THE STATE of ALASKA
GOVERNOR MIKE DUNLEAVY

Department of Revenue

TAX DIVISION

550 W. Seventh Ave., Suite 500
Anchorage, Alaska 99501-3555
Main: 907.269.6620
Fax: 907.269.6644

March 10, 2022

The Honorable Click Bishop
Alaska State Senator
Co-Chair, Senate Finance Committee
State Capitol Room 516
Juneau, AK 99801

The Honorable Bert Stedman
Alaska State Senator
Co-Chair, Senate Finance Committee
State Capitol Room 518
Juneau, AK 99801

Dear Co-Chairs Bishop and Stedman,

The purpose of this letter is to provide you with responses and clarifications to the questions asked of the Department of Revenue (DOR) during the presentation to the Senate Finance Committee on March 2, 2022. We are also providing a corrected version of a slide from the original slide deck.

1. Is there a regulated return that Alaska pipeline companies receive for the service they provide?

The tariff calculation for the Trans-Alaska Pipeline System (TAPS) includes a 10.86% allowable equity return per the TAPS Variable Tariff Methodology Settlement (2017). As part of the settlement, the TAPS Owners have the ability to revise that return, but they have not started that process. DOR reviewed tariff filings and settlement agreements for several other Federal Energy Regulatory Commission (FERC) and Regulatory Commission of Alaska (RCA) regulated pipelines within Alaska. The regulated rates of return for those pipelines were between 10% and 14%.

2. Please provide the effective tax rate as part of the income statement slide for FY 2023.

For FY 2023, the estimated effective production tax rate for North Slope oil, as a percentage of production tax value, is about 13%. This is based on Fall 2021 forecast assumptions. Currently, oil prices are higher than forecasted and at higher oil prices the effective production tax rate would also be higher.

3. If the per-taxable-barrel credit for non-Gross Value Reduction (non-GVR) eligible production was capped at $5 per taxable barrel, at what oil price would companies begin to pay above the minimum tax floor?

As stated in testimony, under the Fall 2021 forecast assumptions, estimated North Slope production tax revenue for FY 2023 would exceed the minimum tax floor at prices above $50 per barrel. The exact “crossover” point varies by company and generally ranges from $50 to $70 per barrel for most taxpayers.

If the per-taxable-barrel credit for non-GVR production were capped at $5 per taxable barrel, holding all else equal, estimated North Slope production tax revenue for FY 2023 would exceed the aggregate minimum tax floor at prices above $42 per barrel. Again, the exact “crossover” point would vary by company and generally would range from $40 to $55 per barrel for most taxpayers. This analysis does not consider any potential changes in company behavior, investment, or production as a result of a tax increase.

4. Please provide an additional line at the bottom of Slide 18 showing the accumulation of lease expenditures from prior years plus the lease expenditures from the current year in order to show the total liability to the state at the end of each fiscal year. Also include an additional line showing the effective production tax rate for each year.

Below please find the requested updated table. The additional calculations have been added in two new rows at the bottom of the table.

	ACTUAL FY 2020		ACTUAL FY 2021		Current Year FY 2022		Forecast FY 2023		Forecast FY 2024	
	Value ($ million)		Value ($ million)		Value ($ million)		Value ($ million)		Value ($ million)	
Total Annual Production/Value	**$8,999.3**		**$9,605.1**		**$13,452.7**		**$12,962.4**		**$12,664.4**	
Royalty and Federal barrels	($1,110.0)		($1,196.2)		($1,648.1)		($1,588.6)		($1,611.9)	
Taxable Barrels	**$7,889.3**		**$8,408.9**		**$11,804.6**		**$11,373.7**		**$11,052.5**	
Transportation Costs	($1,234.9)		($1,427.9)		($1,511.5)		($1,456.6)		($1,439.9)	
Gross Value at Point of Production	**$6,654.4**		**$6,981.0**		**$10,293.1**		**$9,917.1**		**$9,612.5**	
North Slope Lease Expenditures										
Deductible Operating Expenditures	($2,245.8)		($2,135.0)		($2,339.1)		($2,449.1)		($2,530.2)	
Deductible Capital Expenditures	($2,031.8)		($1,390.5)		($1,367.8)		($1,638.4)		($1,700.3)	
Total Lease Expenditures	($4,277.5)		($3,525.5)		($3,706.9)		($4,087.4)		($4,230.5)	
Production Tax Value (PTV)	**$2,376.8**		**$3,455.5**		**$6,586.2**		**$5,829.7**		**$5,382.0**	
Production Tax	Min Tax Floor	Net Tax	Min Tax Floor	Net Tax	Min Tax Floor	Net Tax	Min Tax Floor	Net Tax	Min Tax Floor	Net Tax
Gross Value or Production Tax Value	$6,654.4	$2,376.8	$6,981.0	$3,455.5	$10,293.1	$6,586.2	$9,917.1	$5,829.7	$9,612.5	$5,382.0
Gross Value Reduction (GVR)	$0.0	($82.7)	$0.0	($66.3)	$0.0	($148.5)	$0.0	($129.7)	$0.0	($105.3)
GVPP or PTV after GVR	**$6,654.4**	**$2,294.1**	**$6,981.0**	**$3,389.2**	**$10,293.1**	**$6,437.7**	**$9,917.1**	**$5,700.0**	**$9,612.5**	**$5,276.7**
Tax rate	4%	35%	4%	35%	4%	35%	4%	35%	4%	35%
Tax before credits	**$266.2**	**$802.9**	**$279.2**	**$1,186.2**	**$411.7**	**$2,253.2**	**$396.7**	**$1,995.0**	**$384.5**	**$1,846.9**
Higher of minimum tax floor or net tax	**$802.9**		**$1,186.2**		**$2,253.2**		**$1,995.0**		**$1,846.9**	
Per-taxable-barrel credits	($586.3)		($740.4)		($1,234.1)		($1,247.3)		($1,238.6)	
Other credits against liability	($7.8)		($46.9)		($58.5)		($0.6)		($0.5)	
Total Tax after credits	**$208.9**		**$399.0**		**$960.6**		**$747.1**		**$607.8**	
Other items / adjustments	$76.2		($10.0)		$19.0		($5.9)		$13.1	
Total Tax paid to the state [1]	**$285.1**		**$389.0**		**$979.6**		**$741.2**		**$621.0**	
Net New Lease Expenditures Earned and Carried Forward [2]	*$412.0**		*$510.6*		*$597.5*		*$680.8*		*$664.1*	
Total Carried Forward Lease Expenditures [2]	**$412.0**		**$922.6**		**$1,520.1**		**$2,200.9**		**$2,865.0**	
Effective Tax Rate	**12%**		**11%**		**15%**		**13%**		**12%**	

[1] Amount includes hazardous release surcharge for FY 2020 and FY 2021 but not FY 2022+

[2] Entire balance as of end of FY 2020 is attributed to FY 2020 for this presentation.

Corrections and Clarifications to Testimony:

In addition to answering the follow-up questions above, we wish to provide clarifications to a few questions answered in testimony on 3/2/2022.

1. A question was asked about whether carried-forward lease expenditures could be transferred, and we responded that they cannot. While this is generally the case, we wish to clarify that there are specific instances where a carried-forward lease expenditure could be transferred. This would require a transfer of the lease or property in which the carried-forward lease expenditure was earned, and the lease expenditure could transfer with the lease or property. Further, an acquiring company would need to bring the lease or property into production to utilize any benefit from the carried-forward lease expenditure.

2. A question was asked about why the per-barrel amounts for the per-taxable-barrel tax credits shown in the income statement were lower than $8 and $5 per taxable barrel, and we responded that the amounts shown reflected an average value across all producers. While this is accurate,, the more complete explanation is that the averages shown in the presentation ($7.45 and $0.33 per-taxable-barrel) were calculated by dividing the total value of each credit by the total estimated taxable barrels, not just the taxable barrels for GVR or non-GVR production. Dividing only by the relevant taxable production, the average per-taxable-barrel credit for GVR-eligible production would be $4.99 per taxable barrel for FY 2023, and the average per-taxable-barrel credit for non-GVR-eligible production would be $7.99 per taxable barrel for FY 2023. DOR will consider updating how these are reflected in future presentations.

3. A question was asked about which land types are eligible for GVR. To clarify, a 20% GVR is available for any qualifying new production on the North Slope that is subject to the production tax, regardless of land ownership. The 30% GVR is available for qualifying new production that is comprised exclusively of state-issued leases with a royalty rate of greater than 12.5%.

4. Following the presentation, we discovered that Slide 19, which presented an aggregate production tax calculation, misstated what production tax revenue would be with a single taxpayer under the Fall 2021 forecast. A corrected version of the chart from Slide 19 is included below.

   In testimony, we stated that the state would receive more revenue with a single taxpayer. This was true under the Fall 2020 forecast, because a single taxpayer would not be able to realize value from per-taxable-barrel credits for non-GVR production due to the minimum tax floor. However, this is incorrect for the Fall 2021 forecast due to the higher oil price forecast, and the state would receive slightly less revenue with a single taxpayer under the Fall 2021 forecast. For FY 2023, at the forecast price of $71 per barrel, a single taxpayer would be able to utilize 100% of the value of all per-taxable-barrel credits, while in the forecast we assume that a small portion of the credits would be forfeited(?) by minor producers.

Illustration Assuming a Single North Slope Taxpayer: FY 2023

	Per Barrel	Barrels	Value ($ million)	
Avg ANS Oil Price ($/bbl) & Daily Production (ths bbls)	***$71.00***	***500.2***	***$35.5***	
Total Annual Production/Value	**$71.00**	**182,569**	**$12,962.4**	
Royalty and Federal barrels		(22,375)	($1,588.6)	
Taxable Barrels	**$71.00**	**160,194**	**$11,373.7**	
Downstream (Transportation) Costs ($/bbl)	($9.09)	0	($1,456.6)	
Gross Value at Point of Production (GVPP)	**$61.91**	**160,194**	**$9,917.1**	
North Slope Lease Expenditures				
Deductible Operating Expenditures	($15.29)		($2,449.1)	
Deductible Capital Expenditures	($10.23)		($1,638.4)	
Total Lease Expenditures	($25.52)		($4,087.4)	
Production Tax Value (PTV)	**$36.39**	**160,194**	**$5,829.7**	
Production Tax			Min Tax Floor	Net Tax
Gross Value or Production Tax Value			$9,917.1	$5,829.7
Gross Value Reduction (GVR)			$0.0	($132.2)
GVPP or PTV after GVR			**$9,917.1**	**$5,697.5**
Tax rate			4%	35%
Tax before credits			**$396.7**	**$1,994.1**
Higher of minimum tax floor or net tax	**$12.45**	**160,194**	**$1,994.1**	
GVR Per-taxable-barrel credits	($0.33)		($53.4)	
Non-GVR Per-taxable barrel credits	($7.47)		($1,196.1)	
Tax after per barrel credits	**$4.65**	**160,194**	**$744.6**	
Other items/adjustments			($6.5)	
Total tax paid to state	**$4.61**	**160,194**	**$738.1**	

***This illustration assumes a single North Slope taxpayer for simplification and will not equate to the FY 2023 production tax estimate. In practice, the application of the per-taxable barrel credits will depend on the individual taxpayer's circumstances.**

I hope you find this information to be useful. Please do not hesitate to contact me if you have further questions.

Sincerely,

DocuSigned by:
Colleen Glover
CD6B2B88C07447E...

Colleen M. Glover
Tax Division Director