State of Alaska
Department of Revenue
Commissioner's Office

ANGDA ~ Tax ~ Treasury ~ ARMB ~ AMBBA ~ APFC ~ PFD ~ AHFC ~ CSSD ~ AMHTA ~ DOR

SEAN PARNELL, GOVERNOR
550 West 7th Avenue, Suite 1820
Anchorage, Alaska 99501
Phone: (907) 269-0080
Fax: (907) 276-3338

March 25, 2011

Senator Joe Paskvan
State Capitol Room 115
Juneau AK, 99801

Re: Answers to questions posed March 17, 2011

Dear Senator Paskvan:

The purpose of this document is to respond to the questions you raised in our meeting with you on March 17, 2011. The requests/questions and responses follow.

1. **Prepare a version of the FY 2011 income statement that replaces the "credits applied against tax liability" with "total credits earned" regardless of when or how those credits are used.**

   Please see income statement for FY 2011 on the following page.

FY 2011 Production Tax Estimates with Total Credits earned[4]

	Price	Barrels	Value ($M)
Avg ANS Oil Price ($/bbl) & Daily Production (bbls)	$77.96	615,902	$48.0
Annual Production (bbl)			
Total		224,804,230	$17,525.7
Royalty, Federal and other barrels[1]		-34,100,490	($2,658.5)
Taxable barrels		190,703,740	$14,867.3
Downstream (Transportation) Costs ($/bbl)			
ANS Marine Transportation	-$2.07		
TAPS Tariff	-$4.17		
Other	$0.24		
Total Transportation Costs	-$6.00	190,703,740	($1,144.2)
Lease Expenditures			
Total Operating Expenditures	-$13.39		($2,553.0)
Total Capital Expenditures	-$13.49		($2,572.0)
Deductible Operating Expenditures[2]	-$12.99		($2,477.0)
Deductible Capital Expenditures[2]	-$10.43		($1,988.4)
Total Deductible Lease Expenditures	-$23.42	190,703,740	($4,465.4)
Production Tax			
Production Tax Value (PTV)			$9,257.6
Base Tax (25%*PTV)			$2,314.4
Production Tax Value per barrel	$48.54		
Progressive Tax = (7.4% * PTV)			$686.7
Total Tax before credits			$3,001.1
Credits			
Credits applied against tax liability			($400.0)
Estimated Total Tax after credits[3]			**$2,601.1**
Total credits earned (including not applied against tax)[4]			($665.0)
Total Tax before credits less total credits earned[4]			$2,336.1

Notes: (1) Royalty, Federal and other barrels represents our best estimate of barrels that are not taxed. This estimate includes both state and federal royalty barrels, barrels produced from federal offshore property and barrels used in production.

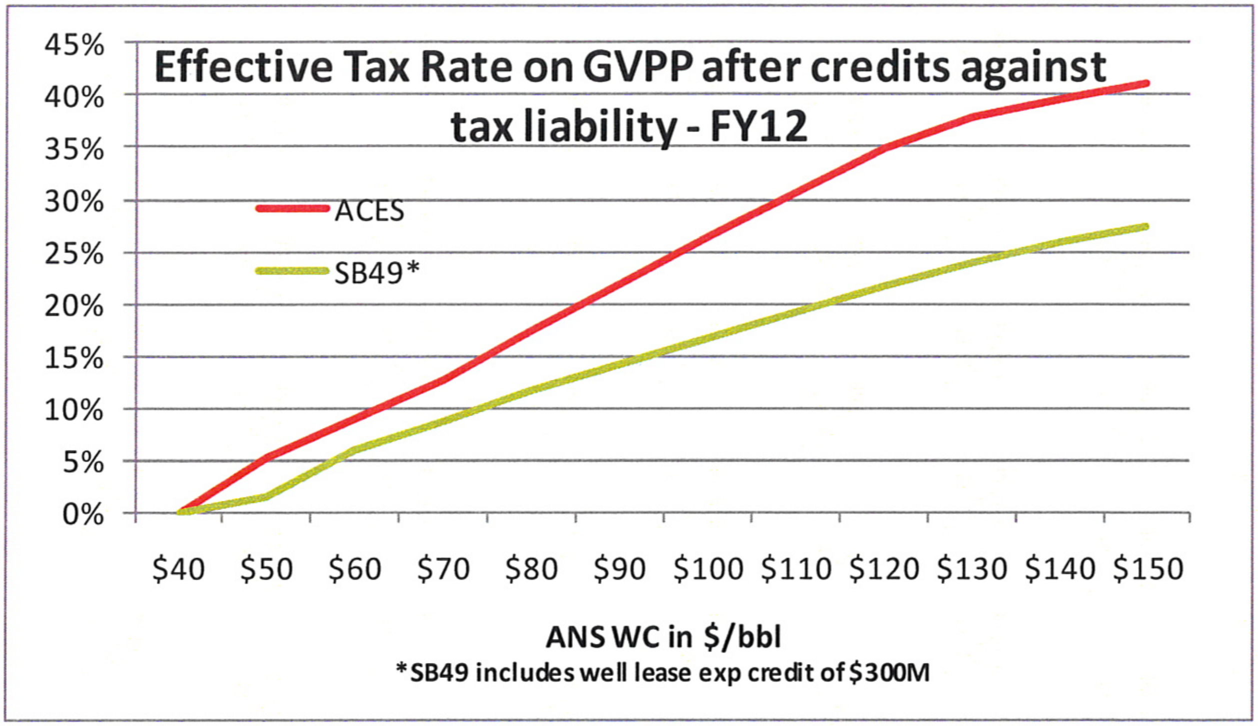
(2) Deductible Lease Expenditures represents our best estimate of lease expenditures that are applicable to currently producing fields that are likely to produce a tax liability for the company or companies producing them. The per-barrel expenditures reflect expenditures **per taxable barrel** and do not reflect expenditures per all barrels produced.

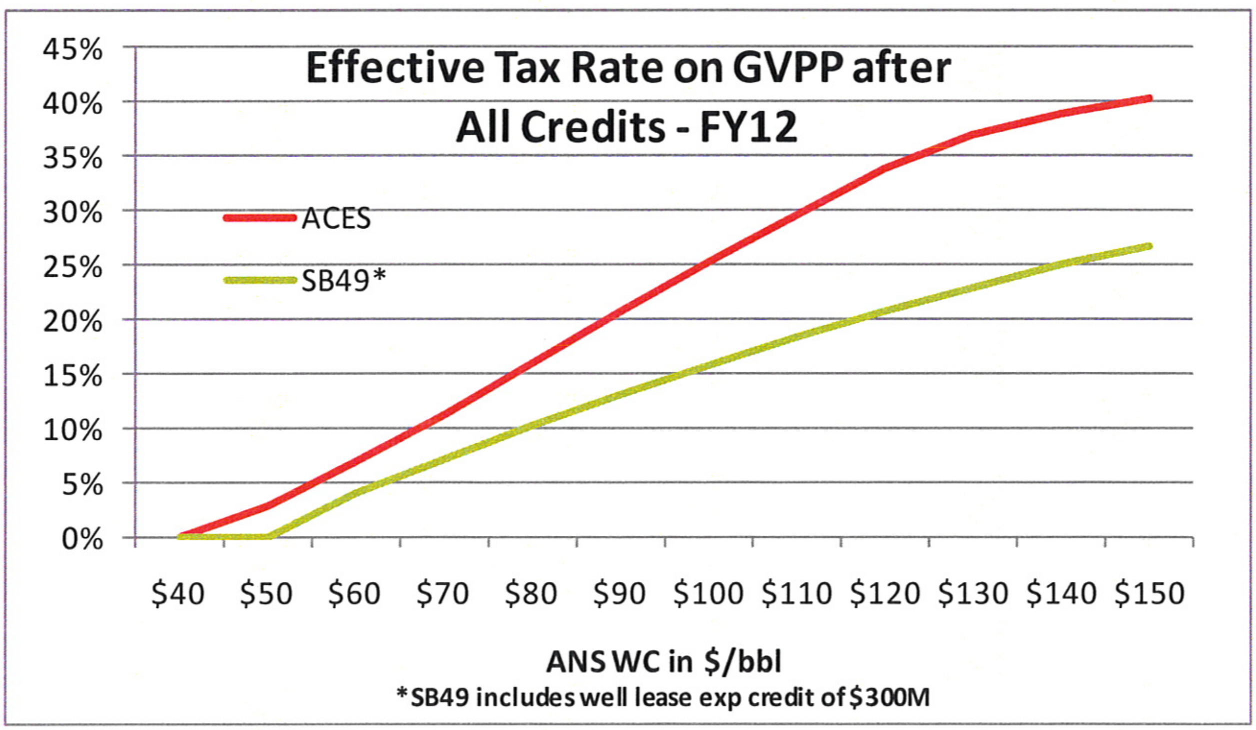
(3) Estimated Total Tax after credits is a calculated total based on constant daily production, constant oil prices, and constant expenditures for the entire year. Variations in these assumptions captured in larger revenue models will produce different results that differ from the estimates in the simple model above.

(4) Total credits earned is shown by request and is intended to reflect the net exposure to the state from all production tax credit activity in a year without regard to when and how the credits are applied or redeemed.

2. **Prepare slides showing effective tax rates on gross (after credits) for ACES and SB 49, for FY 2012-2016. Prepare similar slides showing effective tax rate on gross after all credits – including those used against tax liability and those which will likely be certificated – for ACES and SB 49 for the same years.**

   See the following pages for the slides requested in question number 2.


Effective Tax Rate on GVPP after credits against tax liability - FY12
ACES
SB49*
45%
40%
35%
30%
25%
20%
15%
10%
5%
0%
$40 $50 $60 $70 $80 $90 $100 $110 $120 $130 $140 $150
ANS WC in $/bbl
*SB49 includes well lease exp credit of $300M


Effective Tax Rate on GVPP after All Credits - FY12
ACES
SB49*
45%
40%
35%
30%
25%
20%
15%
10%
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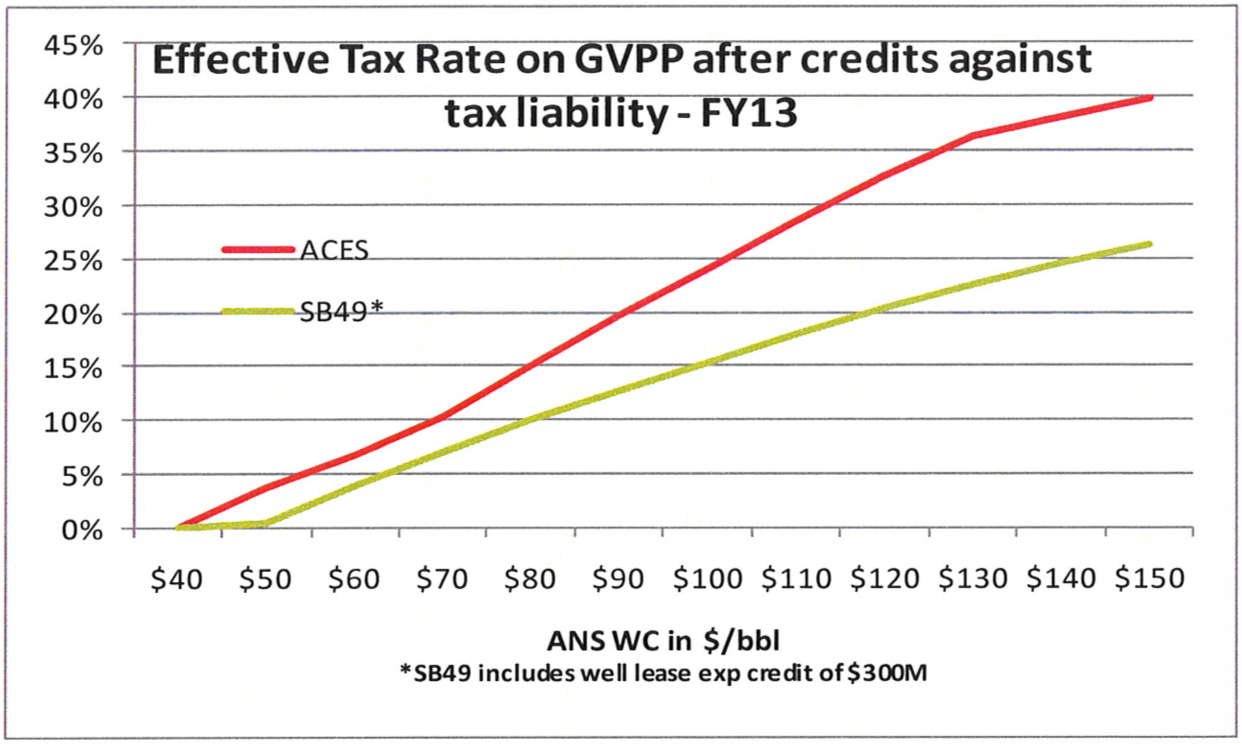
0%
$40 $50 $60 $70 $80 $90 $100 $110 $120 $130 $140 $150
ANS WC in $/bbl
*SB49 includes well lease exp credit of $300M


Effective Tax Rate on GVPP after credits against tax liability - FY13
45%
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35%
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25%
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10%
5%
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ACES
SB49*
$40
$50
$60
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$80
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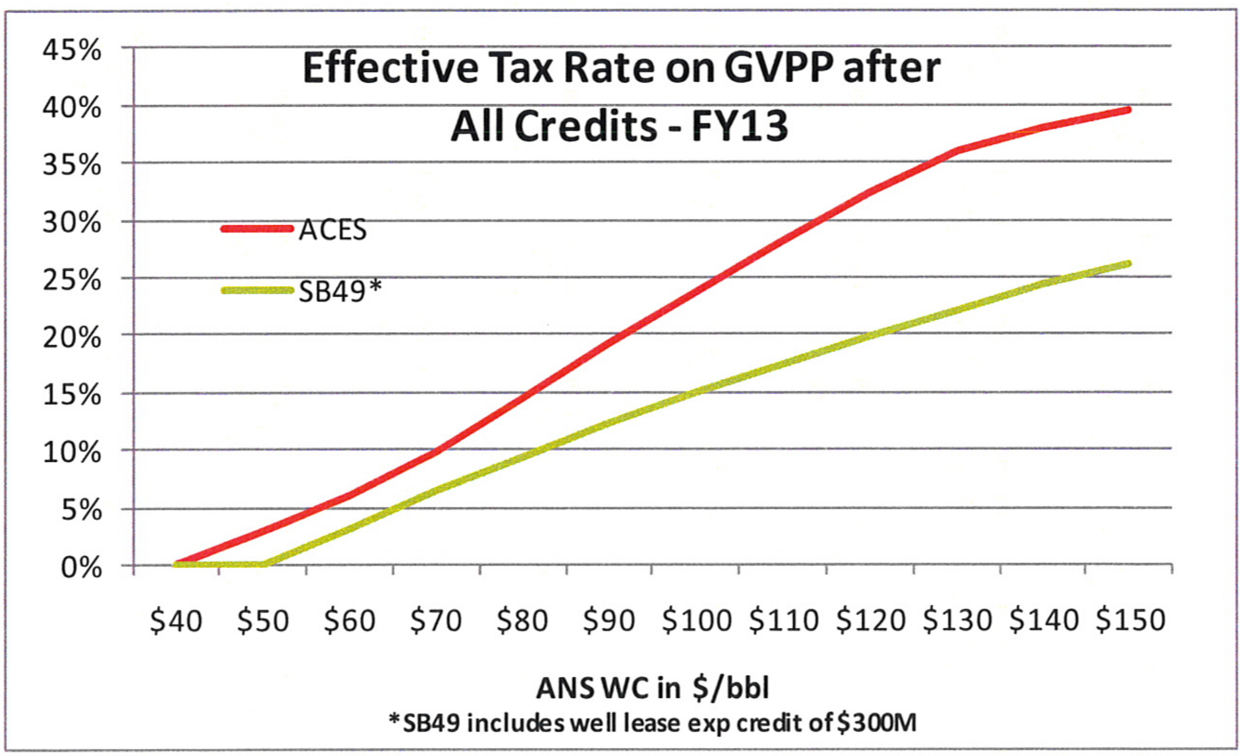
$110
$120
$130
$140
$150
ANS WC in $/bbl
*SB49 includes well lease exp credit of $300M


Effective Tax Rate on GVPP after All Credits - FY13
45%
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ACES
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$140
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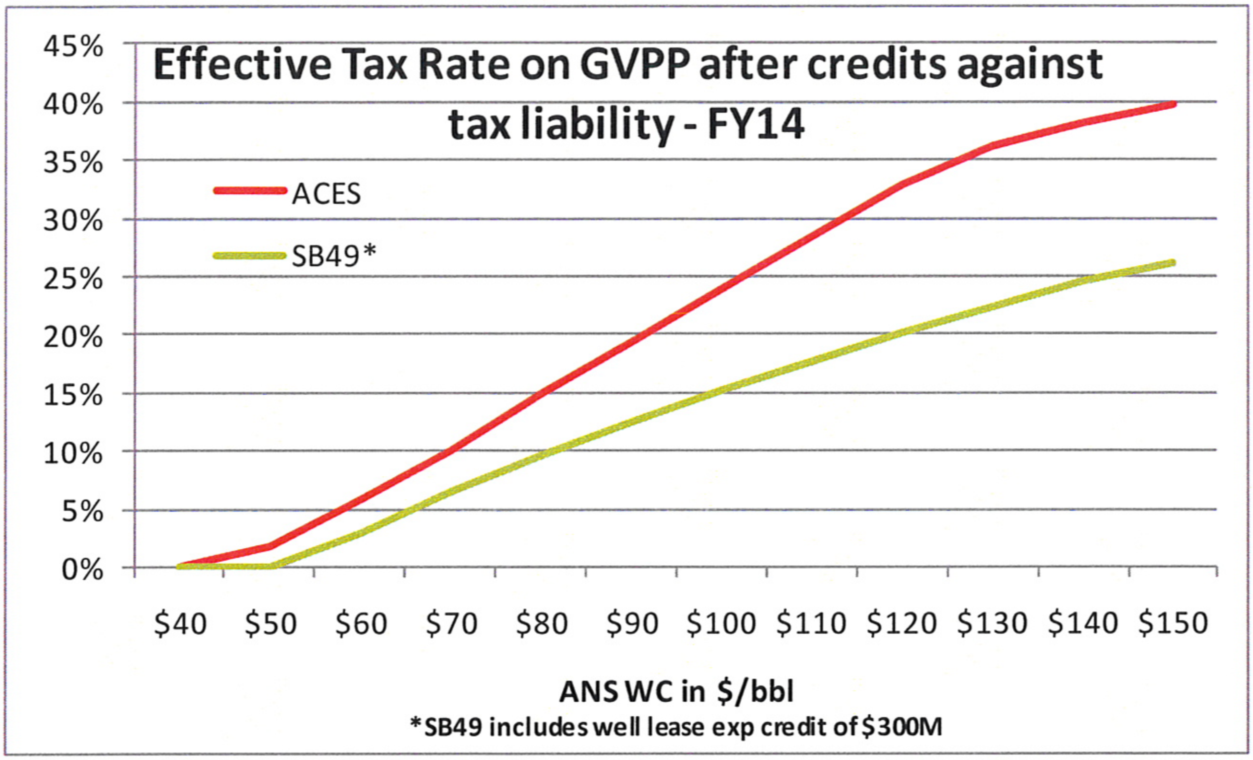
ANS WC in $/bbl
*SB49 includes well lease exp credit of $300M


Effective Tax Rate on GVPP after credits against tax liability - FY14
45%
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ACES
SB49*
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$140
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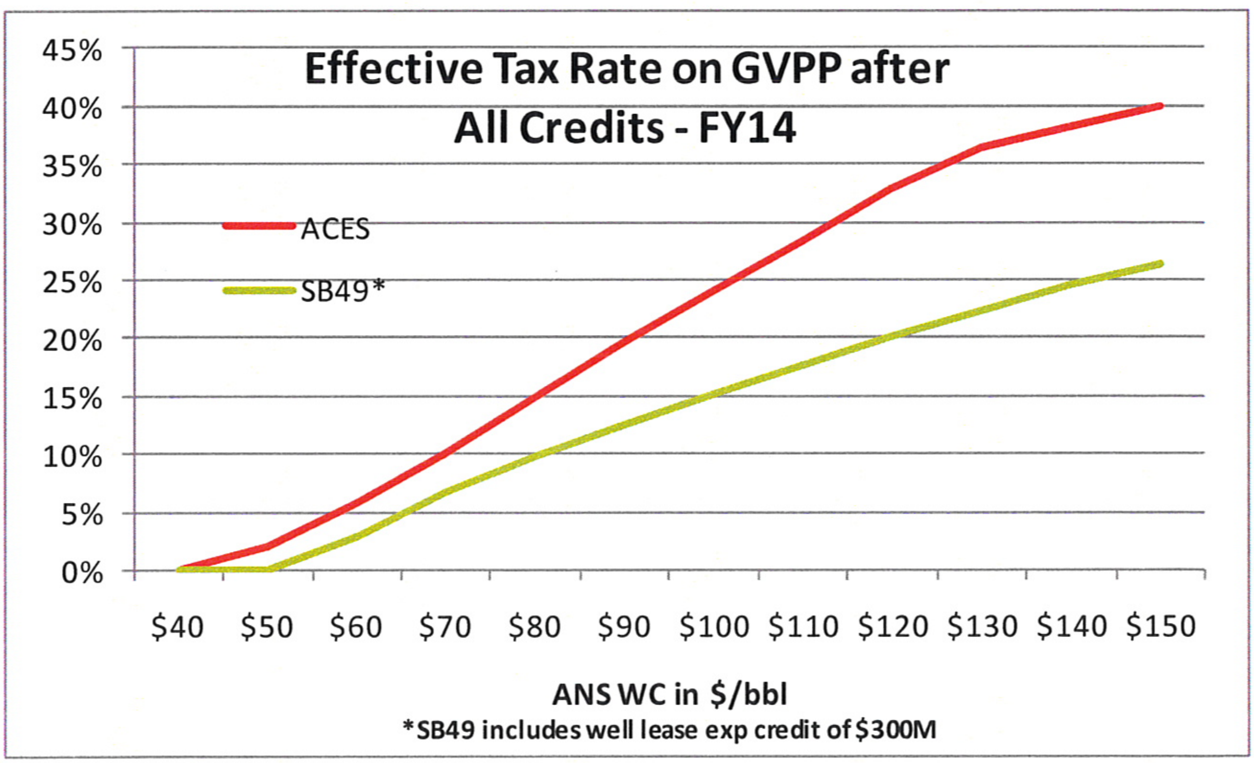
ANS WC in $/bbl
*SB49 includes well lease exp credit of $300M


Effective Tax Rate on GVPP after All Credits - FY14
45%
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ACES
SB49*
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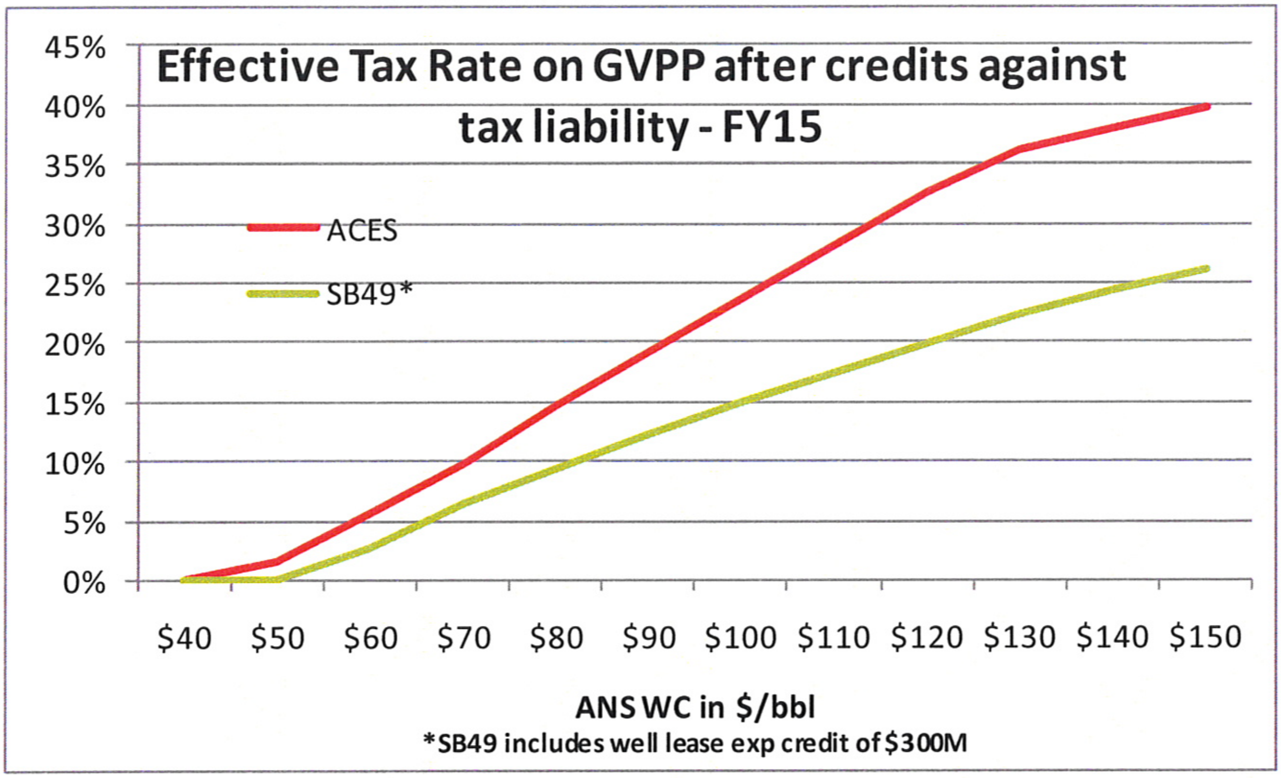
$140
$150
ANS WC in $/bbl
*SB49 includes well lease exp credit of $300M


Effective Tax Rate on GVPP after credits against tax liability - FY15
45%
40%
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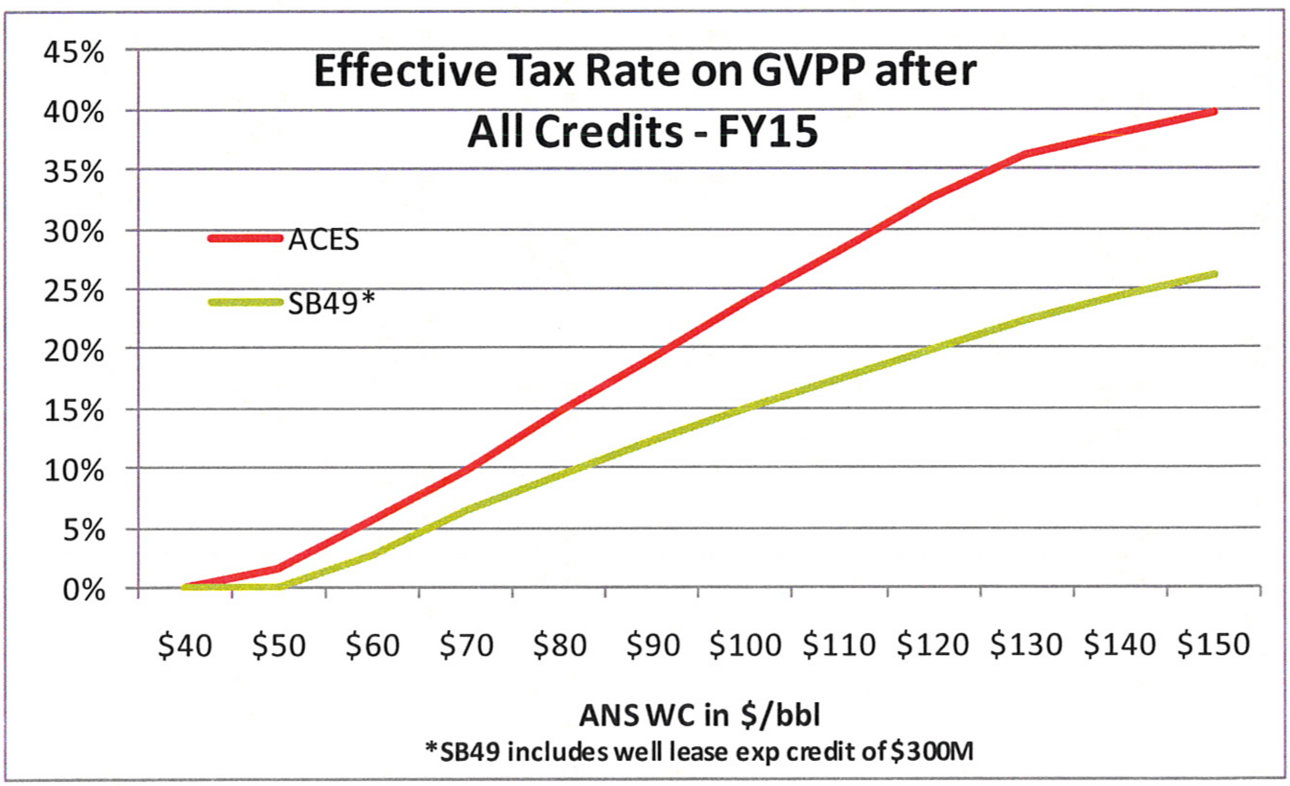
ACES
SB49*
$40 $50 $60 $70 $80 $90 $100 $110 $120 $130 $140 $150
ANS WC in $/bbl
*SB49 includes well lease exp credit of $300M


Effective Tax Rate on GVPP after All Credits - FY15
45%
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25%
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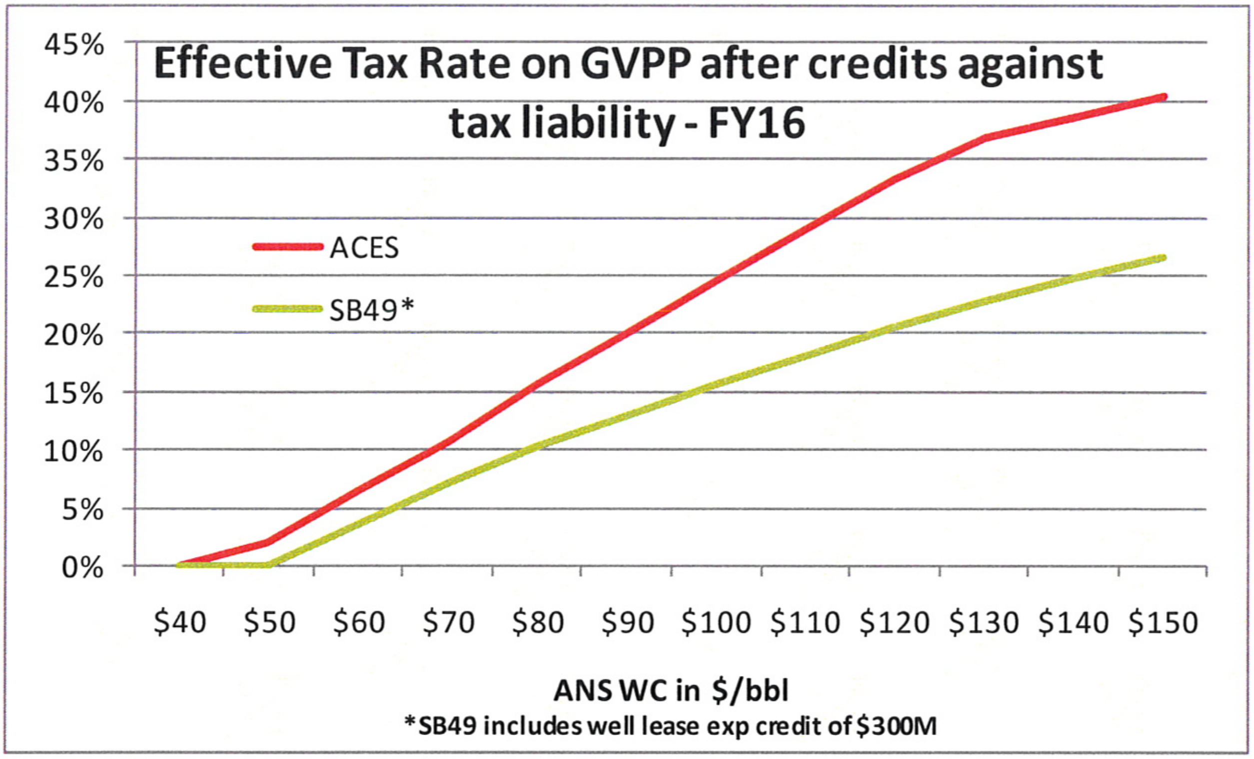
5%
0%
ACES
SB49*
$40 $50 $60 $70 $80 $90 $100 $110 $120 $130 $140 $150
ANS WC in $/bbl
*SB49 includes well lease exp credit of $300M


Effective Tax Rate on GVPP after credits against tax liability - FY16
45%
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35%
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25%
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5%
0%
ACES
SB49*
$40
$50
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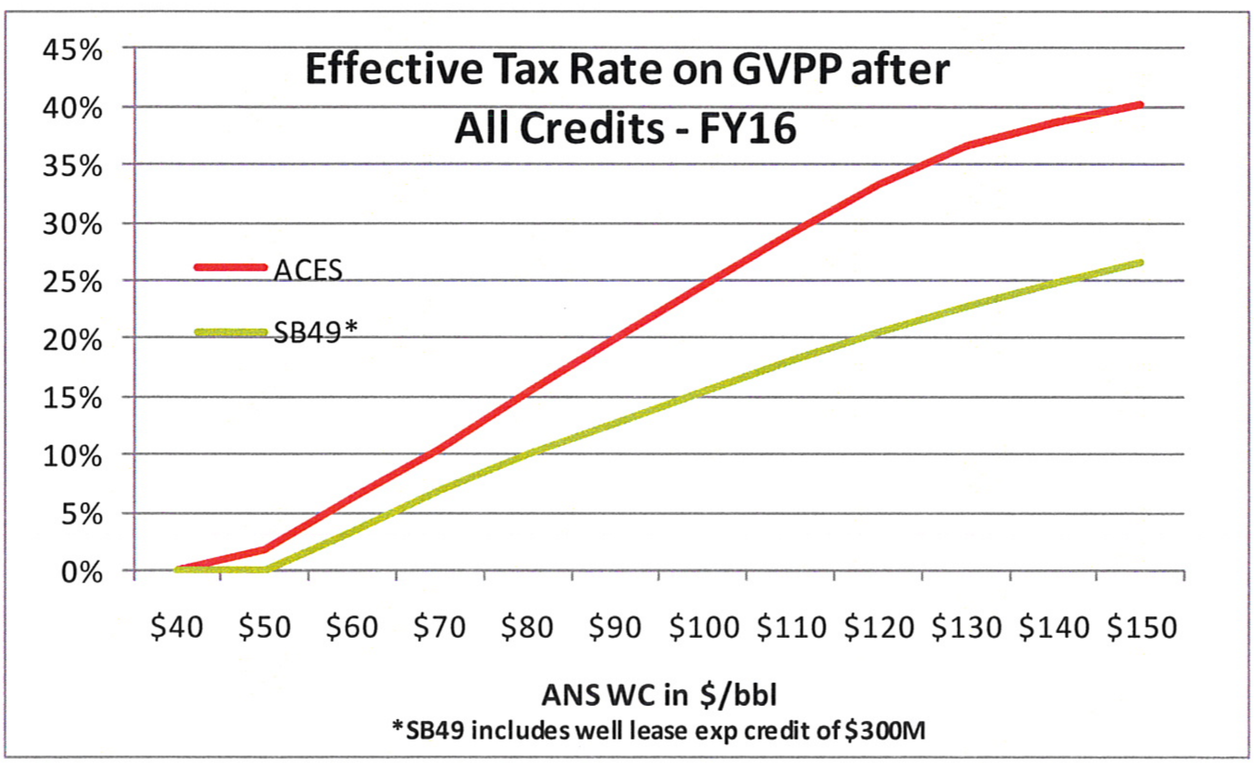
$140
$150
ANS WC in $/bbl
*SB49 includes well lease exp credit of $300M


Effective Tax Rate on GVPP after All Credits - FY16
45%
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ACES
SB49*
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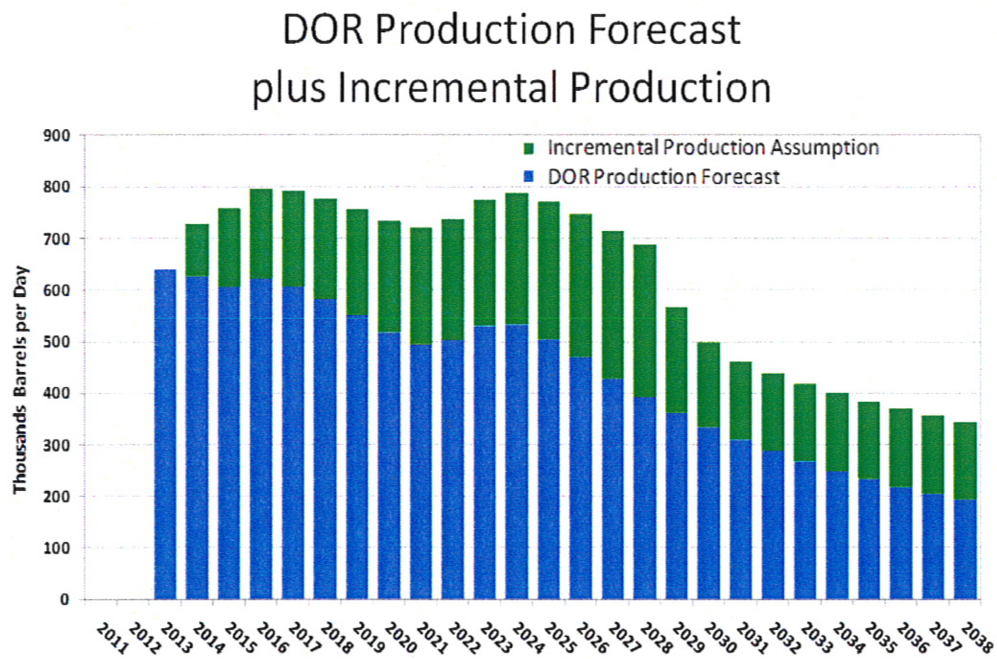
$140
$150
ANS WC in $/bbl
*SB49 includes well lease exp credit of $300M

3. Provide the analysis of the Great Bear scenario that was prepared for the House Resources Committee.

The following charts have been prepared to illustrate the potential impact of incremental production on state revenue. This illustration does not constitute a "best case scenario" but rather one single potential outcome out of a very wide range of possible production and price scenarios. The assumptions used are based on the Fall 2010 production and price forecasts and on recent industry testimony and as such, can be considered as neither excessively optimistic nor conservative. This scenario does not represent a Department of Revenue forecast or expectation. The analysis assumes that following the enactment of HB 110, incremental production beyond what is included in the Department's current production forecast would come from state lands. For this analysis, production included in the Department's forecast is assumed to be taxed at a 25% base rate and a maximum progressivity of 25% under HB 110. For illustration purposes, incremental production has been assumed to follow a profile similar to that presented by Great Bear Petroleum, as described in their 18th February, 2011 testimony[1]. This incremental production is assumed to come from currently non-unitized fields, which under HB 110, would be taxed at a 15% base rate and a maximum progressivity of 25%.



Source: DOR Production Profile; Fall 2010 Revenue Sources Book.
Incremental Production: Great Bear Petroleum; 18 February, 2011.

Overall, the enactment of HB 110 under this set of assumptions would reduce the "State Take" (all state revenues including production tax, royalty, corporate income tax and property tax) from

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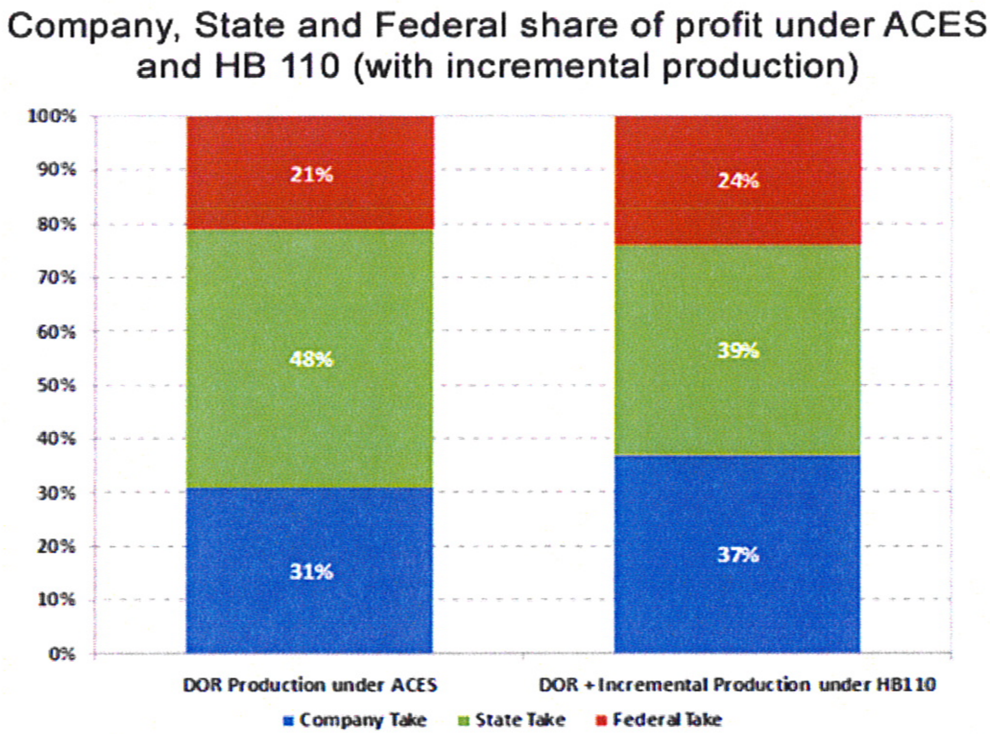
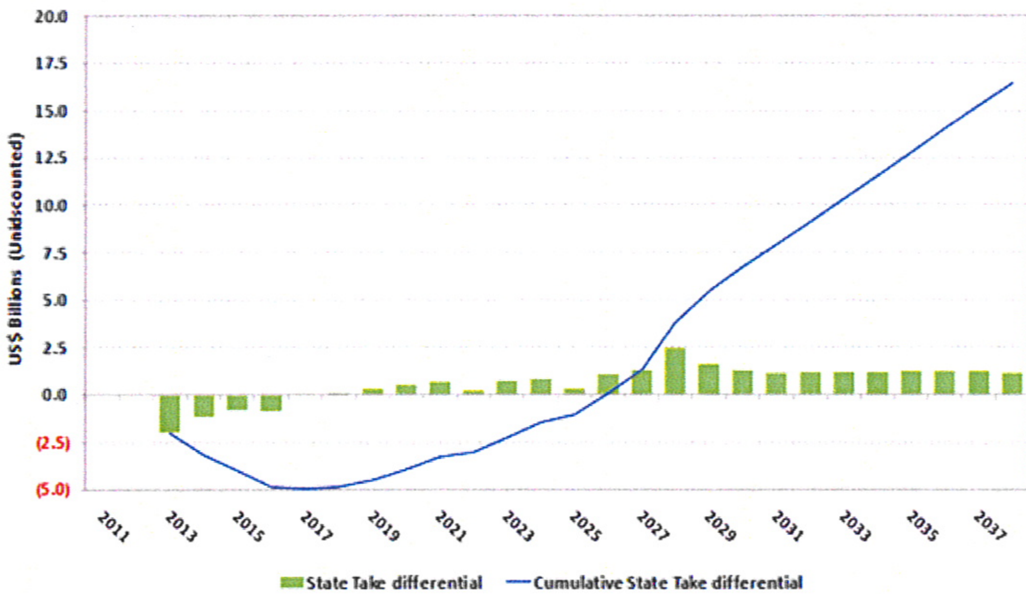
[1] Production starts in 2014 with 295 thousand barrels per day peak in 2028. Note: Great Bear Petroleum labels this as a 'Potential Oil Production Profile' and lists certain assumptions used in the preparation of this profile in their testimony.

48% to 39% of profits. Overall "Government Take", which also includes federal corporate income taxes, would be reduced from 69% to 63%.



However, while the relative State Take decreases under HB 110, it is applied to a "larger pie", which includes the assumed incremental production. Over the 2013 to 2038 period, total state revenue under HB 110, with the incremental production, would be $17 billion higher than it would be under ACES with no incremental production.

Additional state revenue under HB 110



Note: State Take for DOR + Incremental Production under HB110 minus State Take for DOR Production under ACES

Under the assumptions used, state revenue under HB 110, with the incremental production, would be higher than under the status quo beginning in 2018. Cumulative state revenue under the HB110 scenario starts exceeding what would have been received under ACES in 2026. As stated earlier, this is but one many potential scenarios as incremental production could conceivably be greater, or lower, than assumed for the purpose of this illustration.

We hope our responses fully answer your questions.

Sincerely,

Bruce Tangeman
Deputy Commissioner