BlueCrest testimony to House Finance Committee - March 22, 2017

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Good afternoon Co-Chairs Foster and Seaton, and members of the Committee. For the record, my name is J. Benjamin Johnson. I am the president and CEO of BlueCrest Energy Inc. Thank you for the opportunity to speak concerning this very important matter.

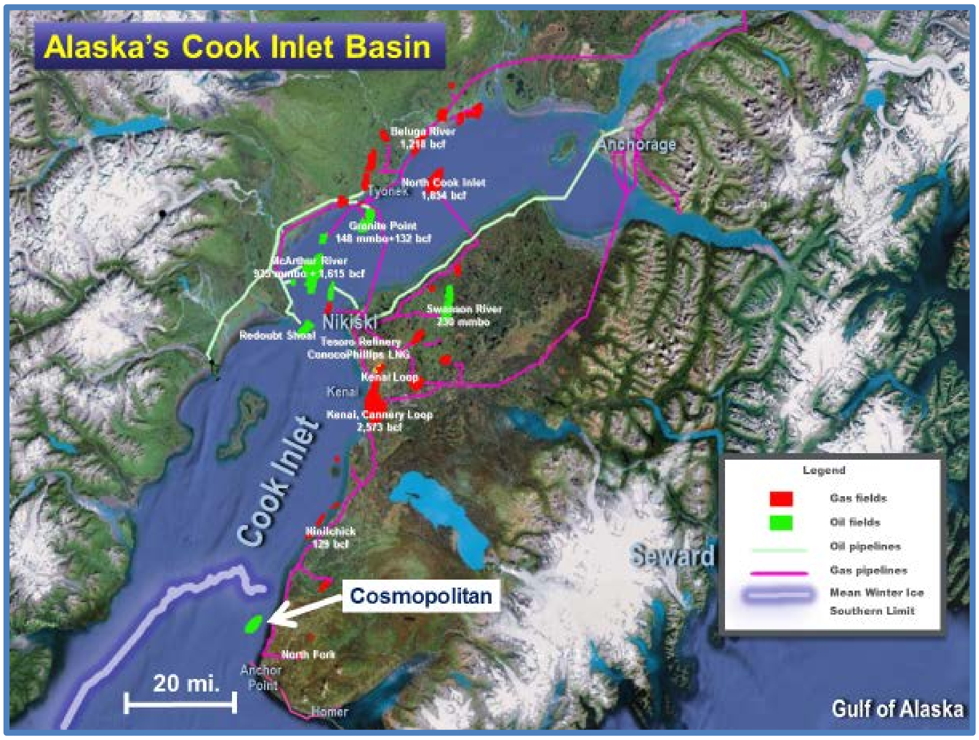
First, I want to echo what we've heard today from Kara Moriarty and other members of the industry. In particular, I want to emphasize the importance to Alaskans of fostering an environment that helps get Alaska's vast resources developed and brings value to its residents.

Just last year we heard many voices claiming that Alaska's oil industry was dying. The conventional wisdom said that it was time to "move on" beyond oil.

But now we know that was wrong! In fact, the positive changes to the state's tax system over past years has attracted the capital and new companies so that the natural decline of TAPS has been stemmed – at least for now – and the state has laid the foundation for decades of continued production.

And of course, we've all heard about three gargantuan oil finds that have been announced on the North Slope. But that's just what has been announced! Who knows what else may be coming as result of more exploration!? These huge new fields will take time and a lot of money to reach production. But if these new finds can be developed, they are poised to usher in a new era of productivity and long term wealth for Alaska.

Right now, we know that Alaska's oil is there. The question is whether the economic conditions will facilitate its development.



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In the Cook Inlet, we have also seen a re-birth of old fields, doubling the total Cook Inlet production of oil and ending the gas supply crisis.


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Right now, BlueCrest is developing a substantial new field in the Cook Inlet. The Cosmopolitan Unit is poised to become the largest oil producing field in the Cook Inlet and has the potential to provide enough natural gas to supply the Southcentral utilities for many years to come. Because of the location, Cook Inlet fields can be developed much more quickly than those on the Slope. Yes, the size is smaller than some of the largest North Slope fields, but so are the costs and time to bring online. For example, we built and turned on our initial onshore production facility in Anchor Point in a little more than a year.


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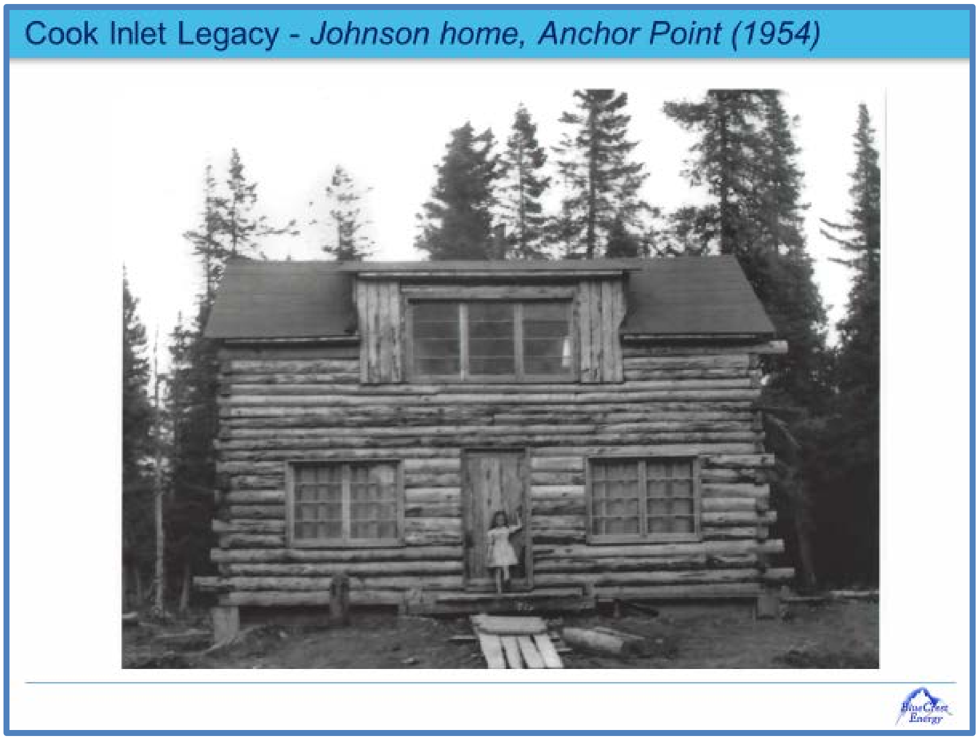
And now, we have completed and started-up the most powerful Extended Reach Drilling rig in Alaska, specifically designed for this project. A couple of weeks ago, we successfully finished drilling the longest-reach well ever in the Cook Inlet, resulting in thousands of feet of net pay for new oil production. And yesterday, we began drilling the next well that will include two long horizontal production zones. We have the potential to drill up to 20 of these large new wells, likely more than doubling or even tripling the current Cook Inlet oil production. While we are drilling, we create between 200 and 300 jobs, and they are almost all filled by Alaskans.

We know the oil is there; it’s just a matter of spending the money to implement the technology to get it out.



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Now let me tell you a little bit about BlueCrest's story. Most of you know that, although our corporate headquarters are in Texas, I am from Alaska. My parents lived in Anchor Point and Homer in the '40's and '50's before I was even born, and I grew up in Kenai. I worked my way through college on the Cook Inlet Platforms and then for ARCO as an engineer on some of the early Prudhoe and Kuparuk projects. I later earned my master's degree from UAA with my thesis written on "What to do with the North Slope gas?". When BlueCrest's current managers initially formed BlueCrest about 7 years ago, I personally hoped we'd be able to come back to Alaska and bring new value to this land. But, in our role as managers of assets for global private investors, we have to do our best to ensure that their investments receive the highest returns possible.

Fact:

Alaska must compete with other locales for investment funding.

Oil in the ground must be found and developed before Alaskans can receive value.

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We've heard this theme earlier today – and I can personally testify that it's a fact. The oil business is largely a matter of competition for investment dollars. Large oil and gas investors look all over the world, and the investment money will naturally go wherever they believe it can generate the highest return. Our investors have the opportunity to invest their money in many locations around the world, and we have to offer a better deal to get them to invest in Alaska.

Long before we made the decision to come here, the BlueCrest management team looked all over the US for investment opportunities that would allow us to find and develop new oil and gas. We certainly expected that Alaska had the resources in the ground, but Alaska's costs and administrative processes simply made it non-competitive with fields in the Permian, Gulf Coast, or North Dakota basins. Investments in Alaska are daunting: it costs roughly three to five times as much to drill a well or build production facilities in Alaska as it does anywhere else in the U.S.

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We weren't even considering investing in Alaska until 2009 when we met some representatives from the State of Alaska who had a booth at the North American Petroleum Exposition. They were enthusiastically urging new companies to come north to develop the state's resources. State officials handed out a book ironically called "Dispelling the Alaska Fear Factor" and provided information sheets describing the incentives the state was providing for new explorers and developers to come to Alaska. The state was remarkably offering to rebate a portion of upfront investments made by oil companies in order to help make the Alaska investments more competitive with investments in the Lower 48, and the state has offered a consistent schedule up until last year for reviewing and paying those credits on time. The tax credits were meant to tip the balance in favor of Alaska. The bottom line is that BlueCrest chose to invest hundreds of millions of dollars in Alaska (instead of investing elsewhere) because the incentives offered by the State were believed to be enough to offset the cost differences between Alaska and the Lower-48.

Let me be very clear. We would not be here – and we would not be developing Cosmopolitan that can provide hundreds of millions of dollars to the State over time – but for our initial belief in the good faith of the State of Alaska to follow through on its promises to us.

When we first looked at developing the Cosmopolitan project a few years ago, we very carefully made sure that we would have the investment funds necessary to get us to completion. We believed that the State would follow through with its highly-promoted tax credit program that actually paid cash rebates to small companies for their investments in the state. Granted, that was a one-of-a-kind opportunity. But nevertheless, it was what the State clearly announced it would do.

So before we ever started, we made sure that we would have enough investment money available to get us to the point where we could finally be cash-flow-positive and begin paying back the investors. And, of course, as committed to us by the state's representatives, that plan was based on the belief that a portion of the total investments would be covered by the state tax credits.

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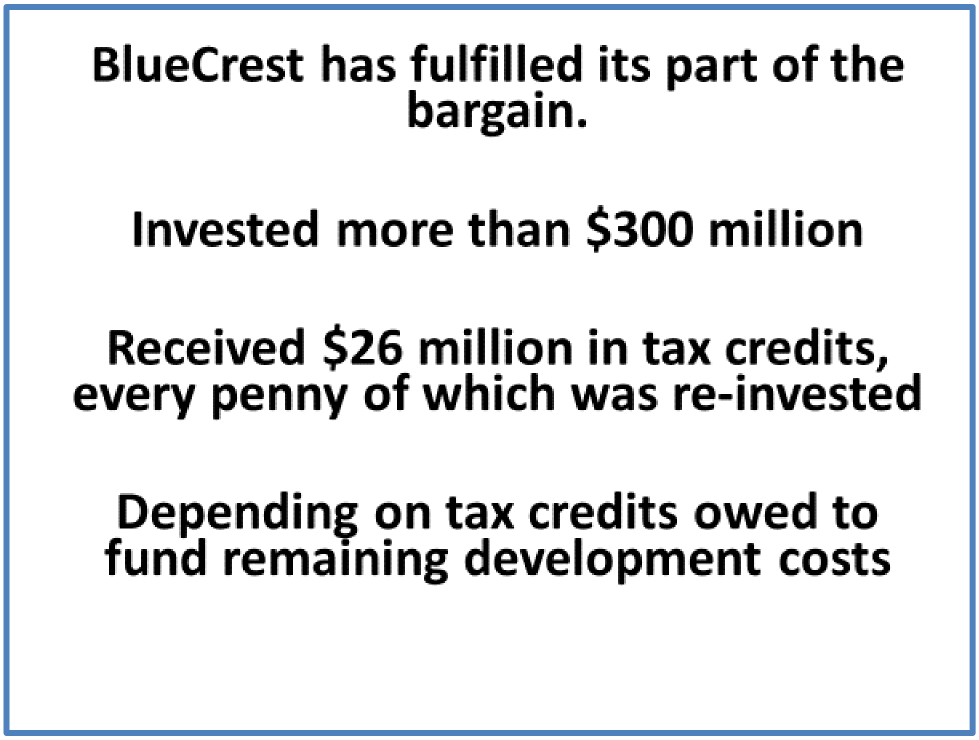
And we did it. As of today, we have successfully proved up the large oil and gas resources in the Cosmopolitan Unit. We have completed a large new production facility (on-time and under-budget), and we have built and started-up the most powerful drilling rig in the state. We have just finished drilling a record-length well that could be the first of many future wells with decades of production. And that new production will likely generate more than $750 million dollars in royalties alone for the state.



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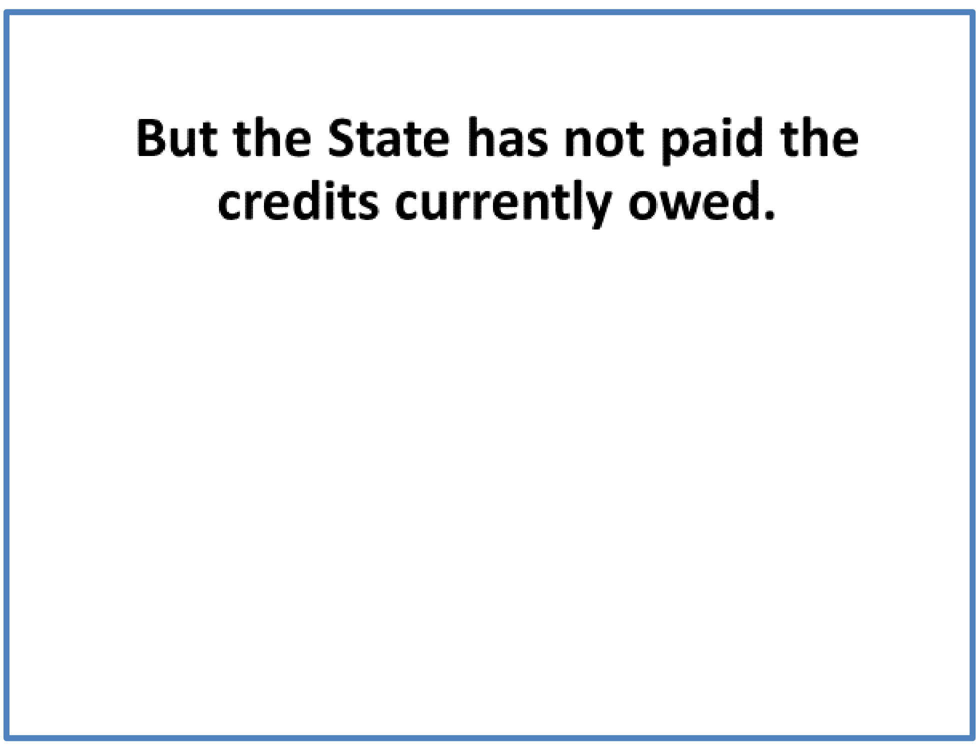
To date, BlueCrest has invested over $300 million, and we have received about $26 million in tax credits. And every penny of those credits has been re-invested in the field development.



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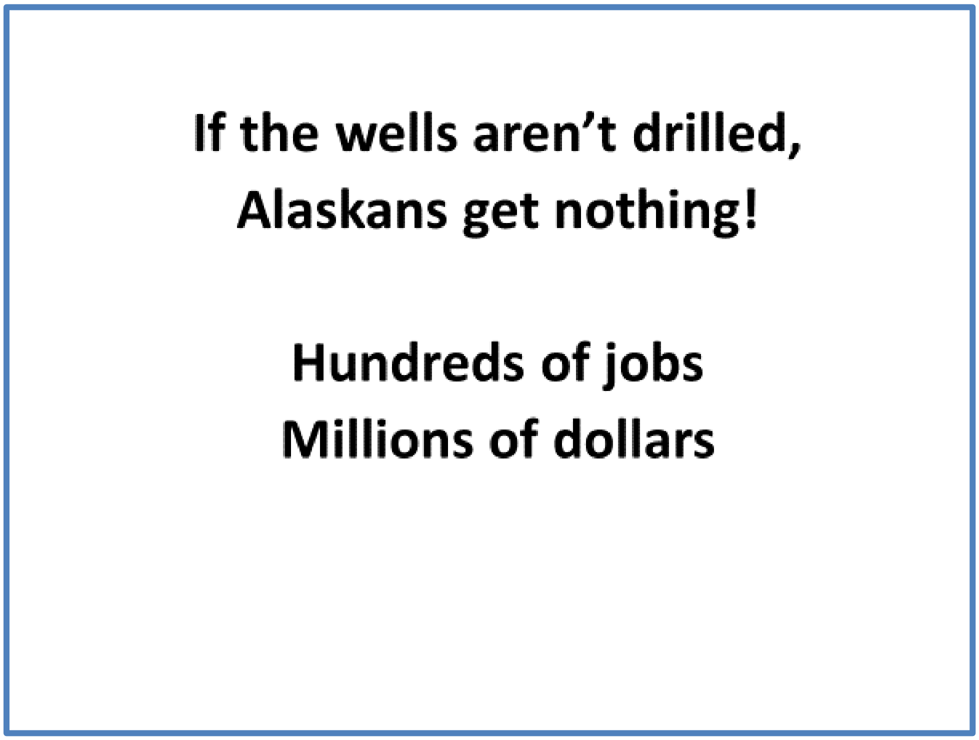
But here's the rub. BlueCrest has done its part and invested everything we said we would, but the State has failed to live up to its original commitments to pay the tax credits that have been earned to date. We fulfilled our commitments to invest hundreds of millions of dollars in hard cash for development of the Cosmopolitan resources. But the State has so far failed to pay its share of the tax credits, and that has left a large hole in our plans for funding the continuation of the field development.



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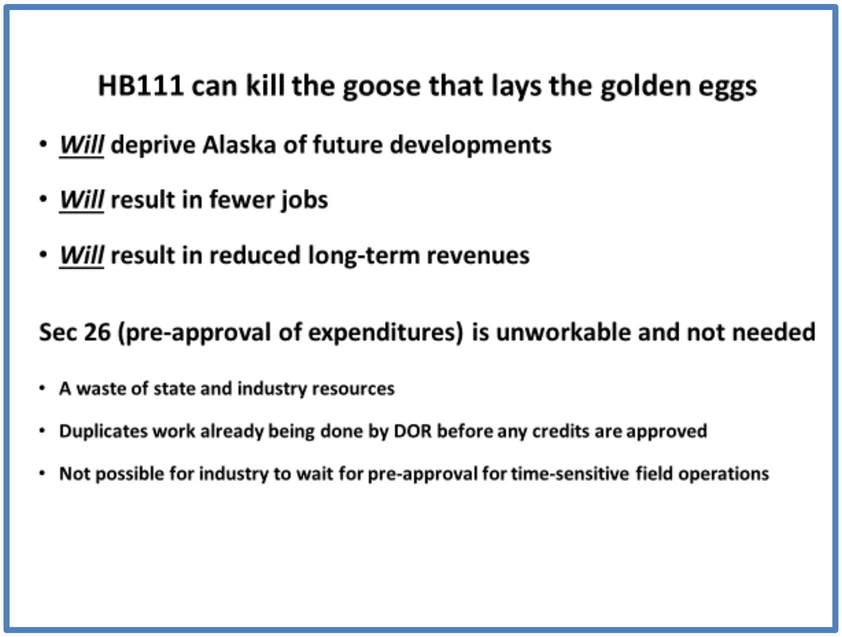
But if the remaining tax credits are not paid, the results to the state are tangible: Without receipt of the rest of the tax credits as originally promised, we could be forced to slow or stop drilling the new oil wells that would unquestionably provide large returns to the state, resulting in a loss of hundreds of jobs for Alaskans. Surely it goes without saying, but if the wells aren't drilled, Alaskans get nothing. Alaska's residents lose jobs. Alaska vendors lose business opportunities. And the state and local governments lose revenue.

A competitive production tax system with incentives for new development is absolutely not a give-a-way. As a major land-owner, Alaska benefits from every barrel that is produced on its lands, and I contend that you should be looking at this as an investment opportunity. Alaska stands to generate tremendous future revenues from a dynamic and successful oil industry. The more you can do to stimulate new development and enhanced production from existing fields, the more Alaska's residents will benefit. Remember, the state gets zero value if that oil is never found or stays in the ground.



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HB111 is a great example of a terribly misguided and shortsighted attack on the goose that lays Alaska's golden eggs. Do you really think you can dramatically alter the tax structure for short term gain or create incredible administrative burdens and still get the same production value in the future? I've been involved in the US oil industry for over 40 years now. I've engineered and managed oil and gas developments all over the country, and I can tell you that passing HB111 *will* deprive Alaska of future developments and *will* result in less future state revenues and fewer Alaskan jobs. In the interest of time, I will only address a couple of the specifics in the bill, but I do agree with the testimony of AOGA and the other companies we've heard today.

I've got to tell you that the pre-approval provision in section 26 has got to be the most egregious waste of government and industry resources I've ever seen in my career. First of all, it's not even possible to conduct oilfield operations if we have to stop and wait for every expenditure to be approved in advance. We can't even always do that internally, because we deal in a business that is fraught with uncertainties, and we often have to react quickly. We have to authorize our line-level managers to make many spending decisions on the spot, and there would absolutely be no time for an external review. When we encounter something while drilling or operating wells and facilities, we have to handle it immediately. Secondly, no matter how you look at it, any money spent by industry costs industry far more than any tax deduction or credit. So no prudent oil company wants to spend one more dollar than is necessary. And keep in mind that under the current existing process, every expenditure is actually reviewed by the DOR after the fact. No deductions or credits are allowed if they are not in compliance with current regulations. So this proposed pre-approval process would provide zero added value to the State, it would require a huge increase in State staff, and it would delay projects. It is a lose-lose proposition.

Payment of tax credits owed is paramount to the success of new field developments.

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Paramount to BlueCrest and other smaller companies in the state is payment of the tax credits that have already been earned and are now owed. We now understand that you may decide to change or even eliminate the tax credit incentives going forward – but please at least honor the state's commitments for the amounts that have already been earned.

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So to wrap up, I'd like to re-emphasize the future potential wealth this state can have if the competitive economic environment is done right. Alaska is a land of tremendous undeveloped potential. I urge you to encourage growth to realize the state's true potential. Let's all work together to wisely develop and grow Alaska's long term value.