SB 192 – Oil and Gas Production Tax Rate/Credit

Sponsored by Senator Bert Stedman

Senate Resources

April 9, 2014

Make Alaska Competitive

Repeal the

History of Alaska's Oil Tax Regimes

- Economic Limit Factor "ELF" (1977-2006)
- Petroleum Production Tax "PPT" (2006-2007)
- Alaska's Clear and Equitable Share "ACES" (2007-2014)
- Senate Bill 21 (2014-Present)

ELF (1977-2006)

- Severance tax rate of 15%
- Multiplied by a fraction between 0 and 1
- If the ELF was 0.5, the effective tax rate would be 7.5%

Problems with ELF

- Natural field decline reduced the tax rate regardless of price

- In 2007, Kuparuk’s economic limit factor was .065
  - 15 X .065 = 0.98%
  - The severance tax for North America’s second largest oil basin was less than one percent

- 15 of the 19 operating fields paid 0% tax rate

PPT (2006-2007)

- Base tax rate is 22.5% of net value after deducting costs
- Introduced progressivity element when net value per barrel > $40/bbl
    - (Net value per barrel - $40) X .0025
- So if oil price is $100 per barrel:
    - Net value per barrel is about $70
    - Progressivity is ($70 - $40) X .0025 = 7.5%
    - Total tax rate is 22.5% + 7.5% = 30%
    - Tax is 30% X $70 = $21 per barrel

Problems with PPT

- Deductible costs were higher than expected
- Revenues were less than expected
- Tainted by VECO corruption scandal

ACES (2007-2014)

- Base tax rate is 25% of net value after deducting costs
- Progressivity element when net value per barrel > $30/bbl
    - (Net value per barrel - $30) X .004
- So if oil price is $100 per barrel:
    - Net value per barrel is about $70
    - Progressivity is ($70 - $30) X .004 = 16%
    - Total tax rate is 25% + 16% = 41%
    - Production tax is 41% X $70 = $28.70 per barrel

Problems with ACES

- Progressivity rate was too high resulting in an unfair split of profit oil between producers and the state
- Excessive credits driving adverse economic behavior
- Complexity

Credits under ACES

- Capital credit - 20%
- Well lease expenditure credit (excluding North Slope) - 40%
- Exploration credit - 20% - 40% depending on location
- Small producer credit - $12 million if sufficient offsetting income
- Loss carry-forward credit - 25% of annual loss

Senate Bill 21 (2014-Present)

- Base tax rate is 35% of net value after deducting costs
- Per barrel tax credit between $1 - $8 based on Alaska North Slope (ANS) wellhead value
- 20% - 30% Gross Revenue Exclusion for new production
- Monetization of net operating losses – 45% through 2015 and 35% thereafter
- Minimum tax is 4% of gross value at point of production
- $12 million small producer tax credit

Problems with SB 21

- Per barrel tax credits are too high and not contingent on any performance measures
  - In FY15, the per barrel tax credits will cost the state almost one billion dollars
- 4% minimum tax is too low
  - The state’s risk exposure increases as oil prices drop
- Regressive tax structure without the per barrel tax credit
- **Bottom Line: Alaskan’s share of hydrocarbon value from the legacy fields is too low**

Senate Bill 192

- SB 192 cuts the per barrel credits in half
  - Almost half a billion dollars in revenue per year
- Raises the minimum tax from 4% to 15% of gross value at point of production
  - As oil prices go down and credits go up, a higher minimum tax is needed to protect the state's share of its resource wealth from legacy fields
  - No revenue impact at current oil price

Per Barrel Credits

ANS wellhead value	SB 21	SB 192
$140 - $150	$1	$.50
$130 - $140	$2	$1
$120 - $130	$3	$1.50
$110 - $120	$4	$2
$100 - $110	$5	$2.50
$90 - $100	$6	$3
$80 - $90	$7	$3.50
Less than $80	$8	$4

Government Take

- In 2012, Dr. Pedro van Meurs advised the legislature that a 70% – 75% government take for existing production in legacy fields is reasonable compared to similar jurisdictions

- Under SB 21, government take is too low in the legacy fields and unstable

Count the Cash

FY15 Forecast			
ANS West Coast Price **$105.06**	Daily Barrels	Annual Barrels	Annual $
Barrels of Oil Produced (North Slope)	498,400	181,916,000	$ 19,112,094,960
Gross Value (West Coast Price * Production)	$ 19,112,094,960		
Less: Net Royalty Value	$ (2,448,411,218)		
Equals: Gross Revenue (West Coast Price less Royalties)	$ 16,663,683,742		
Less: Total Downstream Costs (Transportation)	$ (1,590,869,483)		
Equals: ANS Wellhead Value (Gross Value at Point of Production)	$ 15,072,814,259		
Less: Upstream Costs (Opex)	$ (2,525,723,000)		
Less: Upstream Costs (Capex)	$ (4,453,400,000)		
Less: Property Tax	$ (314,577,000)		
Equals: Production Tax Value	$ 7,779,114,259		
		Effective Tax Rate	
Less: 35% Base Tax & Gross Revenue Exclusion	$ (2,658,845,331)	34.2%	
Per Barrel Tax Credit	$ 953,233,419	-12.3%	
Net Base Tax less Per Barrel Credit	$ (1,705,611,912)	21.9%	
Less: Loss Carry Forward Credit	$ 222,000,000		

North Dakota

- State of North Dakota take is 11.5% on gross + private royalty owner take is ± 20% on gross = 31.5% gross tax rate

- What if Alaska had the same tax and royalty regime as North Dakota?

Alaska (SB 21) vs. North Dakota

FY15 Forecast					
ANS West Coast Oil Price **$105.06**	Alaska			North Dakota	
Royalties	$	2,319,900,000		$	3,822,418,992
Base Tax	$	2,658,845,331		$	2,197,890,920
Per Barrel Credit	$	(953,233,419)			-
Other Credits	$	(222,000,000)			-
Property Tax	$	314,577,000			-
Income Tax	$	446,971,607			-
Total	$	4,565,060,518		$	6,020,309,912
A difference of	$	(1,455,249,394)			

Alaska (ACES) vs. North Dakota

FY13 Historic				
ANS West Coast Oil Price $107.57	Alaska		North Dakota	
Royalties	$	2,741,084,670	$	4,174,447,476
Base Tax	$	2,782,853,629	$	2,400,307,299
Progressivity	$	1,805,764,038		-
Credits	$	(830,000,000)		-
Property Tax	$	314,577,000		-
Income Tax	$	523,468,576		-
Total	$	7,337,747,913	$	6,574,754,775
A difference of	$	762,993,138		

Alaska is Different

- Alaska is an owner state, the mineral rights are owned collectively by the people

- The oil belongs to every Alaskan and the production tax is nothing more than the selling price of our oil

Value of Legacy Fields

- Not necessary to reduce the tax in the legacy fields of Prudhoe and Kuparuk where production is already economic
- Net present value and internal rate of return surpass the industries hurdle rate and are extremely profitable
- There are approximately 7 billion barrels of proven reserves that are "**technically, economically and legally deliverable**" in the legacy fields*
- An approximate value of $800 billion at current oil prices
- The value of the remaining reservoir is higher than the cumulative value of all the North Slope oil produced to date

*2011 State Superior Court ruling in BP Pipelines, et al. v. State et al. as upheld by 2014 State Supreme Court ruling

Make Alaska Competitive with North Dakota

- Repeal the going out of business sale