Alaska Oil and Gas Association

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AOGA Testimony on Committee Substitute for House Bill 247

Senate Finance Committee - May 15, 2016

Good Morning Co-Chairs MacKinnon and Kelly, and 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 referred to as "AOGA".

Thank you for the opportunity to testify on the Committee Substitute (CS) for HB 247. I have unanimous consent of my diverse group of members to offer these brief thoughts today.

In listening to your discussion yesterday, I was encouraged several of you were asking very important questions such as, "What will the bill do to production and jobs?" We would also encourage you to ask, "How will state revenues be impacted by this bill next year or even five years from now? What will Alaska's economy look like following the adoption of this bill?"

HB 247 is a dramatic shift in oil tax policy for both Cook Inlet and the North Slope, and it will definitely result in less production, less investment, fewer Alaskans working, and ultimately, and somewhat ironically, less revenue for the State.

In my limited time this morning, it is impossible to go through every section of the bill that causes concern, especially when industry did not see the full 60 page amendment to HB 247 until it was introduced on the House floor. There was no opportunity for industry or the public to fully vet some of the concepts contained in the bill before you. There have also been claims that industry was okay with the amendment. Let me be clear, all AOGA members believe the bill before you is the worst committee substitute to date.

Unfortunately, in this low price environment we have seen a dramatic cutback in industry. Most painfully, Alaskans have lost jobs. We recognize the operating budgets are not final, but there could be 50-75 state employees that will lose jobs too. But for the oil and gas industry, the job loss has been even more severe, with over 1,000 Alaskans no longer working directly for industry as compared to a year ago. This does not include the contractor workforce.

As a reminder, the McDowell Group has estimated that for every direct job the industry provides another 20 jobs are created throughout the broader Alaskan economy. I know of no other private sector industry, or state government agency that creates such economic growth, so we would respectfully disagree with comments that suggest cutbacks from the oil and gas industry would not be as harmful to the Alaskan economy as reductions in other industries or government.

There was also a suggestion that the state can't do anything about the current downturn in the oil industry because the decisions have been driven by the price of oil. That is partially true. While there will be impacts due to price that are out of the state's control, state policies can exacerbate the problem. Will the state have policies that drive investment to Alaska when prices go up?

Under this bill the answer is no. Instead, it creates policies that will not drive investment to Alaska from explorers and producers alike when prices go up because it will now take a much higher oil price for industry investment to return or increase in Alaska, if it returns at all.

As the state grapples with low prices, and budget shortfalls, ironically, the State is actually setting the stage for an inevitable loss of revenue regardless of what credits it removes or taxes it raises.

Under this bill, the State will see lower oil and gas production, which will then drain State finances. For example, the owners of Prudhoe Bay just updated their plan of development and have estimated that production will decline about 20,000 – 60,000 barrels per day due to the shut-down of 3 rigs. This lost drilling time could result in a 10-30% decline in Prudhoe Bay alone

Utilizing the Department of Revenue's Spring Forecast, we have examined what production decline will look like over the next five years. I believe you have the charts we have developed. If production estimates stay where they were in April, production in FY 2021 will be about 418,600, about a 4% decline. However, if the proposed legislation is enacted, the DOR's production estimates will become far too optimistic. In reality, increased taxes and omitting tax credits will accelerate production decline.

If we had a 10% decline per year for 5 years, production would be about 307,000 barrels per day, and in terms state revenue, a 10% decline in production will result in $793 million less in royalties alone for the State.

The technical aspects of operating TAPS are made more challenging with less production. Alyeska has stated that TAPS faces a significant operational obstacle at throughputs at around 300,000 barrels per day, which is about the 10% decline mark. Despite some of the best and most innovative people in the industry focused on this scenario, an operational solution has not yet been identified to sustain TAPS operation at this level.

It is fair to say, that this 6th change in tax policy in 11 years makes several fundamental alterations to SB 21 and to the tax system in Cook Inlet. This new policy will not attract investment or new independents to Alaska, causing exciting projects to be shelved. The bill spells doom for Cook Inlet as some credits will be removed in less than 6 weeks which is basically a retroactive tax increase as companies have made investments for the calendar year expecting a credit system to remain in place for a longer period. Additionally in Cook Inlet, the companies will be faced with extremely high tax rates, which will invariably be passed onto South Central natural gas consumers in the near future.

This bill sends a strong signal to the world that Alaska is constantly changing tax policies, regardless of oil price, and regardless of the economic condition of the industry.

In closing, the industry is not asking for a tax decrease or for tax or royalty relief. But it is my job to let you know what impacts your decisions will have.

- The bill will not increase production from the Slope or Cook Inlet.
- It will not encourage new companies to invest in Alaska, and will likely drive companies out of the state.
- It will not lead to more long-term revenues for the state.
- It will not provide long-term energy security.

We understand the politics associated with this issue are challenging. We get it. And yet, to my member companies, the politics are largely irrelevant to the core of what drives decision-making, and that is economics. My member companies will not pursue projects that don’t pencil out. I can assure you that HB 247 just made project economics worse for producers and explorers alike, and the decisions the companies will make in response will not be good for Alaska.

Thank you for the opportunity to testify today, and I’m happy to take any questions you may have.