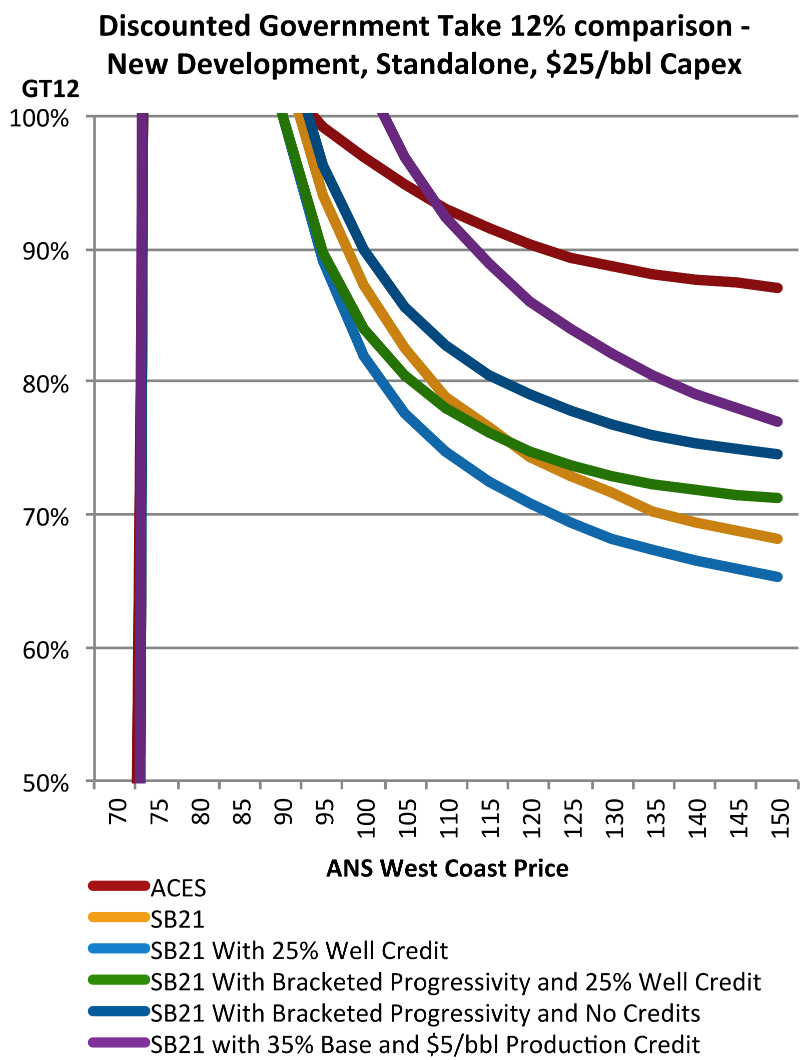
Government Take Comparison
$16/bbl New Development, Standalone



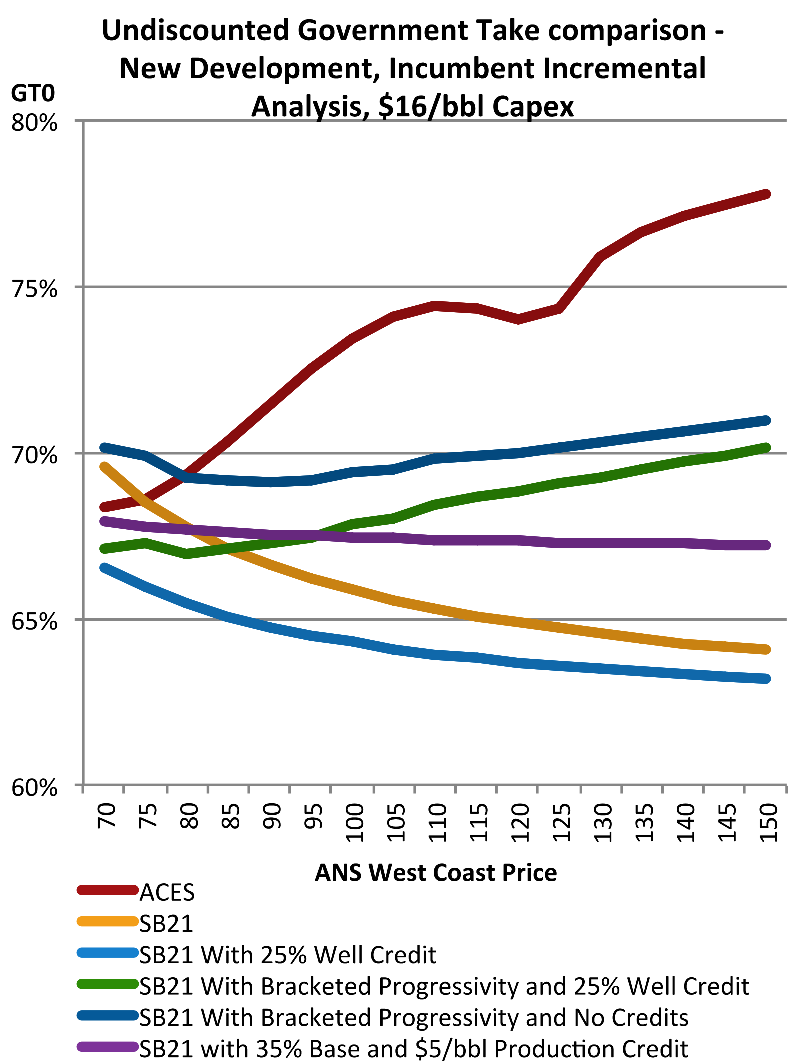


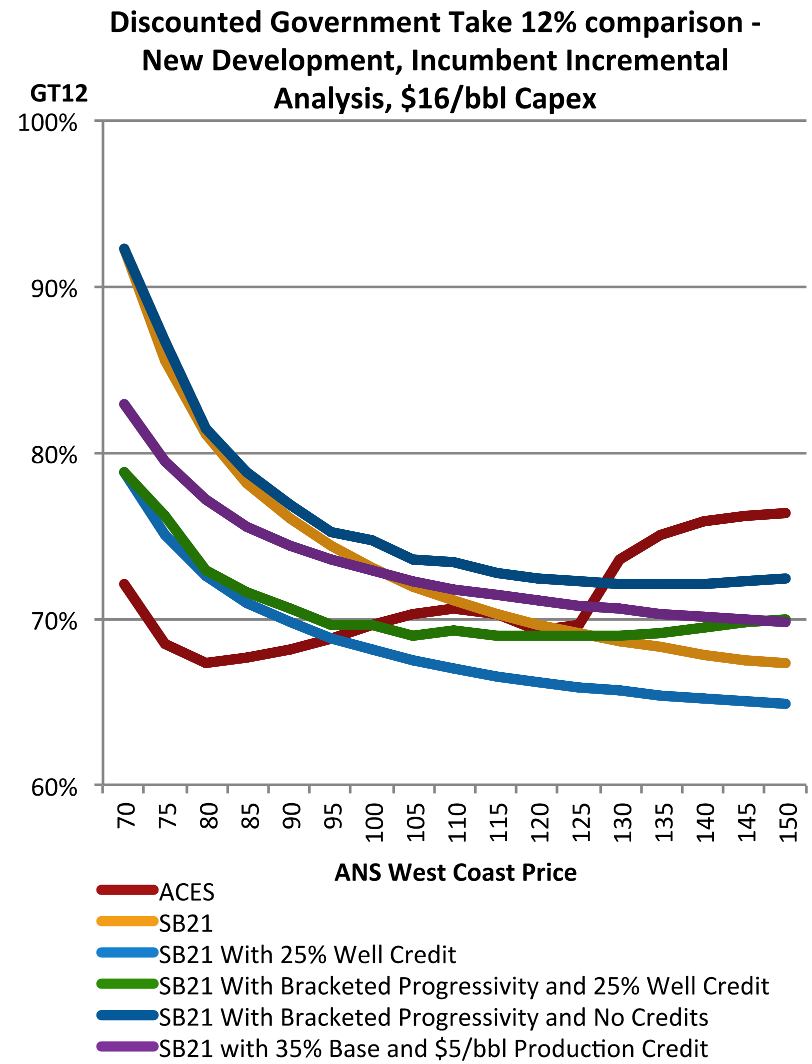
Government Take Comparison
$25/bbl New Development (with GRE), Standalone



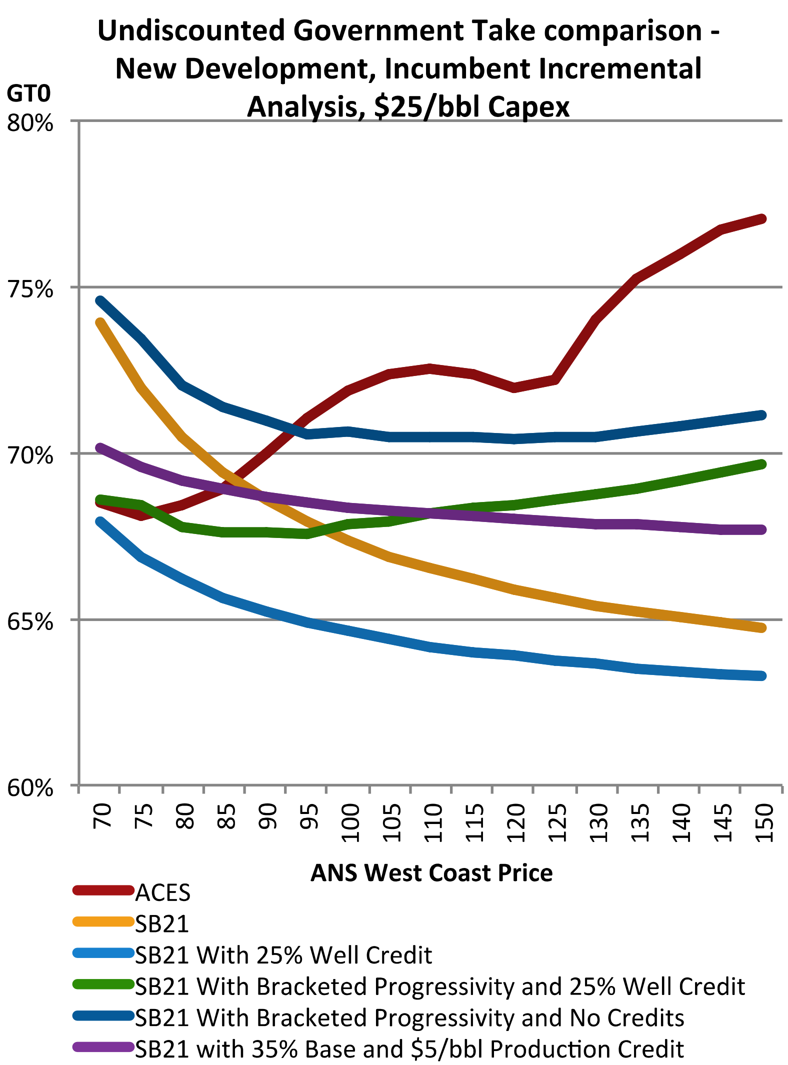


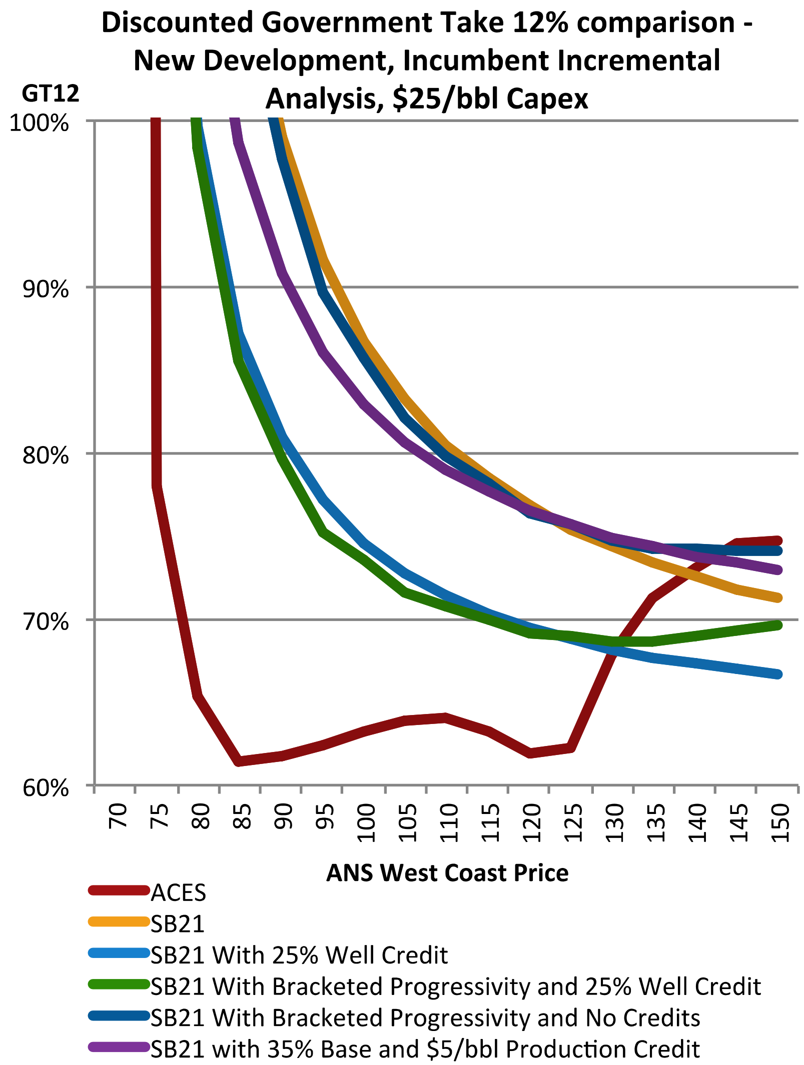
Government Take Comparison
$16/bbl New Development, Incumbent Producer Incremental Analysis



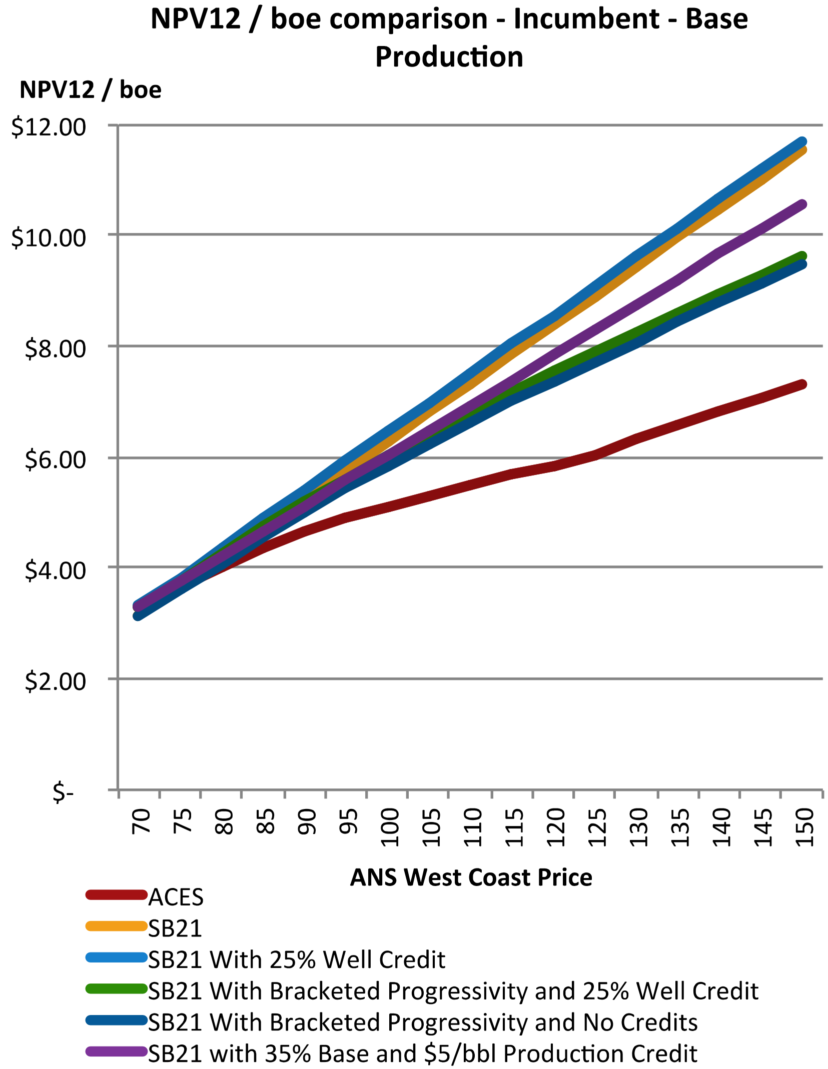


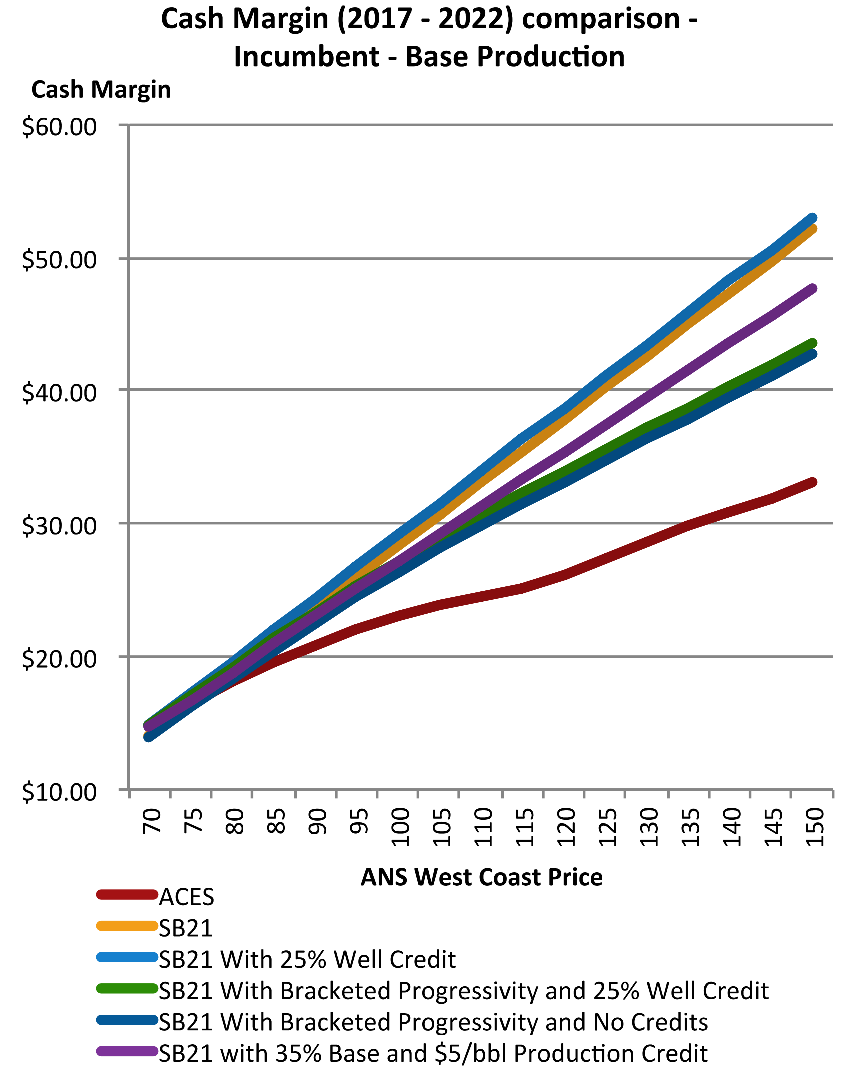
Government Take Comparison
$25/bbl New Development, Incumbent Producer Incremental Analysis



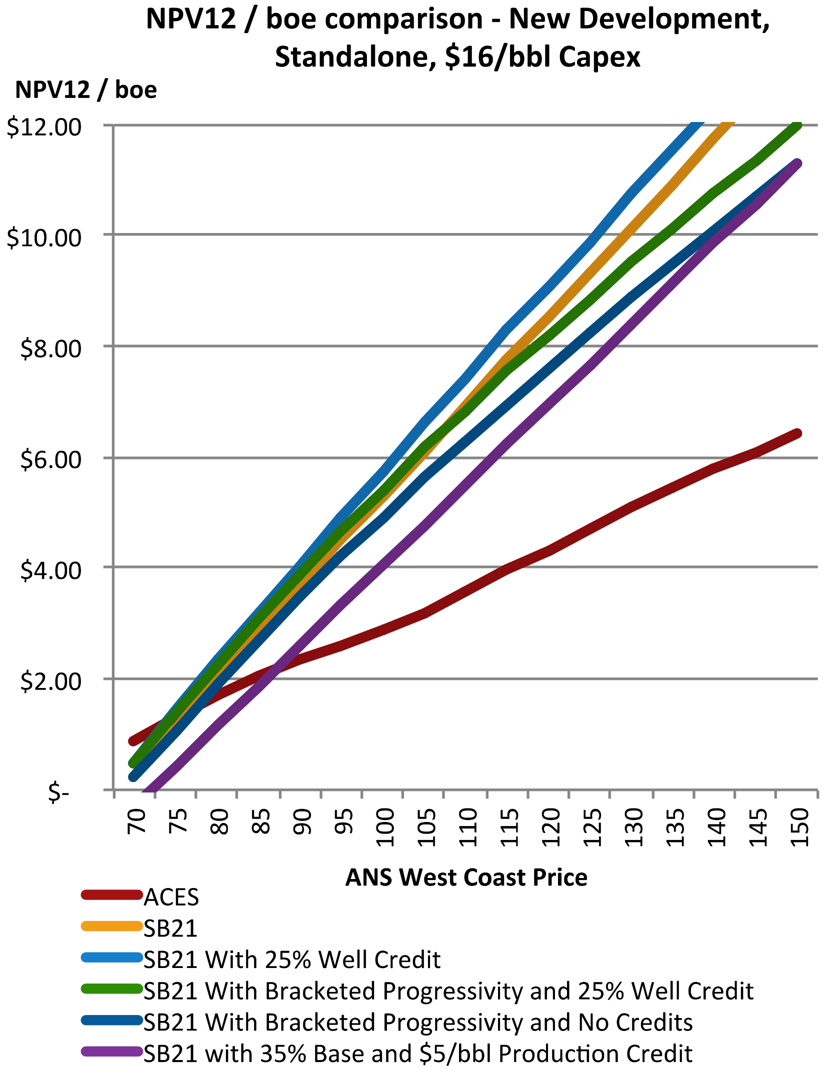


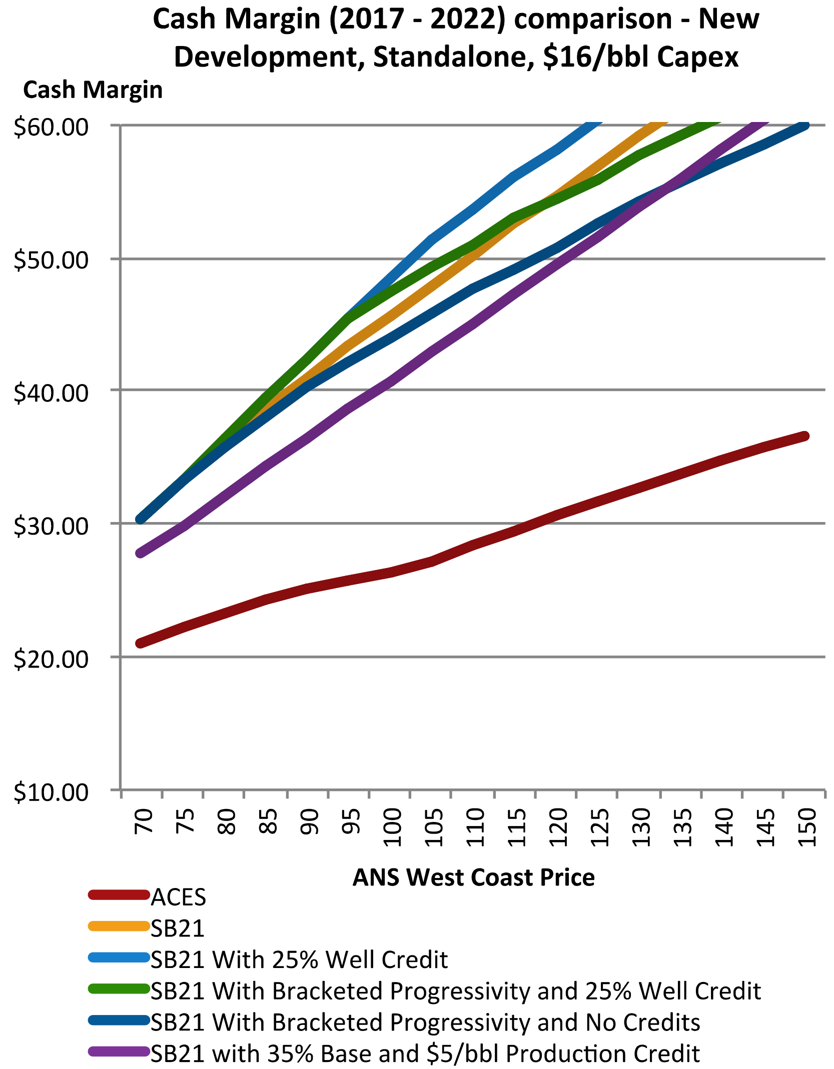
NPV12/bbl & Cash Margin Comparison
Incumbent, Base Production



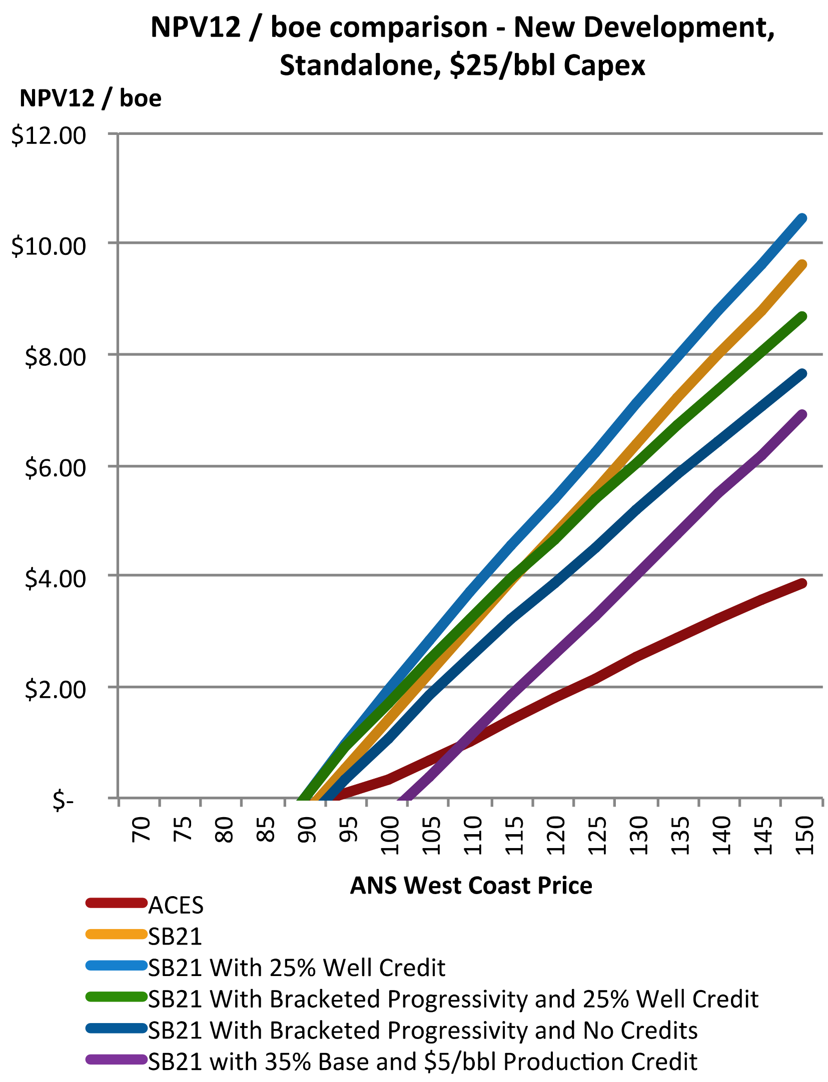


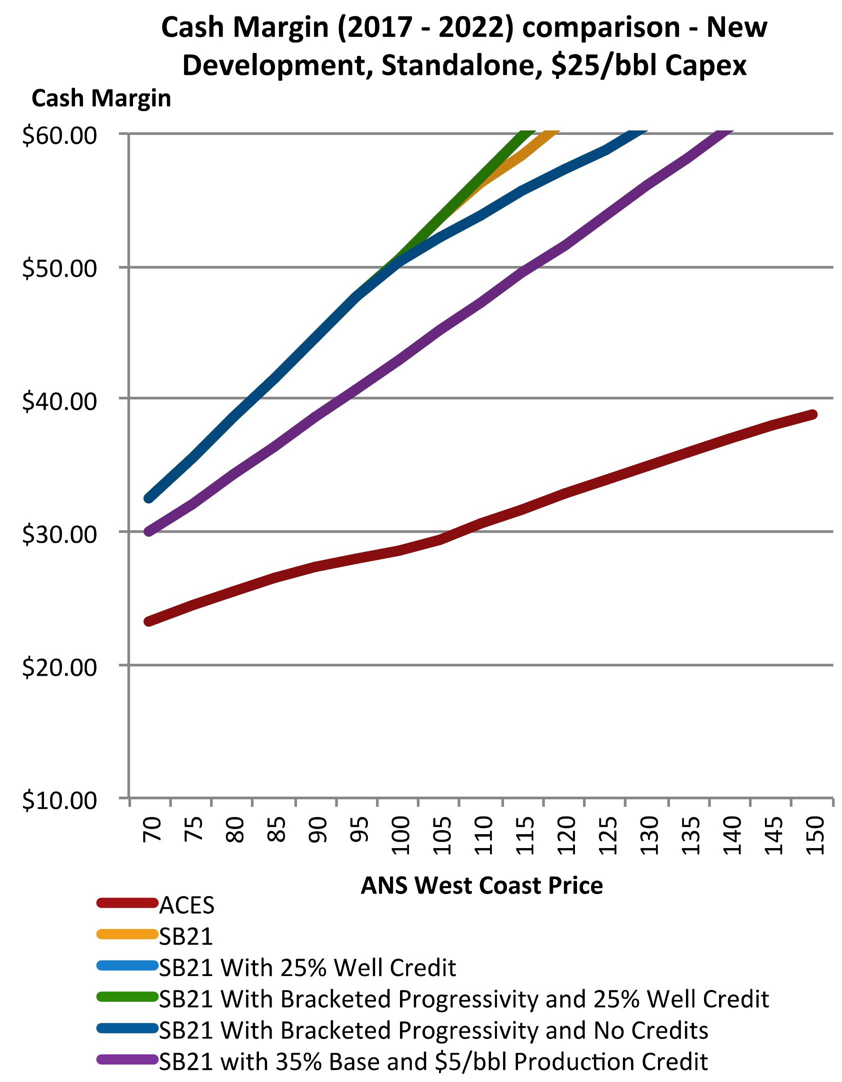
NPV12/bbl & Cash Margin Comparison
$16/bbl New Development, Standalone





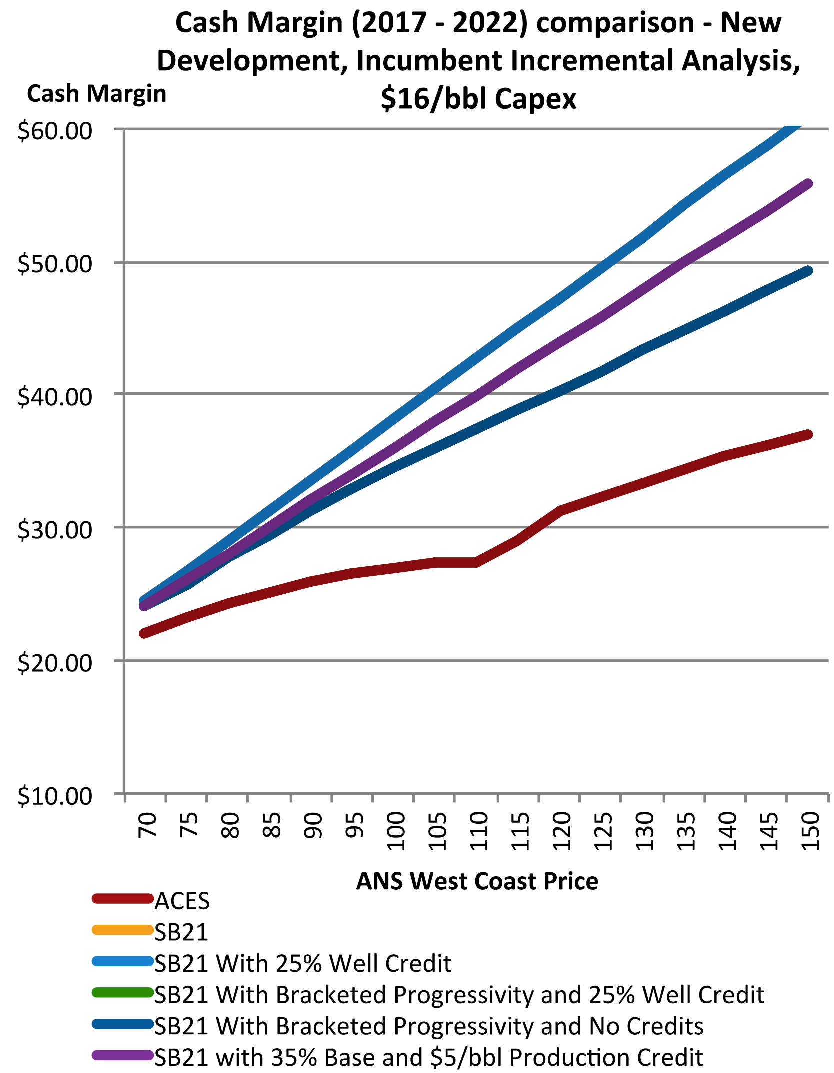
NPV12/bbl & Cash Margin Comparison
$25/bbl New Development, Standalone



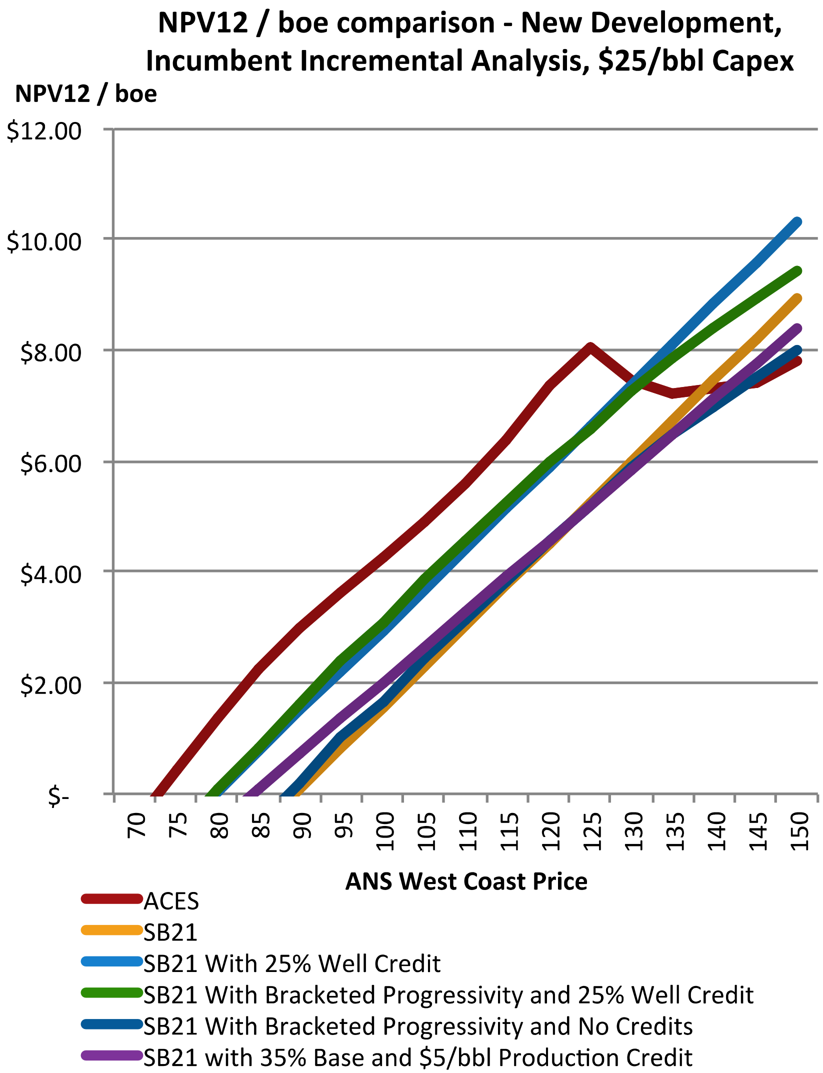


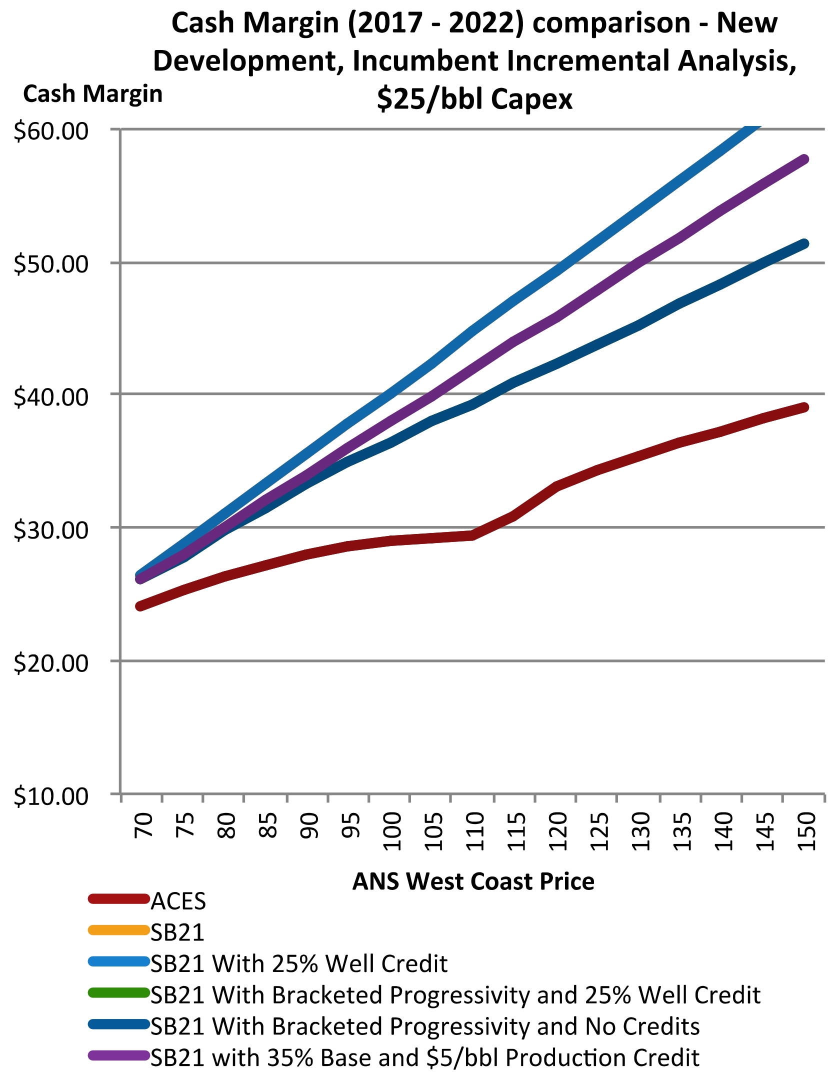
NPV12/bbl & Cash Margin Comparison

$16/bbl New Development, Incumbent Producer Incremental Analysis

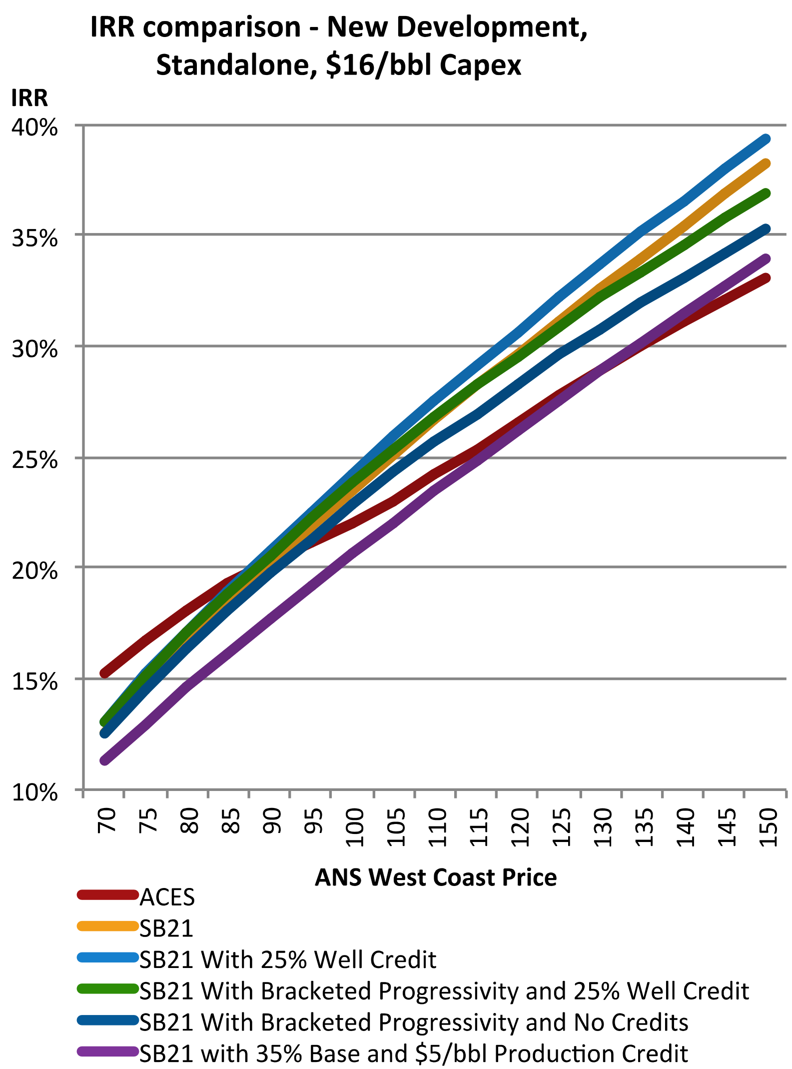


NPV12/bbl & Cash Margin Comparison
$25/bbl New Development, Incumbent Producer Incremental Analysis

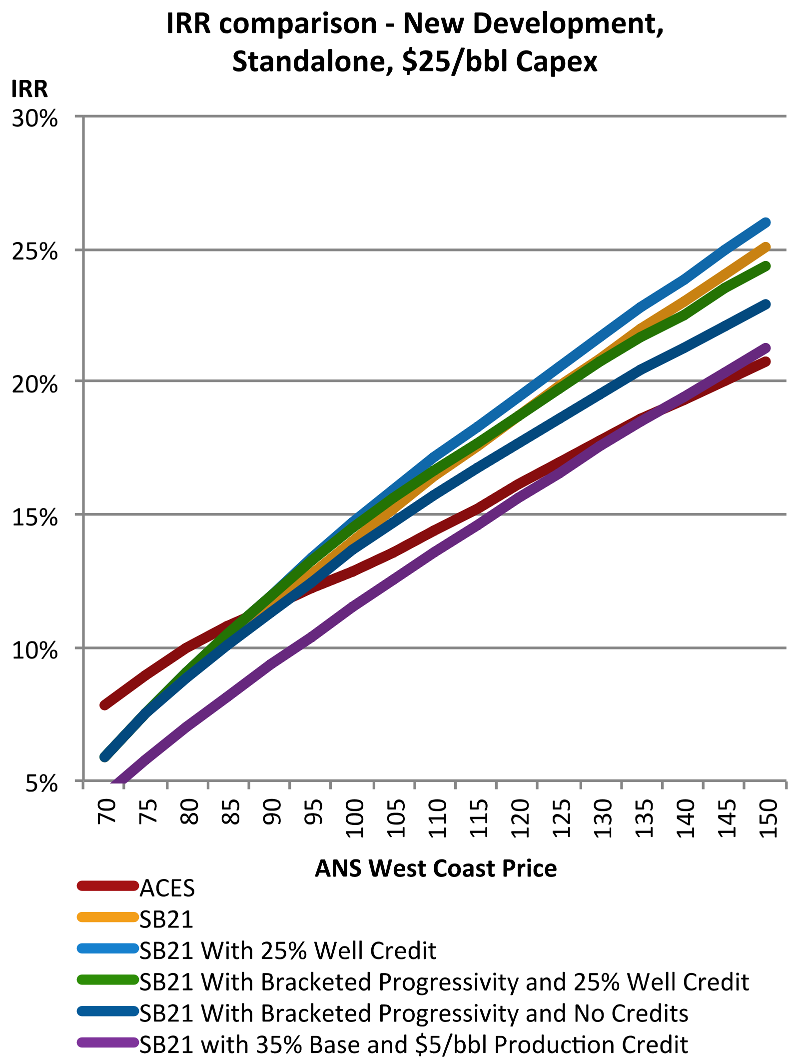




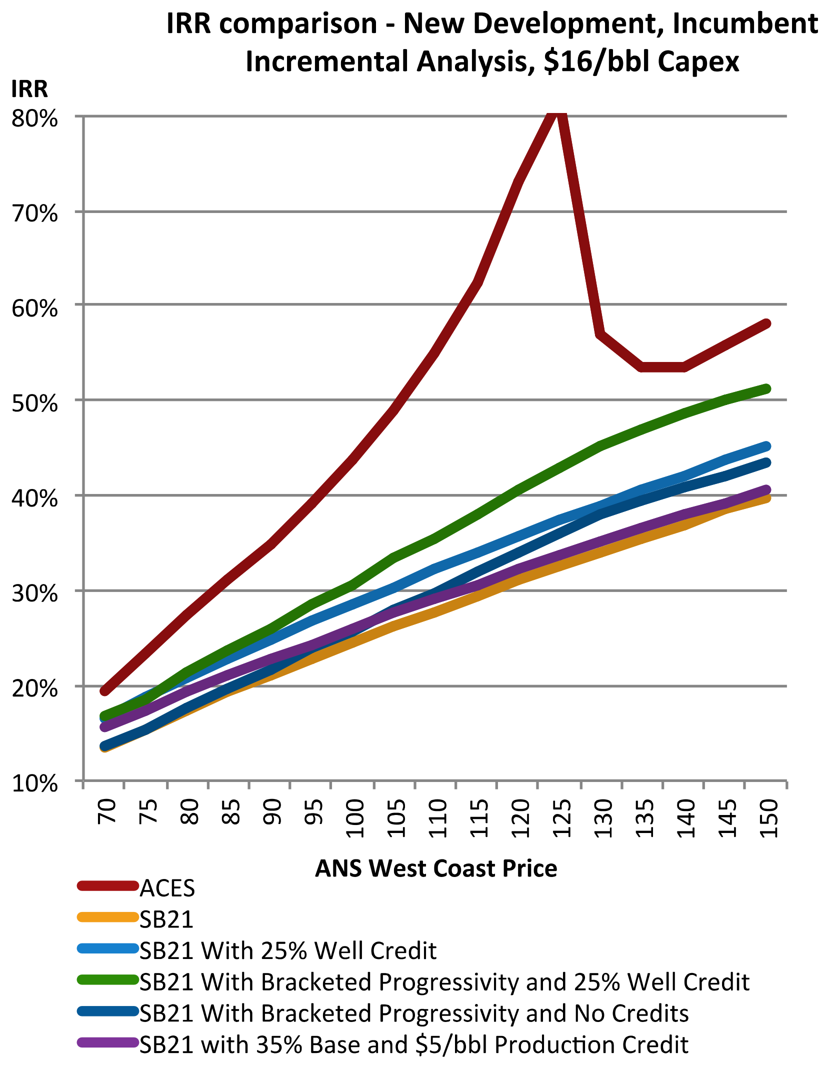
IRR Comparison
$16/bbl New Development, Standalone



IRR Comparison
$25/bbl New Development, Standalone

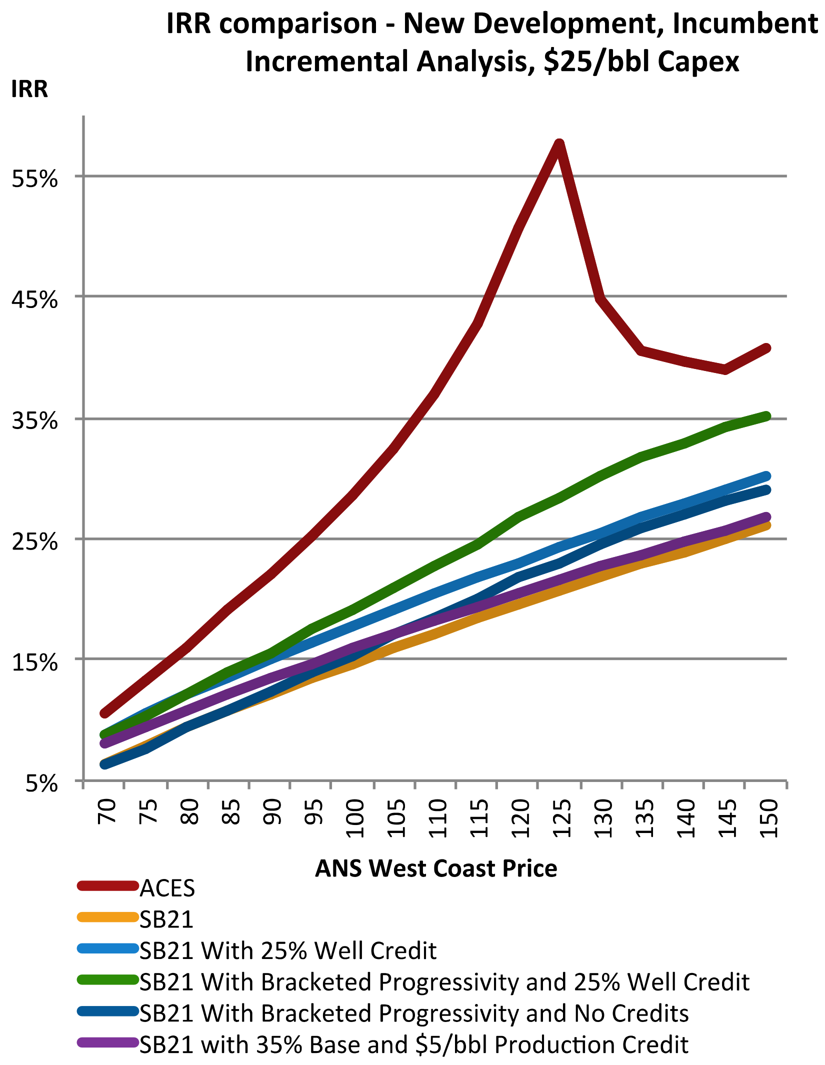


IRR Comparison
$16/bbl New Development, Incumbent Producer Incremental Analysis



IRR Comparison

$16/bbl New Development, Incumbent Producer Incremental Analysis



Conclusions

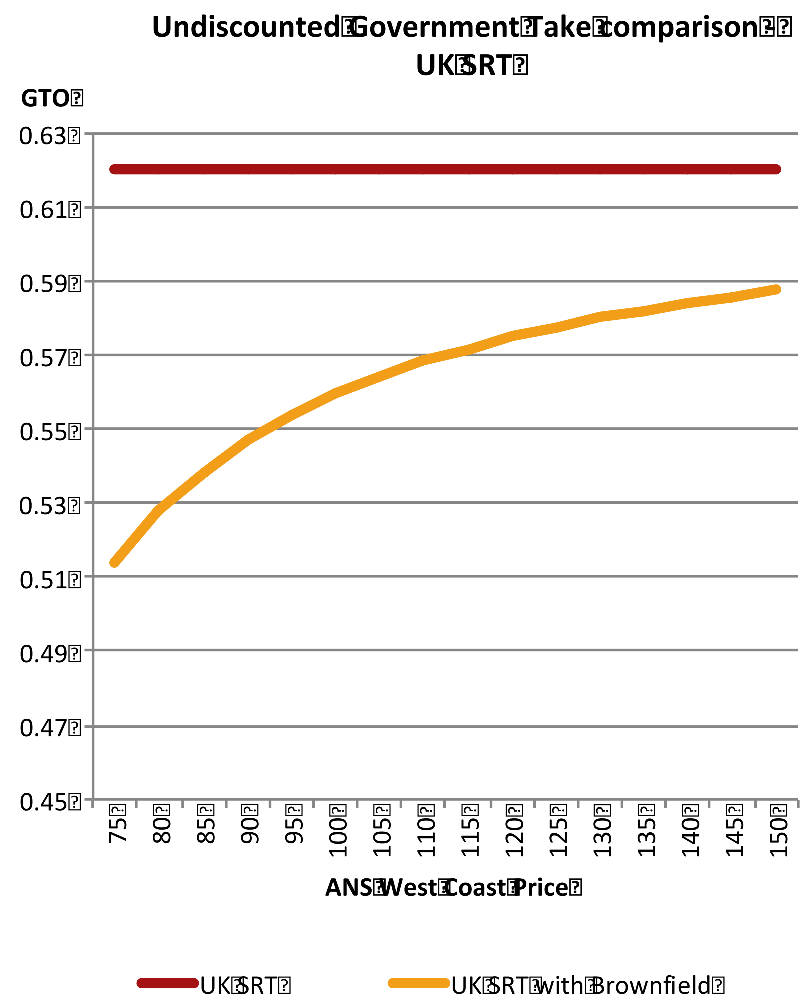
- Elimination of credit has a significant negative impact on project economics at low prices, or high development costs – though for new developments outside existing areas, this is more than offset by the GRE.
- Partial reinstatement of credits (for instance more targeted well expenditure credit) can partially mitigate this, but not fully.
- Bracketed progressivity a feasible approach to balancing revenue impact of partial or full reinstatement of credits.
- Higher base tax and production-based credit an interesting approach, and may help question of tax increase for base production at low prices. Since credit does not contribute when costs are incurred, does not address impact on higher-cost development.

Requested Analysis:

Impact of UK Brownfield Allowance

Impact of UK Brownfield Allowance

- The UK's fiscal regime is a relatively simple one, with two core components – a Corporate Income Tax (CIT) of 30%, and a Supplemental Resource Tax (SRT) of 32%, levied on the CIT tax base
- The UK Brownfield Allowance is an income exclusion, used in calculating the SRT. Up to a total £250mm of income can be excluded, with up to 20% of the exclusion amount allowed in a given year. For projects subject to the additional Petroleum Tax (pre-1993 projects), the exclusion is up to £500mm of income
- Because it is a fixed exclusion, it has a greater impact at lower oil prices
- Projects are individually assessed for qualification, and for the total amount of relief available. Qualifying projects are incremental projects increasing production from mature fields.
- A 100mmb incremental development, with costs of $25/bbl, could see its government take reduced by to anywhere from 3 to 11 percentage points, depending on the oil price level



Main Regional Offices

Asia

PFC Energy, Kuala Lumpur
Level 27, UBN Tower #21
10 Jalan P. Ramlee
50250 Kuala Lumpur, Malaysia
Tel (60 3) 2172-3400
Fax (60 3) 2072-3599

PFC Energy, China
79 Jianguo Road
China Central Place Tower II, 9/F, Suite J
Chaoyang District
Beijing 100025, China
Tel (86 10) 5920-4448
Fax (86 10) 6530-5093

PFC Energy, Singapore
15 Scotts Road
Thong Teck Building, #08-04
Singapore 228218
Tel no: +65 6736 4317

Europe

PFC Energy, France
19 rue du Général Foy
75008 Paris, France
Tel (33 1) 4770-2900
Fax (33 1) 4770-5905

North America

PFC Energy, Washington D.C.
1300 Connecticut Avenue, N.W.
Suite 800
Washington, DC 20036, USA
Tel (1 202) 872-1199
Fax (1 202) 872-1219

PFC Energy, Houston
2727 Allen Parkway, Suite 1300
Houston, Texas 77019 ,USA
Tel (1 713) 622-4447
Fax (1 713) 622-4448

www.pfcenergy.com | info@pfcenergy.com

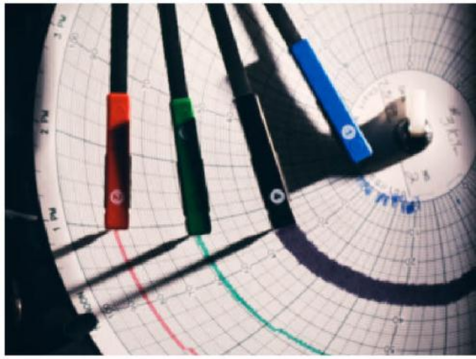
Notice

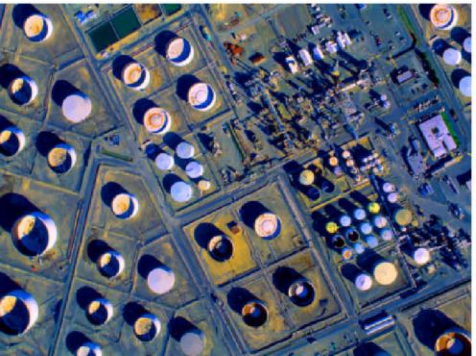
PFC Energy has prepared the materials utilizing reasonable care and skill in applying methods of analysis consistent with normal industry practice, based on information available at the time such materials were created. To the extent these materials contain forecasts or forward looking statements, such statements are inherently uncertain because of events or combinations of events that cannot reasonably be foreseen, including the actions of governments, individuals, third parties and market competitors. ACCORDINGLY, THESE MATERIALS AND THE INFORMATION CONTAINED THEREIN ARE PROVIDED "AS IS" WITHOUT WARRANTY OF ANY KIND, EITHER EXPRESS OR IMPLIED, INCLUDING BUT NOT LIMITED TO THE IMPLIED WARRANTIES OF MERCHANTABILITY, ACCURACY, OR FITNESS FOR A PARTICULAR PURPOSE. Conclusions presented herein are intended for information purposes only and are not intended to represent recommendations on financial transactions such as the purchase or sale of shares in the companies profiled in this report.

PFC Energy has adjusted data where necessary in order to render it comparable among companies and countries, and used estimates where data may be unavailable and or where company or national source reporting methodology does not fit PFC Energy methodology. This has been done in order to render data comparable across all companies and all countries.

This report reflects information available to PFC Energy as of the date of publication. Clients are invited to check our web site periodically for new updates.

A trusted advisor to energy companies and governments for over twenty five years





PFC Energy