

**ALASKA STATE LEGISLATURE
HOUSE RESOURCES STANDING COMMITTEE**

March 15, 2006

1:18 p.m.

MEMBERS PRESENT

Representative Jay Ramras, Co-Chair
Representative Ralph Samuels, Co-Chair
Representative Jim Elkins
Representative Carl Gatto
Representative Gabrielle LeDoux
Representative Kurt Olson
Representative Paul Seaton
Representative Harry Crawford
Representative Mary Kapsner

MEMBERS ABSENT

All members present

COMMITTEE CALENDAR

HOUSE BILL NO. 488

"An Act repealing the oil production tax and gas production tax and providing for a production tax on the net value of oil and gas; relating to the relationship of the production tax to other taxes; relating to the dates tax payments and surcharges are due under AS 43.55; relating to interest on overpayments under AS 43.55; relating to the treatment of oil and gas production tax in a producer's settlement with the royalty owner; relating to flared gas, and to oil and gas used in the operation of a lease or property, under AS 43.55; relating to the prevailing value of oil or gas under AS 43.55; providing for tax credits against the tax due under AS 43.55 for certain expenditures, losses, and surcharges; relating to statements or other information required to be filed with or furnished to the Department of Revenue, and relating to the penalty for failure to file certain reports, under AS 43.55; relating to the powers of the Department of Revenue, and to the disclosure of certain information required to be furnished to the Department of Revenue, under AS 43.55; relating to criminal penalties for violating conditions governing access to and use of confidential information relating to the oil and gas production tax; relating to the deposit of money collected by the Department of Revenue under AS 43.55; relating to the calculation of the gross value at the point of production of oil or gas; relating to the determination of the net value of taxable oil and gas for purposes of a production

tax on the net value of oil and gas; relating to the definitions of 'gas,' 'oil,' and certain other terms for purposes of AS 43.55; making conforming amendments; and providing for an effective date."

- HEARD AND HELD

PREVIOUS COMMITTEE ACTION

BILL: HB 488

SHORT TITLE: OIL AND GAS PRODUCTION TAX

SPONSOR(S): RULES BY REQUEST OF THE GOVERNOR

02/21/06	(H)	READ THE FIRST TIME - REFERRALS
02/21/06	(H)	RES, FIN
02/22/06	(H)	RES AT 12:30 AM HOUSE FINANCE 519
02/22/06	(H)	Heard & Held
02/22/06	(H)	MINUTE(RES)
02/23/06	(H)	RES AT 12:30 AM HOUSE FINANCE 519
02/23/06	(H)	Heard & Held
02/23/06	(H)	MINUTE(RES)
02/24/06	(H)	RES AT 12:30 AM HOUSE FINANCE 519
02/24/06	(H)	Heard & Held
02/24/06	(H)	MINUTE(RES)
02/25/06	(H)	RES AT 10:00 AM SENATE FINANCE 532
02/25/06	(H)	Joint with Senate Resources
02/27/06	(H)	RES AT 12:30 AM CAPITOL 124
02/27/06	(H)	Heard & Held
02/27/06	(H)	MINUTE(RES)
02/28/06	(H)	RES AT 12:30 AM CAPITOL 124
02/28/06	(H)	Heard & Held
02/28/06	(H)	MINUTE(RES)
03/01/06	(H)	RES AT 12:30 AM CAPITOL 124
03/01/06	(H)	Heard & Held
03/01/06	(H)	MINUTE(RES)
03/02/06	(H)	RES AT 12:00 AM CAPITOL 124
03/02/06	(H)	Heard & Held
03/02/06	(H)	MINUTE(RES)
03/03/06	(H)	RES AT 12:30 AM CAPITOL 124
03/03/06	(H)	Heard & Held
03/03/06	(H)	MINUTE(RES)
03/04/06	(H)	RES AT 2:00 PM HOUSE FINANCE 519
03/04/06	(H)	Heard & Held
03/04/06	(H)	MINUTE(RES)
03/06/06	(H)	FIN AT 12:30 AM HOUSE FINANCE 519
03/06/06	(H)	Presentation by Legislative Consultant
03/06/06	(H)	RES AT 12:30 AM HOUSE FINANCE 519

03/06/06	(H)	Testimony by legislative consultant
03/07/06	(H)	RES AT 12:30 AM CAPITOL 124
03/07/06	(H)	Heard & Held
03/07/06	(H)	MINUTE(RES)
03/08/06	(H)	RES AT 12:30 AM CAPITOL 106
03/08/06	(H)	-- Meeting Canceled --
03/09/06	(H)	RES AT 12:30 AM CAPITOL 106
03/09/06	(H)	-- Meeting Canceled --
03/10/06	(H)	RES AT 12:30 AM CAPITOL 106
03/10/06	(H)	Heard & Held
03/10/06	(H)	MINUTE(RES)
03/11/06	(H)	RES AT 10:00 AM CAPITOL 106
03/11/06	(H)	-- Meeting Canceled --
03/13/06	(H)	RES AT 10:00 AM CAPITOL 124
03/13/06	(H)	Heard & Held
03/13/06	(H)	MINUTE(RES)
03/14/06	(H)	RES AT 12:30 AM CAPITOL 124
03/14/06	(H)	Heard & Held
03/14/06	(H)	MINUTE(RES)
03/15/06	(H)	RES AT 1:15 PM CAPITOL 124

WITNESS REGISTER

BRIAN WENZEL, Vice President of Finance and Administration
 ConocoPhillips Alaska, Inc.
 Anchorage, Alaska
 POSITION STATEMENT: Testified against changes to HB 488.

PAT FOLEY, Manager
 Lands and External Affairs
 Pioneer Natural Resources
 Anchorage, Alaska
 POSITION STATEMENT: Testified against changes to HB 488.

MARK HANLEY, Manager
 Public Relations
 Anadarko Oil Company
 Anchorage, Alaska
 POSITION STATEMENT: Testified against changes to HB 488.

ANGUS WALKER, Commercial Vice President
 BP Alaska
 Anchorage, Alaska
 POSITION STATEMENT: Testified against changes to HB 488.

TOM WILLIAMS, Tax Counsel
 BP Alaska

Anchorage, Alaska

POSITION STATEMENT: Testified against changes to HB 488.

JOHN ZAGER, General Manager

Alaska Chevron

Anchorage, Alaska

POSITION STATEMENT: Testified against changes to HB 488.

TIM ENGLAND, Senior Manager

Global New Ventures

Talisman Energy Inc.

Calgary, Alberta, Canada

POSITION STATEMENT: Testified against changes to HB 488.

JON HANDFORTH, Manager

International and Frontier Operations

Talisman Energy

Calgary, Alberta, Canada

POSITION STATEMENT: Testified against changes to HB 488.

RICHARD OWEN, Production Manager

ExxonMobil Corporation Alaska

Vice President

ExxonMobil Alaska Production

Anchorage, Alaska

POSITION STATEMENT: Testified against changes to HB 488.

ACTION NARRATIVE

CO-CHAIR RALPH SAMUELS called the House Resources Standing Committee meeting to order at [1:18:44 PM](#). Representatives Samuels, Gatto, Kapsner, Elkins, Crawford, Seaton, Ramras, and Olson were present at the call to order. Representative LeDoux arrived as the meeting was in progress.

HB 488-OIL AND GAS PRODUCTION TAX

CO-CHAIR SAMUELS announced that the only order of business would be HOUSE BILL NO. 488, "An Act repealing the oil production tax and gas production tax and providing for a production tax on the net value of oil and gas; relating to the relationship of the production tax to other taxes; relating to the dates tax payments and surcharges are due under AS 43.55; relating to interest on overpayments under AS 43.55; relating to the treatment of oil and gas production tax in a producer's settlement with the royalty owner; relating to flared gas, and to oil and gas used in the operation of a lease or property,

under AS 43.55; relating to the prevailing value of oil or gas under AS 43.55; providing for tax credits against the tax due under AS 43.55 for certain expenditures, losses, and surcharges; relating to statements or other information required to be filed with or furnished to the Department of Revenue, and relating to the penalty for failure to file certain reports, under AS 43.55; relating to the powers of the Department of Revenue, and to the disclosure of certain information required to be furnished to the Department of Revenue, under AS 43.55; relating to criminal penalties for violating conditions governing access to and use of confidential information relating to the oil and gas production tax; relating to the deposit of money collected by the Department of Revenue under AS 43.55; relating to the calculation of the gross value at the point of production of oil or gas; relating to the determination of the net value of taxable oil and gas for purposes of a production tax on the net value of oil and gas; relating to the definitions of 'gas,' 'oil,' and certain other terms for purposes of AS 43.55; making conforming amendments; and providing for an effective date."

CO-CHAIR SAMUELS noted that there is a Committee Substitute (CS) that will be ready soon, and the major changes brought about by the forthcoming CS were made public the previous day. He said it is being reviewed by Robert Mintz of the Department of Law.

1:20:44 PM

BRIAN WENZEL, Vice President of Finance and Administration, ConocoPhillips Alaska, Inc. (Conoco), said the changes presented by the House Resources Standing Committee will have a negative impact on the attractiveness of investments in Alaska by Conoco. He said Conoco absolutely opposes any proposals that increase its taxes beyond the \$1 billion per year proposed by the governor. He said the CS increases taxes by \$18 billion over the next 10 years if oil prices stay the same. He said the proposal puts state revenue and jobs for Alaskans at risk. The CS destroys the balance that was contained in HB 488. He said consultants informed the committee that the state may see an increase in investments by such a tax, but he said Conoco has hired consultants too. The consultants aren't the ones who need to live with the tax. The consultants who are telling the committee that the CS will not have a negative impact are wrong, he opined. Taking away billions of dollars from his industry will have a negative impact, and taking a significant portion of the upside potential in a basin that has long lead times and low prospectivity will negatively affect investments and state

revenue. "It is a natural consequence of the action you are taking," he stated.

1:24:52 PM

MR. WENZEL said the CS will cause Conoco and others to lose confidence in the state. He said the unreasonable changes in the CS will cause investors to question when Alaska will again change its tax regime and again "impose an unfair, unreasonable burden." It is irrelevant if the future change will be a production tax, property tax, corporate income tax or a new tax. "The point is that investors will now need to consider another significant risk in making their economic decisions in Alaska: the risk that Alaska will not approach future fiscal policy changes in a reasonable manner that recognizes the commitment and contributions" of Conoco and others. He said, "As an example of the type of thinking that will negatively affect potential future investors' view of Alaska," Conoco received a letter from Alaska Representative Les Gara and Senator Hollis French regarding Conoco's media ads. The letter suggests that private sector profits are bad, that state government has not shared in the benefit of higher oil prices, and that Conoco's commitment is irrelevant. He is concerned about the antipathy expressed in the letter. "It has become, for some, an exercise in seeing how much the state can take from the private sector for no other reason [than to] simply take more." "Unfortunately this CS is structured to take more from the very industry participants that are most committed to Alaska's future."

1:27:10 PM

MR. WENZEL said the House Resources Standing Committee has destroyed the balance in the governor's bill. The proposed profit-based petroleum production tax (PPT) is, in effect, a windfall profit tax. At today's prices it will triple the tax rate of the current Alaska tax system. "This change is neither fair or reasonable to current investors and will be viewed as unreasonable and unfair by potential future investors," he stated. The CS penalizes the very companies that have been developing oil and creating jobs in Alaska. It reduces the value of credits. "These credits only affect about 4 percent of the Department of Revenue's expected future sources of production and investment in Alaska," he stated.

1:28:50 PM

MR. WENZEL said, "You have reduced by over 30 percent the effective value of the base allowance, which is intended to encourage small explorers and new entrants. You have moved the effective date of this bill back to a completely impractical date." He said procedures and computer systems "cannot possibly be adopted by April 1 of this year, which means that production taxpayers in Alaska will have to guess at their tax liability, make unsupported payments of tax in an uncertain attempt to avoid punitive interest cost. And you have suggested a punitive interest penalty of 5 percent on top of a statutory rate of 11 percent, which, obviously already includes a punitive element." He said the changes in the CS are completely inconsistent with the goals of a fair and reasonable fiscal policy," he said.

[1:30:03 PM](#)

CO-CHAIR RAMRAS thanked Mr. Wenzel for his thoughtful and sensitive testimony.

REPRESENTATIVE KAPSNER asked for a copy of the letter from Representative Gara and Senator French.

[1:30:19 PM](#)

REPRESENTATIVE KAPSNER said the industry recognized that it was time to make a change in taxes and it's done once in a great while, "so I do have concerns with the ads that you are running giving the public the perception that redoing our taxes is completely unthinkable."

MR. WENZEL said the point of Conoco's ads is that Conoco sees where the legislature is going, including the summary of the House Resources' CS, and it is not a balanced and reasonable approach. It is a tax and spend approach, he stated.

REPRESENTATIVE KAPSNER asked if Conoco made the commercial after the CS summary was developed.

MR. WENZEL said no; the commercials were done before, "but many of these questions have been coming along. The CS has not yet been released." He stated that the governor's bill is balanced, and "it was a hard pill for us to swallow," but it was accepted in order to go forward with investment and the gas pipeline.

[1:32:10 PM](#)

REPRESENTATIVE KAPSNER said the industry felt that the bill from the governor was an end product. Speaking from the legislative branch, she said it is "pretty far reaching to expect 60 members of the legislature who are elected to represent their own communities, to just say, 'Oh, this is what the governor decided, OK...Our work is done.'" There are three branches of government; the legislature appropriates the budget, sets taxes and makes laws. The governor signs the laws and upholds them. She said, "It is within our purview to take a look at the governor's product. And I think that it is insulting, to a large degree, to think that we should just say our work is done before we take into consideration what the consultants said. Every consultant that has been before us has said 25/20 is a good starting point."

[1:33:48 PM](#)

MR. WENZEL said no one has said not to debate the bill, in fact "we recognize the sovereignty of the legislature." He said his hope was that by meeting with legislators privately and by testimony, he could help the legislature come to the same view as the governor in terms of meeting the needs of the state and growing the industry. He said he hoped that the legislature would come to the same conclusion. He said he never heard the committee discuss lowering the tax rate in order to stimulate more investment.

[1:35:15 PM](#)

REPRESENTATIVE GATTO said he heard Mr. Wenzel say that if oil prices continue then Conoco will lose \$1.8 billion [under the CS]. If prices continue at about \$62 per barrel, he asked, how much will Conoco profit in Alaska?

MR. WENZEL said he doesn't have that number. He said there is no dispute that Conoco will make significant profits at that time.

REPRESENTATIVE GATTO said he is suggesting that there must be some level of oil price where Conoco thinks it is unbalanced--a term Mr. Wenzel uses. Current taxes are substantially unbalanced like a "teeter totter that is shoved all the way to one end, and what we are trying to do is rebalance the teeter totter." He said, "Of course the person who had the advantage is going to say the initial proposal was tolerable, but it didn't really lead to a balance." He said he saw the television ads, and he thought, as well as a lot people, that the ads were

dirty. The ads tried to convince the public that Conoco was in trouble and would pull out of Alaska because of taxation. He said he wishes he had the money to write a TV ad in order to present the other side of the issue. He said Conoco should be on notice that that sort of thing doesn't help because it is one-sided. He said it is an issue of fairness. He said that is why he asks the question: "At current prices, a reduction of \$1.8 billion in ConocoPhillips' profits represents what? Is it truly unfair? If we turned around and wrote you a check for \$1.8 billion on top of what you're going to make at the current prices, wouldn't you think that is the most unfair thing we could do?"

[1:38:54 PM](#)

MR. WENZEL said he disagrees on several counts. Conoco looks at "that profit tax, that structuring, with a net cash flow element as a very progressive tax. "As the industry does better, the state also will receive more in tax revenue." He said it is not simply a flat dollar amount, so the original bill was balanced at all prices. He said Representative Gatto seemed to imply that Conoco is not going to run away, and Mr. Wenzel said that was right because the company has too much invested in large assets. He noted that those large assets take money to maintain, and if Conoco loses confidence to make big long-term investments there will be a decline in jobs and revenues.

[1:40:43 PM](#)

MR. WENZEL said his company will make money at high prices, but the state receives a lot money by having Conoco here.

REPRESENTATIVE CRAWFORD said since this all started, he has asked questions to the oil companies of what they based their projections on and has never gotten any answer other than "your guess is about as good as mine." He noted that Mr. Wenzel presented firm numbers about how much Conoco will lose in taxes. He asked what he was basing that on, because if oil prices are under \$32 per barrel, this bill allows Conoco to pay less tax than under the current system, so "this makes you money." He said there is plenty to be unhappy about on every side. He really worries about Alaska at the lower end, "although \$32 a barrel would have made us all real overjoyed two or three years ago."

[1:43:26 PM](#)

MR. WENZEL said Conoco does not make their price forecast public, but economists aren't saying that prices will rise. He used the number that the administration used at today's prices. He said Representative Crawford's guess is as good as Conoco's in terms of whether the price of oil will stay at current levels. He said the PPT results in Conoco perhaps paying less taxes than under the current tax system. The premise is that the state was willing to accept that downside to get more from the upside. He said the PPT system is beneficial to the industry when profits are down.

[1:45:32 PM](#)

REPRESENTATIVE LEDOUX said Conoco didn't create its ads when the CS summary came out. She asked when the company did create them.

MR. WENZEL said it was in the last week or more that Conoco put those ads together. He said it was based on the fact that testimony has been one-sided, and it was his company's obligation to show the other side.

[1:46:39 PM](#)

REPRESENTATIVE OLSON expressed his understanding that Conoco is going into Libya.

MR. WENZEL said that is correct.

REPRESENTATIVE OLSON noted that all American companies were thrown out 20 years ago and the industry was nationalized. He asked what the government take in Libya is; he heard it is about 90 percent.

MR. WENZEL said it is very high, but the different in Libya is a question of prospectivity and the likelihood of finding large resources. Conoco will be "stepping into assets" it previously had there.

[1:47:49 PM](#)

REPRESENTATIVE OLSON asked if Conoco will be running ads on Libyan television.

[1:48:08 PM](#)

REPRESENTATIVE KAPSNER said she now has a copy of the letter by Representative Gara and Senator French, and she does not see where the letter says that private profits are bad, which is what Mr. Wenzel stated. The letter says "the ads are misleading at a time when it is very important to educate Alaskans fairly about the issues of oil tax reform." The letter says that Conoco implies [in its ads] that it is paying too much, but after-tax profits are staggeringly high. She said the letter does not note that profits are a bad thing. "All of us, especially me, are acutely aware of the contribution that your industry makes to Alaska." She said, "We definitely appreciate that," but she is concerned about how the state will pay the bills in the future. There has been a financial decline in education and corrections, and "we're nervous about how we're going to pay the bill." She said she didn't think any legislator feels that Conoco should not make a profit, but everyone is just trying to judge what is fair.

[1:50:26 PM](#)

MR. WENZEL said when he reads the letter he sees an implied complaint about being profitable in Alaska.

REPRESENTATIVE KAPSNER said the ads are misleading because they imply that Alaska's tax is too high and changing it will cripple the industry. She noted Conoco's \$829 million profit. She said she is not out to scare Conoco away, but the ads are a disservice to the public who don't get a chance to look at your bottom line.

[1:51:52 PM](#)

MR. WENZEL said Conoco does not believe the ads are misleading.

CO-CHAIR SAMUELS said he may be the only one, but the ads didn't bother him, and perhaps it is because he is cynical.

[1:52:20 PM](#)

CO-CHAIR SAMUELS said he appreciates the civility shown to him and the Co-Chair by the industry and the administration.

[1:53:06 PM](#)

PAT FOLEY, Manager, Lands and External Affairs, Pioneer Natural Resources, said Pioneer is a relatively new investor in Alaska. He said when considering changes in taxation the legislature can

shoot low or high. He said the governor's bill shoots a little low and leaves a vibrant industry, but the CS does not. Looking at the proposed tax structure and the value of the exemption, the CS will not create the investment-friendly environment that was the goal of the administration, he said. It fails to take into account that at higher oil prices, production costs are higher. In 2005 there was a 50 percent cost increase. He expects it will go up in 2006. It is a misconception that as oil price rises, the profit margin increases in direct relationship. He said the profit margin decreases because costs increase.

MR. FOLEY said the CS appears to extend the SB 185 credits for ten years, which is helpful but only somewhat modestly. The credits have a provision of taking a 40 percent credit on certain activities, but because only some of the costs are eligible, it translates to an effective credit that is much closer to 30 percent. He said he believes a more efficient and beneficial way to incent the industry would be through a PPT; "simply take the 20 percent number and push it up...and have it apply not to just exploration, but also to development." He said the bill has a proposal that \$10 million of credits can be purchased at the state at face value, which is beneficial to an explorer but not necessarily to a developer. He said Pioneer will spend about \$100 million in investments at Oooguruk in the next two years and then about \$50 million for the drilling phase "for the next couple of years." He said he hopes it is combined with a robust exploration program. He said Pioneer's total investments in Alaska would generate credits far in excess of \$10 million. He said it is helpful to sell them at face value, but "we're left with: to whom do we sell our remaining credits?"

1:58:00 PM

CO-CHAIR SAMUELS asked about the amount of credits for Oooguruk or another development like that. He said he had "concerns with an open-ended...the state has to just [be] on the hook to buy, so "what range of numbers would you want the 100 percent buy-back for?" He said his concern was "opening it up to hundreds and hundreds of millions of dollars."

MR. FOLEY said investments at Oooguruk will be about \$125 million, and combined with an exploration program it is close to \$150 million. He said Pioneer has no production, "so we would be looking at, not just a 20 percent investment credit, but we would also be looking to sell our loss...so 40 percent of \$150 million is \$60 million."

[1:59:18 PM](#)

REPRESENTATIVE SEATON asked if it is a better provision over the sellable credit that was in the original bill and if Mr. Foley would like it to be higher.

MR. FOLEY said yes; it could be a discount floor and the state would buy it at a certain percent. He said it would also be helpful to expand the pool of who Pioneer could sell the credit to, "specifically, if the credit could be taken, not only against PPT tax, but also against income tax, then it would broaden the pool outside of the industry."

[2:00:17 PM](#)

CO-CHAIR SAMUELS said that the entire industry has gotten together on that. "The thinking of not having it with the income tax was that at low prices we're already taking risks from the progressivity, but at the low we are getting less. We didn't want to put the state on the hook also for the income tax money. We wanted to have some steady cash flow at the low end."

REPRESENTATIVE SEATON said the committee was talking earlier about 90 percent. "Is 90 percent a floor that you could live with and that would be helpful?"

[2:01:15 PM](#)

MR. FOLEY said 90 percent would be a helpful number.

CO-CHAIR SAMUELS said it is free money to ExxonMobil Corporation, BP Alaska and Conoco, and he assumes they compete against each other.

MR. FOLEY said if the bill must have a progressive tax rate, and if the trigger is an oil price, Pioneer would encourage that whatever prices are used, that they be inflation adjusted. He said the benchmark should be ANS [Alaska North Slope] West Coast delivered price instead of WTI [West Texas Intermediate].

[2:02:34 PM](#)

CO-CHAIR RAMRAS said he is sensitive to an inflationary component because the cost of exploring will go up, but he questioned whether the price of oil is subject to inflation or driven by speculators and global events. He noted that the

costs incurred in bringing oil to market is inflationary, but perhaps not the cost of oil.

[2:04:02 PM](#)

MR. FOLEY said there may not be a direct link in inflation and the price of oil, but there is a time value in money. It may be considered a discount rate instead of an index. If the legislation is based on a benchmark price, that price should have the same buying power throughout the term of the bill.

CO-CHAIR RAMRAS noted that that issue is addressed in the PPT since it is a tax based on profits, and he asked if it is just the progressive part of the tax that Mr. Foley is criticizing.

[2:05:52 PM](#)

MR. FOLEY said he needs to think about that. He said the progressive nature is that at higher prices the state should enjoy a bigger piece of the pie, "and my point is that make sure those are real price changes and not just through inflation."

[2:06:28 PM](#)

CO-CHAIR RAMRAS asked if Mr. Foley was saying that the PPT part works, but the progressivity piece is not inflation-adjusted.

MR. FOLEY said yes.

[2:06:56 PM](#)

REPRESENTATIVE CRAWFORD said if the legislature is worried about inflation-proofing oil taxes, it should also think the same way about the minimum wage, unemployment insurance, poverty rates and others, "but we don't."

[2:08:05 PM](#)

CO-CHAIR SAMUELS said as long as this legislation is not in a contract, "you would always have the ability to petition the government to come and adjust things like the minimum wage." He said putting a price of oil in this legislation was difficult because in five years it could be arbitrary. Inflation indexing assumes something he doesn't think is true, he said. He said the industry will not be shy about trying to change something legislatively.

2:09:09 PM

MARK HANLEY, Manager, Public Affairs, Anadarko Oil Company, said he used to be in the legislature when it faced a fiscal gap. The original 20/20 [tax rate/credit rate ratio] that the governor wanted was balanced, it improved Anadarko's exploration economics, and the company felt good about the proposal. The CS goes a little in the opposite direction, he said, and his company's costs have gone up so this is not as good as the 20/20. The CS is a little worse for exploration than the original bill, he opined. The 40 percent credits that are going to be extended are a benefit, but not enough to offset other changes in the CS. The exploration incentive credits are only for the first exploration well, but the credits throughout the PPT formula apply to exploration wells, delineation wells and development costs.

2:12:09 PM

CO-CHAIR SAMUELS said the reduction of the \$73 million to \$50 million is not offset enough by the SB 185 extension; "is that the trade off you're talking about?"

MR. HANLEY said yes; there is an assumption that as the price of oil goes higher, oil companies can pay more. He said that doesn't take costs into consideration. He said, "We do discounted rates. You saw a net present value analysis; the whole point of that was to say, 'hey, here's the time value of money. It's worth less in the future than it is today.'" He said he would agree that if today the price of oil goes up to \$100 per barrel, Anadarko's costs won't go up. But if the price of oil goes up to \$60 or \$70 per barrel over a ten-year period, it is likely that Anadarko's costs will go up. He said that the original PPT works itself out, but under the escalator, it is a tax on the gross revenues that does not have a consideration for costs. The bill had an inflation adjustor at \$40 per barrel. If the price of oil goes up to \$100 per barrel for six months or a year, the tax on gas will go up, and the price of gas may still be at \$6 per MCF, and it can have a dampening effect on gas exploration.

2:15:39 PM

REPRESENTATIVE SEATON said he understands separating gas from oil for prospectivity, and he asked about a schedule for prospectivity that Mr. Hanley would like.

[2:16:22 PM](#)

MR. HANLEY said he will work on it.

REPRESENTATIVE SEATON asked about the cost increases, and he said that most industries have been worried about energy costs because that is a huge factor. But the oil industry gets free use of gas and oil, he pointed out.

[2:17:19 PM](#)

MR. HANLEY said Anadarko needs to pay those energy costs by paying contractors who run the drilling rigs. The high costs of energy is driving up steel prices. He said obviously the company gets more revenue, but it does have a cost impact to it.

REPRESENTATIVE SEATON said he was talking about all the gas for compressor stations, gas for drilling rigs, and all the oil used in operations in the field and in the lease area. "I don't even think you pay royalties on those."

[2:18:14 PM](#)

MR. HANLEY said his company does have that fuel available, but other costs go up.

[2:18:45 PM](#)

CO-CHAIR RAMRAS pointed out the irony of oil companies explaining increases in their costs because the price of energy is going up. He said gas and oil move separately, and he is concerned that natural gas has its own volatility. He asked what would be good prospectivity for gas. Natural gas tripled recently and has fallen in the last several days. There is a need to address that separately. Progressivity is now a key component of HB488.

[2:20:39 PM](#)

MR. HANLEY said picking the appropriate number is more the issue than the concept of progressivity.

[2:21:58 PM](#)

CO-CHAIR RAMRAS said, "Capex [capital expenditures] and opex [operational expenditures] have an inflation component but it's addressed in the PPT. So it is really only the progressivity

piece that is subject to some degree to inflationary pressure." But, he said, natural gas has not followed an inflationary curve since Hurricane Katrina. It has followed speculators and world events. How can the progressivity be maintained while addressing inflation on the windfall side? he asked.

[2:22:58 PM](#)

MR. HANLEY said there could be an inflation factor or "you could actually put it below the line that allows you to deduct your expenses." He said he would have to think about it, but "the main point is, just looking at the price side...there can be cost factors that are not being considered as part of that, and that can have a negative impact."

[2:24:06 PM](#)

REPRESENTATIVE SEATON said it is a profit-based tax so all of the costs get subtracted out. It is all taken into account; the tax is based on profit, and increased costs get deducted "before we ever get to applying the tax anyway."

[2:24:50 PM](#)

MR. HANLEY said that is not correct. The 20 percent tax will be on profit, but the incremental taxes will be on gross income.

CO-CHAIR SAMUELS said, "It is deductible off of the PPT. So the \$50 mark could be in the wrong place as your costs increase; you could get to the point where you're not making as much money at \$50—you could inflation-proof the 50 to go up higher. But costs could decrease with technology, in which case the \$50 line could move over."

[2:25:31 PM](#)

MR. HANLEY said at \$60 per barrel under the CS, "my understanding is up to \$50, you have the 20 percent. So you have the \$10 a barrel increase; you have a 0.3 percent escalator, so \$10 time 0.3 gives you a 3 percent additional tax, right?" He continued: "You will take 3 percent times your gross revenue before you deduct anything; you'll get a tax. That will set over here. Then you go through [and] deduct all your expenses and costs and come up with net income, multiply that by 20 percent, [which] will give you a tax. You add the two taxes together and that's your gross tax against which you can apply credits. And that's where the problem with that 3 percent; [it]

does not have a cost factor in it. It's just multiplied times your gross revenue."

[2:26:33 PM](#)

The committee took an at-ease from 2:26 PM to 2:31 PM.

[2:31:52 PM](#)

ANGUS WALKER, Commercial Vice President, BP Alaska, said he stands by previous testimony that he has given. He said since 1999 industry and the Department of Revenue have consistently overestimated production forecasts. This is of great concern because a 100,000-barrel a day drop in production relates to a decline of \$500 million in state revenue. He showed a chart of historic production from the Alaska North Slope and of a precipitous decline in production forecasts. He said he tried to outline the current reality of the North Slope, and with no investment, the fields will decline at 15 percent per year, ending the "business" at about 2015. He said he talked about a future where production would decline about 6 percent per year with an ongoing investment of \$1 to \$1.5 billion, which is the current investment in the North Slope. At that rate the business would be over in 2020/2030. He said a three percent decline would require doubling today's investments, and that would extend the business out to 2050, and it would keep the oil business healthy under a timeframe that would support gas [development]. He said the real question that the legislature should be asking the industry is: what would it take to double investment in the North Slope?

[2:35:58 PM](#)

CO-CHAIR RAMRAS said he is taking some offense from the content of today's testimony. He said he is hearing that "what makes Alaska worthwhile to invest in is not the reasonable profits that are gleaned by the industry as we move through the 20/20 PPT that has to happen at reasonable oil prices--not at stressed oil prices." He said he sat through many meetings on the gas line and discussed the stressed price of gas. And now we have, really, over the last three or four weeks, started talking about the stress price of oil--\$20, \$22.50 was represented to us as the stress price of oil for BP at which it becomes break-even or less than break-even. And I accept that. I am not here to quarrel with that figure, although I respect some of the other members for calling that figure into question. But we certainly determined that \$30 and \$40 are reasonable; that we may see

those again; that \$50—all the economists told us that \$50 certainly represents the high, high side of any planning that an oil company could do. So I'm finding myself, over the last hour and a half...beginning to take some offense at the suggestion that when we start to see high oil prices, that that is what justifies industry being here; it is not the profit that they enjoy at reasonable oil prices, but it's the opportunity to capitalize on the enormous profits the come when oil is in this upper quadrant... [at] record highs." Co-Chair Ramras said his question to Mr. Walker is: "At what point, on a progressive scale, does the industry want to share the windfalls with the State of Alaska in some progressive mechanism. What's your point? We went all the way out to \$50 [per barrel] in our CS. We covered the whole range of economic models that every presenter...made. At what point do you want to share?"

[2:39:16 PM](#)

MR. WALKER said BP is not in favor of a progressive regime. "We do not believe it is the right regime for Alaska. Alaska is a very tough place to do business. We make no money at low prices; we make moderate profits at moderate prices, but when prices are high we make good profits, but we have to make good profits to be in business."

[2:39:41 PM](#)

TOM WILLIAMS, Tax Counsel, BP Alaska, said he has a question of what people think are windfall profits. In March, 1980, BP's predecessor, Sohio, had a long-term West Coast price of \$33 per barrel and they raised their price through December, "so it is not a flash in the pan price; that's \$75 in today's buying power. Where does the windfall start?"

MR. WALKER said he is presenting a reality and is seriously concerned about what is coming out of this committee, and "all we can do is be honest with you."

[2:41:11 PM](#)

REPRESENTATIVE KAPSNER said she has heard that at \$18 dollars a barrel, the industry still invests in Alaska.

MR. WALKER said the industry invests through the low cycle. He said, "We stop making a profit at \$22.50." If the price of oil went to \$20 a barrel, BP would continue to invest in ongoing projects because the prices should go up. Alaska is one of the

most expensive places to produce oil and gas, so the profits have to be made.

[2:42:25 PM](#)

REPRESENTATIVE GATTO asked if BP lost money worldwide at \$22 a barrel.

[2:42:52 PM](#)

MR. WALKER said Alaska is one of the most expensive places, so the break-even point comes at a higher price.

REPRESENTATIVE GATTO asked about the price on average.

MR. WALKER said he doesn't have an answer.

[2:43:32 PM](#)

MR. WALKER said encouraging new exploration is good but those resources will likely be less than the known resources. It is investment in the known resource that offers the greatest chance of stemming the decline of the Alaska North Slope. He suggested growing the pie rather than increasing state take from the declining pie.

MR. WALKER showed a slide in an attempt to show how growing the pie by incentivizing investment is in the best interest of the state over the long term. The capital investment to make that happen is significant, he stated. He showed different rates of decline in oil production on his graph. Calculating state revenue, the graph shows that 3 percent provides significantly higher revenue to the state, regardless of the amount of severance tax; revenue is driven by royalties and other taxes.

MR. WALKER said that a zero severance tax rate would be a better outcome for the state than a high severance tax with less resource development.

[2:47:07 PM](#)

REPRESENTATIVE GATTO said at a 15 percent decline rate, "you invest \$1 billion and you get \$10 billion; is that \$10 billion for the state and \$30 billion to the company?"

MR. WALKER said only the revenue to the state is represented.

REPRESENTATIVE GATTO said if there is \$10 billion to the state, that would only be one quarter of the pie. So during a 6 percent decline there is \$30 billion to the state, "but it took you \$20 billion...invested to increase the state revenue by \$20 billion, which means, to me, that the company...is doing substantially better." He said that is an incredibly larger investment and it looks like the more invested, the poorer the return to the company. He said it is confusing. "Getting \$60 billion more in state revenue requires a \$60 billion investment on your company, and that must mean that you have to look at the \$60 billion investment," and ask what you are getting for it.

[2:49:11 PM](#)

MR. WALKER said he didn't do a good job of explaining the chart. In each case he is taking the business as it exists today with all the historic capital that has been invested. "If we don't invest anything, then that production will flow, provided we continue to make the expenditures and operating costs, etc." He said that in the six percent decline case, BP would have to make an investment of \$1 billion to \$1.5 billion per year in new wells and facilities. The next graph shows the total capital needed by all of the oil industry over a number of decades. From that derives the production and the revenue in all forms of taxation, he said. His point is that what really matters is barrels down the pipeline, and pushing the severance tax too far is the wrong answer.

[2:51:56 PM](#)

REPRESENTATIVE GATTO said the state is much better off at the slow decline, but it will take a significant investment. He asked if it is a better deal [than the other scenarios].

[2:53:39 PM](#)

MR. WALKER said the state is on a trajectory of six percent. Pushing PPT too high will be a bigger loss to the state. He said the real opportunity is to get to a three percent decline and enable gas. There can't be a gas contract without a healthy oil business.

[2:54:35 PM](#)

REPRESENTATIVE GATTO asked if the six percent decline is ideal for BP.

MR. WALKER said the six percent decline is "where we are and where we have been with the existing tax system. We have been very clear in our testimony that the new tax system is a huge additional burden to us, the major producers on the North Slope." He said the state and BP should be looking for a solution to the decline. It could be stimulated by lower taxes.

REPRESENTATIVE GATTO said that is what we are trying to do.

[2:55:55 PM](#)

MR. WALKER suggested lowering taxes to stimulate activity.

CO-CHAIR RAMRAS said the graphs assume \$40 ANS, and he is frustrated. In helping to craft this CS "we were so cautious" to provide a safe harbor for a whole range of prices where the industry does its economic planning. "We are well outside of \$40 ANS." He said he is struggling with the notion that the committee left the governor's PPT intact through that whole suite of prices. The industry is making a mistake to stand its ground on this point and will lose a lot of the goodwill in the body. He said he is struggling with constituents, the press and other members that it "is giving away the farm not to trigger a progressive scale at \$40 or \$45...You had me at \$50, but I keep seeing these references to assuming \$40 ANS...At what point do you want to share the wealth, the windfall?" He said he hears the oil companies saying they do all their planning at \$40 ANS, but unless they get all the profits out there at \$50 or even \$70, it's not worth it to them to operate. "I am struggling with the posture that you are taking because you're losing my goodwill."

[2:58:39 PM](#)

MR. WALKER said he used \$40 as an illustration. The only thing that matters to Alaskans is getting oil down the pipeline, he said, and that is in the best interest of the industry. He is sorry for being a broken record, and his point of view hasn't changed.

[2:59:22 PM](#)

CO-CHAIR RAMRAS said that is not the message the public is giving to him. He said he is trying to steward a course that balances more oil versus more taxes. He said it is more important to him to have oil in the pipe, but there has to be some point where the industry is happy to share. Every time the

industry came in here it talked about the price of oil in that range. He and his Co-Chair came to a consensus to provide a safe harbor for the industry, and it troubles him to have the industry say that \$50 is not good enough; there should be no progressivity.

[3:00:44 PM](#)

MR. WALKER said to remember where the 20/20 was born. BP was very clear when it made a deal with the governor that it was taken right to the edge of what it was willing to share.

[3:01:18 PM](#)

REPRESENTATIVE SEATON said the ELF has been broken. When BP was getting all of those tax breaks, the state didn't see \$2-3 billion in investments. "The broken ELF was giving you all of those tax breaks and you weren't doing those investments. You weren't doing them." He said he has a hard time with Mr. Walker telling him if the state lowers taxes toward the ELF amounts, it will stimulate investment. He said everything the committee has heard from BP and everything BP has demonstrated from its investments shows it contributing to the six percent decline. He noted that BP said it will take its money and take it somewhere else unless it is tied to an investment credit. He said he has a hard time figuring out why BP is saying that at lower taxes it will invest, when that has not been the demonstration. He noted that BP's investment was small when ELF was at its very bottom, "and all the taxes were going in your pocket, you weren't doing the investment to get to a 3 percent decline."

[3:03:10 PM](#)

MR. WALKER said BP has been investing \$700 million per year in capital. He said BP can't say the exact relationship between tax and investment, and that is where he sympathizes with everybody in the capitol building. He said the industry in totality is investing \$1-1.5 billion annually at the current tax structure. The laws of economics say that increasing taxes makes Alaska less competitive. "You will have to struggle even harder." He said a capital credit structure is good and the PPT has merit, but the numbers just need to be right.

[3:04:35 PM](#)

REPRESENTATIVE CRAWFORD said he has heard testimony on total government take, and on the average "Alaska looks pretty good." Once the oil is discounted for quality of crude, transportation, and production costs, the state would be average worldwide at a 65 percent take. Under the original bill, Alaska oil has a 57-59 percent government take, which would mean that the state would be leaving billions on the table over the long term. Oil production has been on a six percent decline with low taxes, so he asked if the state should look at something else. He said explorers say the cost of facilities access and the pipeline tariff are keeping them from exploring on the North Slope. Low taxes haven't seemed to work in the past, he noted.

[3:07:07 PM](#)

MR. WALKER said government take will be 61 percent under the PPT. It is 114 percent at \$20 per barrel and 70 percent at \$30. Alaska government take is very high; compared to the United States and Canada it is the highest by far, he stated.

[3:08:29 PM](#)

REPRESENTATIVE CRAWFORD asked if Mr. Walker is subtracting other royalty owners in the rest of the country. It has to be considered when comparing government take.

MR. WALKER said he will address it later.

REPRESENTATIVE OLSON asked if BP is going to Libya.

MR. WALKER said he doesn't know.

REPRESENTATIVE OLSON said at \$75 to \$80 per barrel, Alaska oil total take is less than 65 percent, and Libya's take is at least 90 percent. Libya is a third world country with better climate, but with a history of political instability and nationalization [of oil industry]. "Everybody is going over there to pay a 90 percent take. How can you make more money at 90 percent than you can at 65 percent?"

MR. WALKER said he doesn't know what is going on in Libya. He said there are some regimes that can afford a high tax rate, like Norway. But Norway has a wonderful resource base and production has been growing in Norway. Norway can afford to have marginal tax rates because people can still make money due to the quality of the resource base.

3:11:15 PM

REPRESENTATIVE OLSON said Mr. Walker is comparing Alaska to other fields in the United States, and no state has the potential that Alaska has, with the exception of the Gulf of Mexico.

MR. WALKER said there is huge potential in the Gulf of Mexico. No one has the cost structure that Alaska has. "Alaska's resources are challenged, and the fiscal structure needs to enable investment. The viscous oil, enhanced recovery of existing fields, distance to market and location all adds to reduce Alaska's competitiveness, he opined.

3:12:18 PM

MR. WALKER said there is a huge known resource in Alaska, but it is technically difficult. Alaska is one of the most expensive places to operate. With the PPT, Alaska would become the area with the highest marginal tax rate in the United States. Higher tax rates at higher prices is a bizarre regime of being regressive at low prices and progressive at high prices. The legislature should be attracting industry, not make it more difficult. He quoted a consultant who said the United Kingdom's government take was "crazy and irresponsible. The gross benefits to the U.K. government go way beyond direct tax revenues and royalties received from the upstream sector of the petroleum industry." He continued reading the quote that said when take was reduced, "the U.K. offshore became the most active offshore province in the world. Reducing the government take in the following years managed to sustain that boon."

MR. WALKER said he couldn't agree more that reducing taxes sustained an economic boon. It had a ripple effect throughout the country, he stated. That is a good role model, he said. He told the committee to lower the tax rate that the governor proposed in order to "take an important step towards creating a healthy oil business, which will be the foundation for gas." He suggested that raising taxes will increase state revenue for only one or two years and at a cost to future production. He repeated his opposition to the proposed CS.

3:18:00 PM

MR. WILLIAMS said the penalties and interest on underpaid taxes are inappropriate because the federal government imposes no penalties if a taxpayer settles up on April 15. He said self-

employed people, like farmers and fishermen, are required to make estimated tax payments, but they can't predict what the total will be for the year, so they are not charged for interest and penalties. It is exactly the same for oil companies, he said. He said BP will have to file taxes at the end of February when it knows its gross value, but it won't know what the year's total of capital or operating cost will be. "We can make an estimate about what those will be, but often what happens is capital costs tend to load up at the end of the year as people try to get things in service this year, so for federal purposes they can take tax depreciation." He asked what happens if somebody is late in delivering something that BP needs. He said, "You can suddenly find yourself there in November having expected to have a 20 percent credit for the capital expenditure that was going to be put in and arrive in December, and now it's not going to happen until January." There will be a penalty and an interest on that optimism, he stated. He said the original discussion recognized that people will do the best they can to estimate what the costs will be. The 90 percent figure is to keep people honest and reasonable, but it wasn't the idea that BP had to be accurate in forecasting the full years worth of costs.

[3:22:01 PM](#)

CO-CHAIR RAMRAS said he couldn't agree with him more because he is a small business person subject to quarterly taxes. He said there are many quarters where he overpaid due to not being able to forecast his obligations. The provision arises from how much the oil companies, for the last 20 years, "have manipulated the accounting and how much ill-will they have created in requiring the state to pursue litigation in order to get its fair share." He said he couldn't agree with Mr. Williams more, but there is no goodwill from the public, and "these are just the seeds of summers past that have come back to roost."

[3:23:32 PM](#)

MR. WILLIAMS said despite the large tax settlements, the large royalty settlements, and the huge litigation, if one takes out the interest, the oil companies paid over 95 percent of the tax and royalty liability they owed at the time it was due. Even though the settlements were billions of dollars, they were less than 5 percent of the principal. He said he understands there is a public perception that the legislators have to deal with, but "the public are mistaken."

[3:24:13 PM](#)

CO-CHAIR SAMUELS said BP, ConocoPhillips Alaska, Inc., and ExxonMobil Corporation know exactly how much they are going to pay. "You are the king of one of the departments and you know exactly how much you're going to pay." He said that it is the much smaller players that tend to have the problems. He asked why this will be a problem for BP, or if it is just a philosophical opposition.

[3:25:23 PM](#)

MR. WILLIAMS said it is flattering to be told it is easy for BP. He said two people manage the accounting for the number of barrels coming out of the ground and whether they are taxable or not. There are others who make sure the data are entered properly. "We have a system that we have been able to perfect over the years." Taxes are filed electronically with computers summing the numbers. He said the change is the problem.

[3:26:58 PM](#)

MR. WALKER summarized and repeated his points. He said the proposed amendments to HB488 will not maximize the benefits to Alaskans for oil or gas. He repeated the U.K. example. He urged the committee to lower the tax rate on oil and gas.

[3:28:45 PM](#)

REPRESENTATIVE SEATON asked if BP wants the state to look at the U.K. with regard to high taxes on legacy fields and low taxes on exploratory fields.

[3:29:06 PM](#)

MR. WALKER said the U.K. was a marvelous example of reducing taxes across the board, which stimulated investment.

REPRESENTATIVE SEATON asked about the problem of late deliveries and the capital costs. "Do you not incur your capital costs...until the barge hits Prudhoe Bay?"

[3:29:55 PM](#)

MR. WILLIAMS said BP pays bills when they come in, but "if you start off in January and you're expecting something to be finished by the end of the year, and let's say it's being built

in the Gulf of Mexico and there's a strike or a hurricane...and delays it, we're not going be paying." He suggested the state pay the oil companies interest on overpayments. Severance tax has worked in the past, he said.

[3:31:16 PM](#)

REPRESENTATIVE SEATON asked if capitalization costs will be written against January tax from the year before. He said it seems that there is no problem "unless you're trying to forward capitalize and forward credit...and take them off against your first taxes."

[3:31:42 PM](#)

MR. WILLIAMS said BP's billings are costs as they are being incurred. He said BP can keep track of the checks, but the problem is that in March, BP only knows how many checks it has written through the end of February. "If we don't write the checks we expect to write [from May to July], we will find that we over-deducted or over-credited ourselves in those first months of production when we filed our return. And it is too late then because if we didn't hit the 90 percent mark, each of those months will have a penalty and interest."

[3:32:35 PM](#)

JOHN ZAGER, General Manager, Alaska Chevron, said he told the committee three things in previous testimony and none of that counsel was retained in the proposed CS. His three previous points were: Cook Inlet was different from the North Slope and should be considered for special treatment under the PPT; the committee should not "pull all the levers in the bill in the same direction"; and, keep things simple to avoid the costs of tracking the tax.

MR. ZAGER said he would like to applaud "that we've held the line on the 20 percent base tax rate." The progressive tax rate in the CS is complex, and he asked for a much larger step function so that "for every \$5 increment, you see a substantial change." He said the ANS would be a better marker. He questioned why profits for gas would be tied to an oil marker. He noted that the price step at \$50 has no inflation component. The \$40 indexing price is inflated, he said, so it would be fair to use that mechanism on the \$50 starting price on the progressivity. He said taking windfall profits away lowers the expected value to investors. He compared the oil industry to

fishing, and suggested that a person wouldn't buy a fishing boat if there was a similar progressivity. He said people think of the windfalls as free money, but it is part of the overall distribution of expected results.

MR. ZAGER said the CS has a substantial hit to Chevron's annual deduction. It's an increase in taxes, he said, and it penalizes the companies that have been faithfully investing in Alaska, "and now we're being taxed on those profits that is benefiting both the state and the companies." Regarding the exploration enhancement, he said, "the choice between [SB]185 and the 20 percent rate is not a big value addition and that the credits on the back side of this, for any investment decision, is very important." He said that the inclusion of the costs of abandonment would promote timely abandonment of operations. He said the state has benefited from those assets for many years, so abandonment is a legitimate cost of production.

MR. ZAGER said the effective date is an arbitrary move to take more money from the investors. He spoke of the reduction in the \$73 million allowance, which is more important to other companies but is substantial. The tax credit repurchase program helps a few smaller companies, and doesn't do anything for Chevron. He shares the view that 5 percent is punitive, especially when it is layered on top of a 11 percent base rate. He described it as an accounting issue without intended malice.

[3:41:39 PM](#)

CO-CHAIR SAMUELS asked if Chevron anticipates selling tax credits.

MR. ZAGER said Chevron won't need to sell credits. "Our biggest disappointment of all is that the Cook Inlet was not at all recognized as being distinct and separate from the North Slope in terms of its profitability and its unique and valued position to the State of Alaska." He said additional investments should be encouraged in Cook Inlet to help local economies and to supply gas to the area. He said the four-year capital program in Cook Inlet will be put in serious jeopardy under HB 488. He said without capital investment in the Parker River field, the anchor field, it could be gone in four years, causing the Cook Inlet oil industry to shrivel and die in the not-to-distant future. The CS is lopsided in favor of the state, he concluded.

[3:44:59 PM](#)

CO-CHAIR SAMUELS said it is the start of a long process.

[3:45:30 PM](#)

TIM ENGLAND, Senior Manager, Global New Ventures, Talisman Energy Inc., said his group searches for exploration opportunities internationally. He led the entry into Alaska for Talisman a few years ago, and the company's current operation in Alaska is being "operated through our FEX-LP subsidiary." The enterprise value of Talisman is \$23 billion, and it has capital investments of \$3 billion to \$4 billion per year. The company operates in North America, the North Sea, Southeast Asia and other places. He said it has invested over \$30 million in land and over \$100 million in drilling and seismic acquisition in Alaska. The cost of drilling in Alaska is \$30 million and is probably only \$6 million in Libya, he said. A commercial discovery in Alaska would take 5 to 10 years to put on production, and that is a long time from initial investment to recouping the investment; the front end is risky. He said the decision to enter Alaska was dependent on an unchanging fiscal regime. He said the company has to accept the risk of volatility and changing costs, and fiscal stability is really important, he said. The proposed changes will have impacts on Talisman. Exploration will decline even with the proposed incentives under the CS. Investment dollars for Alaska will not be able to compete with other countries, he noted. Sadly, the bonus bids will be reduced, he stated.

[3:49:07 PM](#)

CO-CHAIR RAMRAS asked what oil prices Talisman used for the economic models for making the decision to come to Alaska.

[3:49:28 PM](#)

JON HANDFORTH, Manager, International and Frontier Operations, Talisman Energy, said the company was using \$20 to \$30 per barrel.

MR. ENGLAND said that Talisman invested in Alaska when the WTI was about \$30 a barrel, "but, you know, our exploration costs up in Alaska, we underestimated by about half compared to where they are today."

[3:50:02 PM](#)

MR. ENGLAND said increasing the take after the investment has been made does not bode well for promoting a stable environment. Talisman is global and has plans to invest heavily in Alaska in the near term. He said the bill is not catching the company by surprise, but it is going in the wrong direction. He said if taxes are increased, potential resources would have to be larger to attract investment dollars. The chance of finding larger resources is smaller than finding the small resources. If Alaska's taxes are increased, more oil will be left in the ground, he concluded.

[3:51:44 PM](#)

CO-CHAIR RAMRAS asked what price Talisman uses for its modeling now.

MR. HANDFORTH said anywhere from \$20 to today's price.

MR. ENGLAND said there are cycles, but he is anticipating that the price is going to stay positive, but the worry is that costs are rising at an equal rate as oil prices, especially in remote areas. He said he is looking for the investment cash to find some resources to develop in Alaska.

[3:53:22 PM](#)

RICHARD OWEN, Production Manager, ExxonMobil Corporation Alaska, and Vice President of ExxonMobil Alaska Production, said he is concerned about the CS, and most points have been covered well. He said HB 488 represented a dramatic increase in the tax rate, and it could prevent some challenged resources from being developed. Now the committee is considering a higher tax rate. He said too high of a tax rate discourages investment. He said companies only take the risk of long-term capital investments when there is an opportunity for an upside potential of increased production, larger reserves or higher prices. Capping the benefits of the upside reduces the attractiveness of investments. The high tax base rate will result in a recalibration of decisions, and it will result in a negative impact on the state's economy.

[3:56:55 PM](#)

CO-CHAIR RAMRAS said the state will participate in the reward side, but through the PPT the state is at risk of oil reverting back to lower prices. "When you suggest the model is not built on sharing at the higher end, you are not acknowledging that

through PPT, the State of Alaska is offering to reduce risk for the industry at the lower prices by sacrificing the status quo through the current Elf system. "Why isn't that part of your testimony?"

MR. OWEN said increasing the tax to 20 percent was the balance for the low side. The CS goes beyond the original proposal.

[3:58:55 PM](#)

REPRESENTATIVE SEATON noted that Mr. Owen said the CS caps the upside potential, but it is not capping anything; at the price of \$150 per barrel, the state splits the profits with the industry. "You're not calling that capping, are you?"

MR. OWEN said to a large extent it is reducing the upside potential, not capping it. The transition provision is necessary to mitigate the adverse impact on recent investments, he said. The benefits of a typical oil and gas investment take many years to realize, and the governor's bill provided a reasonable transition provision. The CS does not sufficiently address the significant increase in the tax burden. He said he is prepared to move forward with the governor's proposal since it sought to provide the balance of revenues to the state and the producers across a range of prices and provided incentives for exploration and development risks. Most importantly for Exxon, oil fiscal contract terms will provide the predictability to go forward with the gas project to the next phase. It is important that the quality of the resources and the risk of producers be factored in to the tax system, he stated. He said the industry needs predictability and durability, which gets lost at too high a cost.

[HB 488 was held over]

[4:01:58 PM](#)

ADJOURNMENT

There being no further business before the committee, the House Resources Standing Committee meeting was adjourned at [4:02 PM](#).