Alaska Oil and Gas Association

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AOGA Testimony
HB 411 – House Finance Committee
April 11, 2018

Co-Chair Foster, Co-Chair Seaton, Members of the Committee:

For the record, my name is Kara Moriarty and I'm the President/CEO of the Alaska Oil and Gas Association, commonly known as "AOGA".

AOGA is the professional trade association for the oil and gas industry in Alaska and my testimony this evening on HB 411 has been approved by unanimous consent by our diverse group of members.

Thank you for the opportunity to testify on potentially the 8th change in oil tax policy in 13 years. My testimony tonight will allow me to correct ongoing, misleading rhetoric, update the committee on the status of investment and production in Alaska, and provide our thoughts on this significant increase in tax.

First, rhetoric. I hear time and time again, that the oil companies asked for and supported all of the changes since 2005. The reality is, that is simply not true. As you can see, we have opposed all but two of the previous changes. No other industry has experienced as many changes to its fiscal structure than Alaska's oil and gas industry, even though our industry still accounts for 77% of the unrestricted revenue.

In fact, petroleum revenue doubled from FY 17 to FY 18. Other industries do not even contribute enough to the state treasury to cover the costs to regulate them. The constant bombardment of proposed tax increases we see introduced by the House, does instill uncertainty among already nervous investors. Yes, just discussing taxes makes us nervous. Look at what happened to the stock market when the federal tax bill was being discussed. Investors react to talk, not just action.

Another thing we hear is about how new production won't pay taxes for 7 years. Let's put that in context. First, the lack of payment illustrates how long it takes to start making money on a new development. And, as the Administration said last night, this provision in the tax law was a specific policy measure built to encourage new companies to Alaska. It basically only applies to *new* companies with *new* production. So what portion of this provision applies to current production? Roughly about 7-8% percent. The way some are talking it would appear to the public that all new production would not pay production tax. Not true. And even if it were true, that new production would be paying royalty, corporate income tax, and property tax, not to mention providing jobs and economic benefit to Alaska.

HB 411 is designed to collect more revenue for Alaska. It is clearly not designed to attract more investment and production to the state, which is a shame, because Alaska continues to fall behind the rest of the country in terms of investment and production.

According to this chart, you can see capital investment for the last decade for Alaska and the rest of the US, as it corresponded to oil price. The bottom line is what Alaskans should care about: This year, 2018, energy companies plan to invest $120 billion in capital projects in the United States alone. What portion is coming to Alaska? Less than 2%.

Why would that be? We have the "rocks" – in fact, one-third of the nation's reserves are here in Alaska. We have a well-trained work force, and according to some, one of the lowest tax rates in the country at current prices.~~?~~

And at the beginning of this session, the legislature's consultant, in3energy, shared a presentation outlining that at $60 oil, an Alaskan producer's net is $12/barrel for legacy fields and $1.50/barrel for new fields. Meanwhile, companies operating in West Texas net $31/barrel –Texas many have a higher minimum production tax at these prices, but even with a higher tax rate, due to Texas's cost structure and overall fiscal policy, oil companies can earn a lot more per barrel. And at the end of the day, companies invest where they can make money. Perhaps that's why business is booming in Texas.

With investment dismal compared to the rest of the country, and companies being able to net three times or more compared with their investments elsewhere, it should be no secret that even though we had slight increases in Alaska production the past two years, Alaska has recently slipped to 5th in the nation. When I started working at AOGA 13 years ago, we were 2nd.

Speaking of production tax rates, Rep. Gara is correct. At these lower prices in 2016, we do have one of the lowest production tax rates. Our current system is designed that way because of the high cost environment. But if you look at our tax structure holistically, and not in a vacuum looking only at one component, you will see that according to this recent report, our effective tax rate, at lower prices, is one of the highest in the nation.

HB 411 makes three significant changes that completely alter~~s~~ the current tax structure: it would lower the current base production tax rate from 35% down to 25%, eliminate the sliding-scale per barrel tax credits on legacy production and eliminate the $5 per barrel tax credits on new production. The bill would also create three compounding levels of progressive higher tax brackets, beginning when the "production" taxable value exceeds $40 per barrel. Additionally, the structure of AS 43.55.011(g) as it reads in Section 2 of the bill looks to us like a means to establish a framework for more extreme versions in the new progressivity tax in the future.

To us, HB 411 is merely an attempt to roll back the voter-ratified reforms under "SB 21" in 2013, in favor of the "bad old days" of progressivity.

I think it is important for the committee to recognize that due to the complexity in how the bill was written and the effective dates of these new progressivity rates, it is conceivable that the "progressive" rates could be amended to have different rates for production tax values above the respective thresholds, or different thresholds for the period before 2022 and the one that follows.

In regards to the sliding-scale tax credits, your own legislative consultants and the Administration warned against lowering or repealing the sliding-scale tax credits as those "credits" were essential to keeping Alaska's fiscal regime competitive.

On July 17, 2015, legislative consultants, Enalytica, described the per barrel credit as a "misnomer." They testified that - "The credit against the production tax is not really a credit; it has an explicit tax-rate-setting goal."

On that same day, the DOR Tax Director acknowledged the importance of the sliding-scale tax credits for keeping Alaska's overall production tax competitive. He said: "With SB 21 the (per-barrel) credit is an offset to the tax and is designed to create a progressive element, a little bit lower tax rate at lower prices, a higher tax rate at higher prices, so it's hard to really consider them a credit in the context of an inducement to doing work. It's really what we are calling an integral part of the system."

About two years later, Legislative consultant Roger Marks said that the sliding-scale tax credits were an “important feature” of the current tax structure as an “adjustment of effective tax rate to offset high royalty at low prices.

Adopting House Bill 411’s new tax rate, turning the “progressivity” section back on, and removing the sliding-scale per barrel tax credits would in effect revert the current tax structure to a modified ACES type of tax structure — a tax structure which would raise industry taxes by significant amounts at low prices much as ACES did at high prices.

Constant discussions and changes to tax policy does not impart confidence that Alaska is a good place for oil and gas investment. Instead, HB 411 is simply another attempt to take more from the one industry that pays more than its way in Alaska. HB 411 will not increase production. It does not simplify the tax structure. It will not incentivize investment.

In closing, what is most troubling and concerning to my member companies is the constant barrage of tax increase proposals we have seen introduced in the House this legislative session, even though the Speaker of the House —when speaking on January 4, 2018 about broad based taxes and the potential for industry taxes, he said, “I don’t see that (industry taxes) on the table.” But here we are, on the 86th day of the Session with a bill that would triple our taxes. HB 411 is before us despite your leader’s comment, despite the Administration not supporting this bill, despite the Administration not supporting changes to the oil tax system at this time, and despite all the statements that the Working Group was to be the entity to vet and consider changes to policy. It surprises me that the Finance Committee did not take this draft bill to the co-chairs of the Working Group and ask them and the legislature’s consultants to consider the impacts of this bill and all the others introduced this session.

We have not seen this type of impact since ACES, which on a scale of 1 to 10 for us was a 10, which puts this bill at least a 9.5. My member companies respectfully ask, when will it be enough? When will the constant discussions end?

Thank you for the opportunity to testify and I’m happy to address any questions.