

ALASKA STATE LEGISLATURE
SENATE RESOURCES STANDING COMMITTEE

October 24, 2007

10:05 a.m.

MEMBERS PRESENT

Senator Charlie Huggins, Chair
Senator Bert Stedman, Vice Chair
Senator Lyda Green
Senator Gary Stevens
Senator Lesil McGuire
Senator Bill Wielechowski
Senator Thomas Wagoner

MEMBERS ABSENT

All members present

OTHER LEGISLATORS PRESENT

Senator Bettye Davis
Senator Joe Thomas
Senator Hollis French

COMMITTEE CALENDAR

SENATE BILL NO. 2001

"An Act relating to the production tax on oil and gas and to conservation surcharges on oil; relating to the issuance of advisory bulletins and the disclosure of certain information relating to the production tax and the sharing between agencies of certain information relating to the production tax and to oil and gas or gas only leases; amending the State Personnel Act to place in the exempt service certain state oil and gas auditors and their immediate supervisors; establishing an oil and gas tax credit fund and authorizing payment from that fund; providing for retroactive application of certain statutory and regulatory provisions relating to the production tax on oil and gas and conservation surcharges on oil; making conforming amendments; and providing for an effective date."

HEARD AND HELD

PREVIOUS COMMITTEE ACTION

BILL: SB2001

SHORT TITLE: OIL & GAS TAX AMENDMENTS
SPONSOR(s): RULES BY REQUEST OF THE GOVERNOR

10/18/07	(S)	READ THE FIRST TIME - REFERRALS
10/18/07	(S)	RES, JUD, FIN
10/19/07	(S)	RES AT 9:00 AM BUTROVICH 205
10/19/07	(S)	Heard & Held
10/19/07	(S)	MINUTE(RES)
10/20/07	(S)	RES AT 8:00 AM BUTROVICH 205
10/20/07	(S)	Heard & Held
10/20/07	(S)	MINUTE(RES)
10/21/07	(S)	RES AT 1:00 PM HOUSE FINANCE 519
10/21/07	(S)	Heard & Held
10/21/07	(S)	MINUTE(RES)
10/22/07	(S)	RES AT 11:30 AM BUTROVICH 205
10/22/07	(S)	Heard & Held
10/22/07	(S)	MINUTE(RES)
10/23/07	(S)	RES AT 9:00 AM BUTROVICH 205
10/23/07	(S)	Heard & Held
10/23/07	(S)	MINUTE(RES)
10/24/07	(S)	RES AT 10:00 AM BUTROVICH 205

WITNESS REGISTER

CLAIRE FITZPATRICK, Senior Commercial Vice President
BP Exploration (Alaska)
Anchorage AK

POSITION STATEMENT: Testified on SB 2001.

MIKE UTSLER, Senior Vice President for Greater Prudhoe Bay
BP Exploration (Alaska)
Anchorage AK

POSITION STATEMENT: Testified on SB 2001.

KEVIN MITCHELL, Vice President of Finance and Administration
ConocoPhillips Alaska
Anchorage AK

POSITION STATEMENT: Testified on SB 2001.

JIM TAYLOR, Vice President of Commercial Assets
ConocoPhillips Alaska
Anchorage AK

POSITION STATEMENT: Testified on SB 2001.

BO DARRAH, President
Brooks Range Petroleum Company
Anchorage AK

POSITION STATEMENT: Opposed SB 2001.

MARK SHARP
Fairbanks AK

POSITION STATEMENT: Supported SB 2001.

JERRY WALKER
Fairbanks AK

POSITION STATEMENT: Opposed SB 2001.

RICH SIEFERT
Fairbanks AK

POSITION STATEMENT: Supported SB 2001.

TOM LAKOSH
Anchorage AK

POSITION STATEMENT: Opposed SB 2001.

MERRICK PEIRCE
Fairbanks AK

POSITION STATEMENT: Opposed SB 2001.

TOM MALONEY
Anchorage AK

POSITION STATEMENT: Supported SB 2001.

PAUL KENDALL
Representing himself

POSITION STATEMENT: Testified on SB 2001.

TONY TENGS
Juneau AK

POSITION STATEMENT: Supported SB 2001.

ACTION NARRATIVE

CHAIR CHARLIE HUGGINS called the Senate Resources Standing Committee meeting to order at [10:05:33 AM](#). Present at the call to order were Senators Green, Stevens, Wagoner, Wielechowski, and Chair Huggins.

SB2001-OIL & GAS TAX AMENDMENTS

[10:06:25 AM](#)

CHAIR HUGGINS announced SB 2001 to be up for consideration.

CLAIRE FITZPATRICK, Commercial Senior Vice President for BP in Alaska, introduced Mike Utsler, Senior Vice President for BP in Prudhoe Bay.

She said that the debate is about Alaska's economic future; production is declining and the state and BP have a common objective in trying to minimize that. BP wants to focus the conversation on Alaska's resources and associated costs and geography. BP supports the net tax basis although the rate is too high; the principle behind the tax was to encourage investment and get more barrels into the pipeline. BP makes investments for the short, medium and long terms; it won't say no to investment because of an increase in taxes or walk out on the business. Ultimately it is a decision for the state to make about tax policy, and whether it is increasing or decreasing the desired effect; tax policy changes the scale and pace of an activity.

[10:10:06 AM](#)

SENATOR STEVENS asked for clarification of Ms. Fitzpatrick's position within BP.

MS. FITZPATRICK replied that she looks after financial reporting, planning, taxes, supply chains, and other financial areas; her position is similar to that of a CFO.

[10:11:44 AM](#)

She said that BP's key message is that production is the major factor in determining state revenue for the future years, and the goal is to stem the decline. Changes in production impact royalties, which can be more important than taxes. A fiscal policy dependent on price is not the best approach. Investment in development is key to stemming the decline. BP is concerned about fiscal stability because three tax changes in three years doesn't seem stable.

[10:13:04 AM](#)

SENATOR WAGONER asked Ms. Fitzpatrick to list the changes.

MS. FITZPATRICK said the first was the Economic Limit Factor (ELF) aggregation, the objective of which was to increase revenue to the state. The PPT change came second and the proposed PPT change would be the third.

SENATOR WAGONER responded that the ELF aggregation was not a change in tax structure, but a change in administrative policy.

MS. FITZPATRICK replied that that was his perspective.

SENATOR WIELECHOWSKI asked when the last change was before those being discussed.

[10:15:03 AM](#)

MS. FITZPATRICK replied there had been a period of stability previous to that and offered to give more detail later.

SENATOR WIELECHOWSKI said he heard 1989 mentioned as the last year in which a change was made and only one change since 1989 seemed pretty stable to him.

MS. FITZPATRICK said she bases current investment decisions on current news.

[10:16:14 AM](#)

SENATOR WIELECHOWSKI asked if BP has a defined pool of money it uses to invest around the world or if the amounts invested are flexible.

MS. FITZPATRICK replied BP doesn't have an infinite pot of money. Its financial group decides what investment framework is appropriate for the entire company. It considers debt rates because the company is severely impacted by prices. The investment community expects to see prudence. BP made a strategic decision to invest in Libya, but that didn't take money away from other locations. Alaska gets money by presenting the London office with a robust business plan; a good plan will mean more money over time.

[10:18:18 AM](#)

SENATOR WIELECHOWSKI said he was trying to figure out if Alaska is in competition with other countries or if any profitable project would be developed. His concern was that a higher profit margin elsewhere would mean respectively less-profitable projects wouldn't be developed.

MS. FITZPATRICK responded that she would attempt to answer that question later in the meeting.

CHAIRMAN HUGGINS remarked that Senators McGuire, Stedman, Hoffman, and Thomas were present.

[10:20:40 AM](#)

MS. FITZPATRICK said that there are resources that haven't been discovered in Alaska, but the bulk of opportunity within Alaska

is within its known resources. BP is working on how to actually extract them economically. The debate should be around creating the environment that basically allows them to be accessed.

[10:21:19 AM](#)

She then referenced a slide showing how production has declined in recent years, as well as the related investment numbers; BP invested in 100 wells on the North Slope in 2007 and hopes to invest in 100 more in the next year.

SENATOR WAGONER asked if those wells are exploratory in nature.

MS. FITZPATRICK replied that BP does not use true exploratory wells.

SENATOR WAGONER asked how many wells deal with heavy and viscous oil.

MS. FITZPATRICK replied BP isn't currently producing the thickest heavy oil; it has only one such pilot well.

[10:24:15 AM](#)

MIKE UTSLER, Senior Vice President for BP Exploration in Prudhoe Bay, said a percentage of BP's program is geared towards developing viscous oil in Prudhoe Bay.

SENATOR STEVENS asked how the unknown is defined.

MS. FITZPATRICK replied that she examines production projections; 70 percent of production in coming years will come from the Prudhoe and Kuparuk fields, which will include the viscous and the heavy oils. The exploratory opportunities are unknown by nature; the response to that question will thus change over time.

SENATOR STEVENS asked if she was including the land becoming exposed through global warming in her estimates.

MS. FITZPATRICK replied that she does not take her calculations to extremes.

[10:28:24 AM](#)

SENATOR WIELECHOWSKI asked if her figures were in 2006 dollars or actual dollars per year.

MS. FITZPATRICK replied that the history of spending was in actual dollars spent.

SENATOR WIELECHOWSKI asked if the rate of decline will increase or decrease with the Alaska's Clear and Equitable Share plan (ACES). He added that there were many years of low production taxes, and when the tax increased so did the production.

MS. FITZPATRICK said she couldn't predict what the decline would be if the current bill was passed. The economic outcome is one of the factors she takes into consideration, and overall it's a hugely complicated balancing act, and all decisions aren't made at the same price. Increasing taxes will decrease economics and the decline curve will probably become steeper, she opined, but then added that technology has changed so BP can do more and now prices have gone up.

[10:31:43 AM](#)

SENATOR WAGONER said he doesn't want to have to recoup revenue in hindsight and asked how the state would keep that situation from happening again.

MS. FITZPATRICK said the current PPT was designed to stimulate investment and her personal view is that BP's investment has increased. The oil industry doesn't revolve on annual cycles; so the effect of investments doesn't show immediately.

[10:33:19 AM](#)

SENATOR WAGONER asked what percentage of the investment increase is the result of inflation costs.

MS. FITZPATRICK replied that she would address that issue later. She said that 800 wells have been drilled in Prudhoe Bay in the last 10 years. Drilling a well now is different than 10 years ago; to get the same production rate a company must drill more wells in the future.

SENATOR STEVENS asked if BP alone drilled 800 wells.

MS. FITZPATRICK replied that was the total number drilled by all investors in the bay.

[10:35:41 AM](#)

CHAIR HUGGINS asked for an explanation of what water in the wells means.

MS. FITZPATRICK replied that she would cover that issue later in her presentation if that was alright. She then showed another slide regarding how declining production decreases state

revenues. She stated that 6 percent is the current decline; the DOR is forecasting 1 percent over 10 years and 3 percent over 20 years.

SENATOR WIELECHOWSKI asked for how she got the \$25 billion and \$70 billion figures.

MS. FITZPATRICK explained how those numbers were estimates based on what the administration had presented.

[10:38:18 AM](#)

SENATOR WIELECHOWSKI asked how accurate the numbers were.

MS. FITZPATRICK replied that she hasn't had the opportunity to fully scrutinize them.

SENATOR WIELECHOWSKI asked if she could create a fiscal model for the legislature.

MS. FITZPATRICK said she would be happy to do so; the model is not complicated.

SENATOR WIELECHOWSKI said perhaps the Department of Revenue (DOR) should do so.

MS. FITZPATRICK said she is trying to work with the DOR.

[10:40:42 AM](#)

MR. UTSLER explained that Prudhoe Bay is still the largest producing field in North America. BP believes Prudhoe Bay has another 50 years of possible production and it is at the heart of that future. He then described the area.

SENATOR WIELECHOWSKI asked him to detail the number of wells and their success rates.

MR. UTSLER replied that the 2,500 wells include dry holes; currently 1,200 of them are active.

SENATOR WIELECHOWSKI asked if 50 percent is a high success rate.

MR. UTSLER replied no; an 80 percent success rate is what BP expects. Historically, that is the range in Prudhoe Bay.

SENATOR WIELECHOWSKI asked how that compares to success rates in other parts of the world.

MR. UTSLER replied that 80 percent is consistent around the world.

[10:47:30 AM](#)

SENATOR MCGUIRE asked if he has worked in tar sands.

MR. UTSLER replied no, but he has studied them.

SENATOR MCGUIRE said she and Senator Wagoner were in such an area, and the technology just wasn't there. The Calgary heavy oil industry is now taking off. She asked if that area could be compared to Prudhoe Bay.

MR. UTSLER replied that BP believes in an exciting heavy oil future for Alaska, but there are technical and fiscal challenges. He said he would talk about the ability to leverage the Alberta technologies, and emphasized that a robust supply of light oil is needed to develop heavy oil; the latter can't be developed independently.

[10:51:03 AM](#)

SENATOR STEVENS said he wanted to confirm the speculation that moving west from Prudhoe Bay would lead to finding more gas and less oil.

MR. UTSLER replied that BP believes that the development of the hydrocarbon basin of the North Slope basin suggests that in moving westward, the probability of finding oil with associated gas is greater. Because of the fundamental nature of the depositional environment, BP would expect a more gas-rich terrain, probably including associated liquids.

[10:53:00 AM](#)

SENATOR WAGONER noted that when he was at an oil and gas symposium in Anchorage, BP made a presentation on viscous and heavy oil, which would be useful to the committee.

MR. UTSLER replied that he would be sharing some of that information with them and a group was being put together to address the issue of heavy oil.

[10:54:38 AM](#)

He then talked about a slide showing the cumulative recovery since 1977 with changes in technology noted along the way. Originally Prudhoe Bay was expected to be a 25-year oil field, he said, and currently it may produce for a total of 80 years. Such a field requires tremendous investments and technological

developments. Over time, \$19 billion in capital has been spent to develop the greater bay, not including operating costs.

SENATOR WAGONER asked if that number included all partners' investments.

MR. UTSLER replied that it did.

SENATOR WIELECHOWSKI asked what the total profit has been over the Prudhoe Bay's development period.

MR. UTSLER replied that he didn't have an answer; the field has been profitable in some years, but not others. Overall it is profitable and continues to justify increasing investment.

[11:01:59 AM](#)

He then referenced water production in the drilling process, and explained that water and gas must be separated and re-injected to maintain pressure. Even though oil production is declining, the amount of fluids is actually increasing; but, much of it has no economic value and disposal is costly. However, it allows BP to continue to produce oil for a longer period of time.

He said that Prudhoe Bay has the largest gas plant complex in the world and managing it has many challenges.

[11:04:07 AM](#)

SENATOR WIELECHOWSKI asked how many barrels of oil have been produced from Prudhoe Bay.

MR. UTSLER replied that 11.5 billion barrels have been produced.

SENATOR WIELECHOWSKI asked if the cost was \$1.55 per barrel.

MR. UTSLER replied that would be the capital costs; operating costs would add to that. He said he would return to that topic later in the presentation.

[11:05:32 AM](#)

He referenced another slide to show the well bores that have been drilled, and how the field is in an anticline. He then explained the geography of the reservoirs, and how the oil is recovered from them.

[11:07:30 AM](#)

SENATOR WAGONER asked at what pressure reduction the gas cap loses efficacy.

MR. UTSLER replied that the issue is complex; overall, when there is no more gas in the oil, the oil becomes harder to lift. That situation would require a new sort of mechanism for removing the oil from the ground.

SENATOR STEVENS asked if the existence of a gas line would inhibit oil extraction.

MR. UTSLER replied that BP is working with the Alaska Oil and Gas Commission (AOGC) to determine the optimal level of gas off-take; regardless, there will be an impact to production decline of oil reservoirs. That can be offset somewhat by water, but it is only partially effective. The oil industry and the state are working together to figure out that issue.

CHAIR HUGGINS commented that the answer is always dynamic.

MR UTSLER agreed.

CHAIR HUGGINS asked if CO2 could be injected as a substitute.

[11:11:39 AM](#)

MR. UTSLER replied that CO2 flooding could be used to enhance oil recovery from some reservoirs. The disadvantage is that there will be an additional cost to remove the CO2.

[11:12:36 AM](#)

He explained that only 30 wells re-inject gas back into the gas cap; part of the reservoir is produced with gravity drainage. He then explained the mechanisms of oil extraction and how water flooding helps that.

[11:14:04 AM](#)

SENATOR WIELECHOWSKI asked how Mr. Utsler defined a successful return rate.

MR. UTSLER replied that success means finding projected hydrocarbons and bringing them to the surface; technical success doesn't necessarily mean economic success. BP looks at the well modeling and the costs to drill and develop versus the volume the well will recover; that results in an economic life scenario.

SENATOR WIELECHOWSKI asked for an average barrel number.

MS. FITZPATRICK responded that sometimes assessments are done on a single-well basis, but often assessments have to be done on a program basis to keep the calculations from becoming too unwieldy.

[11:16:29 AM](#)

MR. UTSLER explained that BP has drilled 70 wells in Prudhoe Bay in 2007 on the basis of a program expectation.

[11:17:04 AM](#)

CHAIRMAN HUGGINS called an at-ease due to technical difficulties.

[11:26:18 AM](#)

CHAIR HUGGINS called the meeting back to order.

MR. UTSLER said even a field with 30 years of history presents challenges in moving forward.

[11:28:13 AM](#)

He then referenced a slide regarding water injection projects and pressure history. Pressure began to flatten over a recent period and now BP is looking at different, more specific ways of injection. The longer the pressure profile can remain flattened the better the recovery. BP has had to initiate seawater injection, putting 900,000 barrels of filtered, cleaned and chemically treated seawater into the reservoirs. Seawater injection was started in 1985. As the field has evolved, water produced from drilling wasn't enough and BP brought back seawater injection.

[11:32:29 AM](#)

He said that BP and the state are dealing with a common enemy, in terms of declining production. There is a need to continue to find ways of recovering oil to keep the industry going; fields need continued investment. Just a 1 percent improvement means 250 million barrels of oil over the next 50 years.

[11:34:22 AM](#)

CHAIR HUGGINS commented that BP is now handling as much water as oil and that salt water is now being used. He added that the that technology has extended the life of the field significantly and the challenge is that they are much more significant than people realize.

SENATOR WAGONER asked for the dollar amount that BP budgets per well in the field.

MR. UTSLER replied that BP uses a range of different types of wells, and said he would explain those different wells and their cost structures later in the presentation.

SENATOR STEVENS asked if BP had expected a recovery rate of 45 percent but is currently operating at 57 percent.

MR. UTSLER agreed. The original estimates pointed to a 45 percent rate.

SENATOR STEVENS asked if 1 percent equal 250 million barrels.

MR. UTSLER replied yes.

SENATOR STEVENS asked what important discoveries they came from.

MR. UTSLER replied for example that the Liberty field BP is proposing to develop is a 100-million barrel resource. That was discovered years ago and it's going to take five to seven years to develop. It would get 30,000 to 40,000 barrels of production for the 100 million barrels.

[11:39:50 AM](#)

He then referenced another slide and discussed how BP is working for the future; it is trying to develop a mechanism that allows water to move into restricted areas, and is looking at injecting polymers that solidify with rising temperature and swell to form a plug for the water. It is also experimenting with different techniques in three particular wells, and might recover 1.8 million barrels more.

He then explained another mechanism that involves injecting miscible gas to wells, which picks up molecules of oil as it moves through the water.

[11:47:07 AM](#)

SENATOR GREEN asked how they know for sure that the water is going to the desired pipe.

MR. UTSLER replied that in a miscible sense on the diagram, she would see a fine surface of oil [irreducible oils] left as water is moved through. As the gas comes through, as opposed to water, it is attracted to the surface of oil. It actually literally strips off a few more drops. That mechanism is costly and inefficient in the sense that it doesn't bring large barrels

with it, but it brings more. So, one can take irreducible oil saturations of 19 - 20 percent down to 16 or 17 percent.

SENATOR GREEN asked if BP developed the polymer procedure.

MR. UTSLER replied that it was developed by the industry and several different companies were testing it.

SENATOR STEVENS asked if the companies could recover both the polymer and the miscible gas.

MR. UTSLER replied that the company doesn't recover the polymer; it wants it to stay in the ground. In theory the miscible gas is stripped during use and it has to be re-enriched before re-injection into the ground. BP constantly has to use existing product to be able to return the miscible gas to the reservoir.

[11:51:40 AM](#)

He emphasized that there is a continuing challenge against the backdrop of a continually declining reservoir; this challenge is how to encourage the type of investment it will take to get the production.

[11:52:46 AM](#)

MR. UTSLER then referenced a slide showing underlying decline and how that will continue if new investments are not made. Contributions from new wells have greatly increased production, he said. The oil production would be half of what it is today if BP had stopped drilling in 2003. Keeping the decline in check is very costly.

SENATOR WAGONER asked if oil would stop flowing in six years if there was no technological advancement, and commented that that seemed unlikely to him.

MR. UTSLER replied that the field would not disappear within that period of time, but maintaining a set level of production begs the question of when that production would become uneconomic.

[11:57:52 AM](#)

SENATOR WIELECHOWSKI asked for clarification on the investment chart before the committee.

MR. UTSLER replied in clarifying BP's investment figures. He explained that each year the problem of declining production worsens.

12:00:20 PM

CHAIR HUGGINS asked him to explain an element of the graph.

MR. UTSLER said that the 400 wells drilled by 2007 have contributed 50 percent of the total production stream.

CHAIR HUGGINS stated that Alaskans need to understand that new production within the legacy fields needs to continue and investment is needed.

MR. UTSLER agreed and added that activity in the legacy fields needs to be not only maintained, but accelerated. Their capital spending in greater Prudhoe Bay over the past four years has increased from \$400 million per year to next year's proposed \$1 billion. They are spending more money to mitigate that decline.

CHAIR HUGGINS said that the consequences of misunderstanding the importance of the legacy fields could be dramatic.

SENATOR WIELECHOWSKI asked if the numbers on the chart were in real dollars or discounted.

MR. UTSLER answered that the numbers were meant to be equally weighted. It is meant to demonstrate \$250 million spent in 2002 versus \$250 million spent in 2007 has resulted in the decline.

SENATOR WIELECHOWSKI asked how much the dollar value declined between 2002 and 2007.

MS. FITZPATRICK said that she would be happy to get back to him with that number.

12:05:22 PM

SENATOR MCGUIRE asked for an explanation of a dip in exploration in July 2006.

MR. UTSLER explained that the dip was a result of a partial shutdown of Prudhoe Bay due to an oil leak.

12:06:20 PM

SENATOR STEDMAN asked if it isn't normal for the major producers to move out and let smaller companies enter the field in the case of oil production decline.

MR. UTSLER replied that the question was a complex one; normally, a smaller operator couldn't afford to pay to manage

the infrastructure on a field like Prudhoe Bay. It will likely remain in the hands of the larger companies, and smaller independents will play off that infrastructure.

CHAIR HUGGINS announced a recess at [12:10:00 PM](#) and called the meeting back to order at [1:15:09 PM](#).

MR. UTSLER recapped his technical review of the legacy fields and the challenges of finding the resource and carrying it into the future.

[1:16:09 PM](#)

He referenced a slide regarding seismic imaging and directional drilling enabling development, and explained how BP has developed a way to drill vertically and then in another direction. This method has allowed BP to unlock smaller and smaller resources. He explained that up to five lateral bores can be drilled using one vertical well.

SENATOR STEVENS asked if BP could laterally drill from existing wells.

MR. UTSLER replied that it could, by using coil drilling. BP could drill out about 8,000 feet today and drill within three feet of a target. He then talked about the use of injection wells and the high costs of those, and how they are most effective in producing the viscous oil in the western region of Prudhoe Bay.

[1:22:18 PM](#)

He explained that viscous oil is lighter than heavy oil, which is the consistency of peanut butter. Viscous oil can be pushed with water, but heavy oil cannot. The biggest challenge in developing viscous oil is the needed technology.

[1:24:44 PM](#)

CHAIR HUGGINS asked about the cost differential in terms of processing different types of oil.

MR. UTSLER replied that viscous oil means another \$15 million in facilities costs.

CHAIR HUGGINS commented that the entire business of getting viscous oil to market is complicated.

MR. UTSLER gave an example of how viscous oil wells are more expensive to drill and that it couldn't be done 10 years ago. If

you were to drill five vertical wells to get to five zones, each well is on an average of \$5 million to \$6 million - or about \$25 million to \$30 million. Using the new technology, they could drill one well bore for \$13 million to \$15 million. Offsetting that, though, they would have to drill three additional injector wells at a cost of about \$5 million each. The facilities to handle the viscous oil including pipe, separation and heat necessary to handle viscous oil wells would cost another \$15 million plus. Collectively it's a higher cost and the only way to develop viscous oil at scale currently is to use this type of technology. It takes two times as long to drill as conventional wells, around 60 days. So they can only reasonably drill five to six a year. Only three rigs currently on the North Slope can drill this kind of well. This is how greater Prudhoe Bay will continue to be developed.

CHAIR HUGGINS asked, "When you drill laterally, is that in your tabulation as well or is it just a lateral drill?"

MR. UTSLER explained that viscous oil is predominantly located in the legacy fields in between and on the western plains of Prudhoe Bay. Since 2000 these technologies have helped four new reservoirs to start producing. He said that BP is working as operator with its working interest owners to develop the viscous oil potential. By the end of this year or the beginning of next year they will have a \$2.1 billion proposal to develop new facilities at the surface to deal with the viscous oil, the development and drilling of new viscous wells and all the facilities necessary to support that. This will unlock 250 million plus or minus barrels of new oil.

[1:30:42 PM](#)

SENATOR MCGUIRE commented that Alaskans have a sense that there's no hope for the future of the oil fields, and people say that BP is not investing in Alaska. Hearing talk about new developments is exciting and hopefully it will make people more optimistic.

MS. FITZPATRICK said some of BP's investments aren't necessarily visible, but they are there regardless and there is a future for oil in Alaska.

MR. UTSLER added that BP believes in the 50-year future of Alaskan oil production, and is adding new employees all the time to plan for tomorrow and the future. It has a lot of pride in the oil field work as well as much awareness and sensitivity to the environment.

SENATOR WAGONER remarked that the sensitivity is due to a zero-tolerance policy, and the industry has not always been so sensitive.

[1:34:28 PM](#)

MR. UTSLER went on to describe the tremendous potential of heavy oil production in Alaska, and showed slides about the history of such production.

[1:36:23 PM](#)

He explained that heavy oil isn't as valuable as light oil in the marketplace; the differential is up to \$14/barrel. Most refineries are not designed to process the heavy oils and would need retooling, so the oil is more costly to refine for use in the marketplace as well.

[1:38:09 PM](#)

SENATOR WAGONER said it would seem more appropriate to try a preliminary process in the field; transportation of heavy oil will eat into the profit.

MR. UTSLER said it is not economically feasible. It will have to be mixed with lighter oils to be thin enough to move through TAPS. Getting it out of the reservoir has to be figured out first. Each step requires development of expensive technologies.

[1:40:47 PM](#)

MR. UTSLER said the majority of that resource base sits in the legacy fields. Injecting diesel, solvents, and steam stimulates production.

SENATOR WAGONER asked how deeply buried the heavy oil is.

MR. UTSLER replied that it is between 1500 and 3000 feet below the surface, below the permafrost. The heavy oil will require many more wells and a way to mix the heavy oil with the light oil at roughly a one to one ratio to move through the Trans-Alaska Pipeline System (TAPS).

[1:43:58 PM](#)

SENATOR WIELECHOWSKI asked how much the increased capital costs for heavy oil would be.

MR. UTSLER replied he couldn't estimate that number at this stage in the process; BP is still developing its first well.

MS. FITZPATRICK added that the first models showed that the wells weren't economic, and the numbers are not fully understood yet.

[1:45:21 PM](#)

SENATOR WAGONER asked if the liquids from a potential natural gas pipeline could be used to help drill heavy oil.

MR. UTSLER replied that it would be an economic decision; there wouldn't be sufficient natural gas liquids distilled to create the dilutants needed for the heavy oil.

[1:47:35 PM](#)

CHAIR HUGGINS commented that Senator French had joined the committee.

SENATOR WIELECHOWSKI said he wants to see BP move forward to profitability and he urged them to get together with the DOR and come up with a scheme.

MS. FITZPATRICK said BP has been working with the DOR, but they are still working out the details of the plan.

MR. UTSLER said that so far, BP has drilled one heavy oil well; it is called the CHOPS (Cold Heavy Oil Production) well. It produces sand along with the oil, which creates flow paths and could increase the production rate. This is still in the development phase.

[1:50:33 PM](#)

MR. UTSLER said that, using the state's data, drilling a heavy oil well costs \$16/barrel.

SENATOR WAGONER asked why he used the state's data, because BP's data is more accurate.

MS. FITZPATRICK replied that BP wanted to keep the calculations simple, and the state's data looks reasonable to BP although the company does anticipate that costs will be going up.

[1:51:57 PM](#)

MR. UTSLER explained the higher operating costs in Alaska compared to the average U.S. cost structure which would disadvantage the product's profitability.

SENATOR WIELECHOWSKI asked if the production tax was included in the \$16-dollar figure quoted.

MS. FITZPATRICK replied yes.

SENATOR WIELECHOWSKI asked how much of the Alyeska pipeline BP owns.

MS. FITZPATRICK replied that the company owns about one-third; BP views profitability from an upstream perspective.

SENATOR WIELECHOWSKI asked how BP chooses one profitable project over another.

MS. FITZPATRICK replied that investment decisions aim to balance their global portfolio. The factors of cost, fiscal position, geological and technical risks, and the existence of other opportunities are weighed. There is no single criterion.

MR. UTSLER added that BP's is not an unlimited investment pool. The company starts with a list and works through it. Each year a whole new set of projects comes forward; the investment is incremental.

CHAIR HUGGINS said that there is not one single template for all situations.

[1:58:58 PM](#)

MS. FITZPATRICK said the quality of the resource is known. The engineering needs will continue to be difficult and BP has not yet proved it can get the heavy oil.

[2:00:44 PM](#)

She then referenced the blue line on a slide indicating oil production decline and how the future of oil production is critically dependent on existing large fields and additional investments. She said the blue line didn't adequately show the difference between light and heavy oil, but explained that the IRS attempted to differentiate the two with the windfall profit tax and abandoned doing it, because they couldn't do it successfully. Both Norway and the UK have had many years of conversations trying to establish how it could be done, but hadn't managed it yet. The interdependence of heavy oil and light oil is complicated. She stated, "Speaking from my own perspective, there are many days I know sitting in the office that I wish it could be differentiated more easily simply for me in terms of managing performance. It's not possible."

MS. FITZPATRICK went to the mustard-yellow line indicating additional investments in existing fields and commented that BP estimates about half of that is coming from heavy oil and the other half from light oil. That was the basis of some of her arithmetic for the \$25 billion versus \$70 billion estimate. She reiterated that new technology is key, but there is no guarantee that that will deliver and new investment is needed to keep even the low estimate number and certainly to move it above that number. Of the two new developments, they hope Pioneer will come on next year with Oooguruk and that they can progress on the Liberty field in the next year or two. However, she pointed out that those were on federal lands as opposed to state lands; so they wouldn't be subject to PPT - but she thought the DNR used those numbers in its long-term forecasts.

She reiterated two key issues - the interdependence of light and heavy oil and the facilities and infrastructure. She explained that the North Slope was built with a 25 to 30-year life in mind and now BP is looking at the next 50 and hopefully many years beyond that. So it is appropriate to consider whether the infrastructure is the right one for the next 50 years or if another would be more efficient and fit for the purpose of the up and coming mixed hydrocarbon streams. This investment would be substantial and wouldn't come through in terms of more barrels, but not having it could impact the cost structure of the barrels that are actually getting produced.

SENATOR WIELECHOWSKI commented that this chart she is referencing goes out only 19 more years, but she said that BP is planning to be here for 50 years. He asked if she had modeling somewhere that shows BP can sustain production for 50 more years.

MS. FITZPATRICK replied that the chart came from the DOR and she does have a chart and schematic with a lot of assumptions in it that goes out 50 years. All of its facilities on the North Slope have it on the wall.

[2:05:37 PM](#)

She then showed another slide regarding the fields from which the oil will be produced and how they would affect state revenue. She pointed out that 70 percent of the barrels will come from Prudhoe and Kuparuk.

She went back to the question of how BP makes its investment decisions. She said they use a mixture of things, but no magic template; clearly costs are a part of it. The global steel

shortage will impact the cost structure; there is also a finite supply of rigs on the North Slope. If BP wants to increase its rig count, it would be in direct competition with the other producers. If they get another one up there, it would need a significant revamp to fit the purpose or build new ones. Those discussions would happen in today's supply environment. So, if she wants those things, the market is competitive and the prices are going up.

[2:07:24 PM](#)

SENATOR MCGUIRE asked about the degree to which stability of the political environment impacts BP's decisions.

MS. FITZPATRICK responded that political environment does impact decisions in terms of post-tax cash flow and fiscal policy.

SENATOR MCGUIRE said that people in the public and the capitol want to negotiate what the profits will be.

MS. FITZPATRICK said she is well aware of that fact.

SENATOR MCGUIRE said that people are also thinking about the possibility of another company doing the same business.

[2:12:32 PM](#)

SENATOR WAGONER commented that the replacement of BP's pipeline was estimated at \$255 million and asked if a more recent estimate was available.

MR. UTSLER replied that the pipe has been ordered and would be replaced in the upcoming winter season, at around the same cost as originally proposed. However, there are inflationary costs associated with the manpower needed.

MS. FITZPATRICK thanked Senator Wagoner for his question, and commented that all costs don't increase at the same rate at the same time. She added that BP will continue to develop, but there is a question of scale and pace; attracting investment is key.

SENATOR WIELECHOWSKI said he planned to look at the state's data on the issue, and since the state and BP are partners, he would like to see the company sit down with administration.

MS. FITZPATRICK agreed, and she said she would like the DOR to share its models with her. A number of things in the proposed bill concern BP, and any sort of changes made should be assessed

as to whether they would increase or decrease the risk in meeting objectives.

[2:21:46 PM](#)

SENATOR MCGUIRE asked if there had been any discussion about whether BP would prefer to address the question of tax rates now or in 2011.

MS. FITZPATRICK replied that from her perspective, from what they understood the purpose of PPT to be in terms of increasing investment, she hadn't had any indication that is not yet working. So she thought it was too early to say; she will design a business plan around whatever the law is. The current law is PPT and it has a review date on 2011; she will respect that law.

SENATOR MCGUIRE said she didn't disagree and that the committee will focus on the practicalities of the issue. However, there is an overarching political dilemma regarding the way in which previous decisions were made, and the committee needs to find a way to encourage the public trust. It is a reality and it cannot be changed. She said it is in BP's best interest to encourage this trust as well.

SENATOR GREEN said that there is nothing to keep the legislature from addressing the tax issue every year.

[2:25:56 PM](#)

CHAIR HUGGINS said that the numbers are important to the issue, and the people that rely on BP for business are an important component of the issue; he appreciates seeing the data about those people from BP.

SENATOR GREEN noted an upcoming meeting pertinent to the issue.

MS. FITZPATRICK quoted some data regarding the number of jobs tied to the oil industry in Alaska.

[2:29:47 PM](#)

SENATOR WAGONER thanked the presenters, and asked if Bill Allen and Rick Smith were representing BP when they were lobbying.

MS. FITZPATRICK responded that BP is not under investigation.

CHAIR HUGGINS called an at-ease at [2:32:05 PM](#) and called the meeting back to order at [2:43:33 PM](#).

KEVIN MITCHELL, Vice President of Finance and Administration for ConocoPhillips (CP) Alaska, said that CP is Alaska's largest producer and leaseholder, and a major explorer and industry community supporter.

[2:46:03 PM](#)

He said that industry and the state should be in partnership; it is too early to determine whether the PPT is doing what it was expected to do, and thus too early to make any changes. An increase in taxes will mean the industry will make a claim that investment will be inhibited.

He said that his presentation would show how an increased PPT would impact investments; that hadn't been done in previous testimony. He then showed a chart for the 2007 fiscal year and the projections from when the Economic Limit Factor (ELF) system was in place. He explained that the PPT is delivering higher revenues than expected, and that prices of oil have been higher as well. However those prices have been offset by higher costs. Prices, production and costs have all differed from predictions, but such variances are a part of business.

[2:50:26 PM](#)

He explained that actual results always differ from the budget because of prices, volumes and costs. It is difficult to budget with run-up in prices and the inflation rates of goods and services; it's important to think about the bigger picture of revenue shaping up to expectations. PPT contains a safeguard for the state of a 10 percent minimum gross tax on the legacy fields. This makes the tax very regressive by increasing it when industry is suffering the most and when prices decline. The 10 percent floor can be triggered by lower prices or higher investments.

[2:53:15 PM](#)

CHAIR HUGGINS asked if that conversation had been held with the administration.

[2:53:55 PM](#)

MR. MITCHELL replied that the administration does understand the argument. He then showed a chart explaining how the tax floor is calculated, and gave an example. He explained how the additional investment in the example did not attract any incentive.

SENATOR WAGONER said that the credit is still there, but they weren't able to use it all.

MR. MITCHELL replied that was correct, but depending on the spend profile over a period of years; they might not ever get to use it.

CHAIR HUGGINS suggested, "It's a disincentive."

[2:57:55 PM](#)

MR. MITCHELL agreed and showed the next page which was more like reality. He scoped out what a Kuparuk budget might look like using DOR assumptions for volumes, prices, operating expenses, and capital expenses. It indicated the net tax to the state would be \$408 million. Investments are not getting the benefit of the credits and features meant to incentivize. He said that the reality is that the tax will have the same impact in a higher investment climate.

JIM TAYLOR, Vice President of Commercial Assets for ConocoPhillips (CP), said that CP participates on all levels of production and exploration in Alaska. He showed an excerpt of the DOR's projection for the industry, and said that since 1999 CP's exploration wells have led to new fields and satellites with a minimal footprint, yielding 6,000 barrels a day.

[3:05:34 PM](#)

SENATOR WAGONER asked if certain fields on the diagram were ones that had been discovered but not put into production yet.

MR. TAYLOR said that he was not sure; the point is that CP wants to see those fields explored. He then explained different elements of the diagram, and talked about which fields oil will come from in the next decade; investments need to be made in the legacy fields.

[3:08:06 PM](#)

He said that there's a lot of challenge in future opportunities and a lot of needed technological advances. The viscous oil is a large resource base and unlocking its potential is a major focus.

SENATOR WIELECHOWSKI asked about CP's progress in technology for producing viscous oil.

[3:09:33 PM](#)

MR. TAYLOR replied that he has spent time in Canada and there are a lot of emerging technologies there; it's a matter of using them appropriately and having a good economic scenario. Alaska has taken some steps towards meeting this challenge. What makes

the recovery of viscous oil so challenging is that the costs are higher from the start, and the production profile starts out lower and remains flatter over time. The Century project in Canada epitomizes the shallowest of heavy oils; such deposit projects have the advantage of having the infrastructure built already and by having to take small steps along the way. However, as oil prices increase, so do opportunities.

[3:12:07 PM](#)

He then talked about the challenges associated with getting the heavy oil out of the ground, and how it has a lot of associated sand production. He said anything they do that would affect the economics for marginal fields can delay or defer investment there or cause it to become uneconomic. These are real situations they are dealing with today.

SENATOR WAGONER asked what CP will do with the sand.

MR. TAYLOR said there is a plant for disposing of byproducts of production, which are re-injected in similar zones from which they came.

[3:14:45 PM](#)

He said a sizable oil target remains in the legacy assets and that price and the advances in technology have presented this investment opportunity to the industry. He showed them examples of the West Sak wells that have been completed in the Kuperuk area. He pointed out that a single well bore has three different well bores that penetrate a variety of stacked sands. The length from the original well bore to the final length of the well can range anywhere from a mile to a mile and a half. They extend long distances and need technology to make it possible to penetrate the thin sands.

Also because sand production as a byproduct is a possibility, he showed them various completion techniques that can prevent that sand from coming into the wells. They add complexity, cost and risk.

[3:18:46 PM](#)

CHAIR HUGGINS asked for elaboration on water versus oil production.

MR. TAYLOR said in Kuperuk and Alpine, CP is producing 250,000 gross barrels of oil daily with an associated 650,000 gross barrels of water; the ratio is approximately three to one. In addition, CP is injecting seawater as an enhanced recovery

mechanism, so the combined handling is close to 1 million barrels of water daily. He then referenced a table showing the six projects that CP is currently dealing with; the company has a large portfolio of options. Four out of the six are satellite-type projects, and the majority dealt with heavy or viscous oil. The projects are significant if aggregated.

[3:22:23 PM](#)

CHAIR HUGGINS asked if Mr. Taylor was talking about the project modeling.

MR. TAYLOR replied that he was.

CHAIR HUGGINS asked about Mr. Taylor's confidence in the model data in question.

MR. TAYLOR said the data came from consultants who used a wide range of possible projects, but the costs in reality might be higher and the economic results may depend on the investor's actions.

SENATOR WIELECHOWSKI asked how what percentage of Field A was on the North Slope.

[3:24:58 PM](#)

MR. TAYLOR referred to a chart that showed six different projects of an aggregated 50,000 to 60,000 barrels a day. There are 2 billion barrels of oil remaining in the legacy fields, and the viscous and heavy oil target could range between four and 20 billion barrels. While there are significant viscous and heavy oil reserves, they represent a larger target than can be simulated and they do rely heavily on conventional oil; the gross minimum could cause an obstacle to investments.

MR. TAYLOR then referenced another diagram showing how different projects would look under different prices. Under the current PPT, developments are advancing well, he reported.

[3:28:11 PM](#)

SENATOR WIELECHOWSKI asked if Dr. Finiza's estimates were done at \$40-dollar stress rate.

MR. TAYLOR replied yes, and said that the calculations showed that projects would not be economic at \$40.

SENATOR WIELECHOWSKI asked for the net present value.

MR. TAYLOR replied that he was portraying the investors' view of the black solid line with the zero MPV at some hurdle discount rate. Anything above that line would meet or exceed that hurdle and create value; anything below it would not. He explained how these projects are challenged with higher development costs and technical reserve risk. An increase in tax has erosion effects on investment that could turn a project uneconomic because investors didn't receive deductibility.

SENATOR WIELECHOWSKI asked for clarification of net present value between Project 2 on the previous page and Project 5 on the current one.

[3:31:23 PM](#)

MR. TAYLOR explained that anything below the indicated line destroys MPV value and those above have value-added characteristics.

SENATOR WIELECHOWSKI said that the two projects seemed close together on the graph, and looked identical under PPT tax rates.

MR. TAYLOR responded that he would have to compare tax effects and lifting costs on different graphs.

CHAIR HUGGINS commented that the graph didn't do justice to the numbers used.

MR. TAYLOR agreed. He said that his main point was that the gross minimum may have unintended consequences, and he wasn't sure that it captured the full reality of the situation. It may need to be reexamined.

[3:34:12 PM](#)

MR. MITCHELL said that transitional investment expenditure (TIE) credits were introduced into PPT legislation to provide compensation to investors who had invested under a prior tax structure and who will invest in future years. He then gave an example of how TIE credits would work on a development field and explained that a company doesn't get the benefit of it without continuing investments.

[3:37:49 PM](#)

CHAIR HUGGINS asked if the TIE credits had a 2008 sunset date.

MR. MITCHELL replied that they have a five-year sunset period. They are on a two-for-one basis, so a double expenditure is

required over the five years. If the sunset were in 2008, their value would erode.

CHAIR HUGGINS said that in his opinion the TIE credits are disproportional or punitive and the punitive factor should be examined.

MR. MITCHELL agreed. He said he would then briefly discuss CP's position on the legislation. The bill includes an increased level of transparency between the state and the industry, and CP is supportive of that. However, a handful of areas cause them concern including provisions on exploration confidentiality. Some of the explorers will find these be anticompetitive, he said. Cost deductions are another concern and he suggested that lease expenditure deduction should be defined in statute. He urged a full and thoughtful discussion about what the bill wants to accomplish.

SENATOR WIELECHOWSKI asked if CP wanted continued inclusion of dismantlement costs.

MR. MITCHELL relied that the PPT allows for a proportionate share of dismantlement costs. These are necessary expenses in the full life of the field, and CP would view dismantlement costs as a legitimate part of doing business on the North Slope.

SENATOR WIELECHOWSKI asked if including dismantlement costs would encourage investment.

[3:44:16 PM](#)

MR. MITCHELL replied that those make up just one cost component that is factored into the overall economic decision. Including them would help slightly, but at the initial start of the field they don't make a huge impact. He explained that such inclusions are crucial to attracting investors to such a harsh climate.

MR. MITCHELL said that CP absolutely believes that the industry must be aligned with the state and currently there is not enough information to make changes in the PPT. The risk of not getting the right solutions also exists. The third tax change is significant, and no one wants to have to revisit the issue. The 10 percent legacy floor will have a real effect.

[3:47:36 PM](#)

CHAIR HUGGINS said that the presenters had pointed out unintended consequences, and that those are some things to pay attention to. Great Alaskans are writing the regulations for the

PPT, and that takes time. The state does owe CP answers, and it will get them. He commended the administration for recognizing and addressing investment decline, and said that the industry has to bear the brunt of the good and bad.

SENATOR WAGONER said that he would like a response letter regarding prior comments.

MR. TAYLOR replied that none of CP's employees were currently under investigation, and the company's intention is to continue to be active in the process.

CHAIR HUGGINS called a recess at [3:52:32 PM](#) and reconvened the meeting at [6:15:55 PM](#). He announced that the committee would take public testimony.

[6:16:20 PM](#)

BO DARRAH, President of the Brooks Range Petroleum Company (BRPC), said that his company is the newest explorer on the North Slope, and his message is to hold with the status quo. His company is dependent on outside investors; it agreed to explore under ELF and it doesn't believe the proposed system will attract business or cause the producers to make additional investments. As a non-producer, BRPC don't realize any profit now so its investments are high risk. Its end goal is to be a producer, so it's looking at the bill from that perspective. BRPC probably shares the same view of ACES as the major producers. His opinion is that three tax increases in three years is not the answer; the tax is good now and enough time hasn't elapsed to fully judge it. The state is jeopardizing its reputation by changing it again.

[6:25:13 PM](#)

SENATOR STEVENS thanked Mr. Darrah for his confidence in the industry, and asked where BRPC's exploratory wells will be located.

MR. DARRAH said that the company is drilling east of Newitsit and also north of Prudhoe Bay.

CHAIR HUGGINS said that one of the challenges the state faces is that the average citizen only thinks of the big three producers and loses track of the BPRCs of the world; the company's size of exploration is the future for Alaska.

MR. DARRAH said the benefits of PPT do help start-up companies but ultimately his company hopes to be in the big game.

[6:28:37 PM](#)

MARK SHARP, representing himself, said that he testified 18 months ago that PPT was flawed from the start, because the net profits would lead to a gross overstatement of expenses and understatement of profits. Clearly PPT was best for the industry and the 24th Legislature abdicated its responsibility in passing it. The state needs to set the policy standard and make the industry adhere to it. He favored a gross tax.

CHAIR HUGGINS said he recalled that the administration was recently in Fairbanks and asked if Mr. Sharp attended the meetings.

MR. SHARP replied that he did, and said that the gross portion of the governor's proposed tax doesn't kick in until oil prices reach \$30 a barrel; so it appears to him that the tax is more net-based than a hybrid.

[6:35:36 PM](#)

JERRY WALKER, representing himself, said he was a board member of the Alaska Support Industry Alliance. He said that the legislature's role is to recognize the importance of fiscal stability, and that means it shouldn't keep changing the rules. The legislature should not change the PPT, but rather work to increase investment in Alaska.

[6:37:39 PM](#)

RICH SIEFERT, representing himself, said that he agreed with Mr. Sharp, and has always advocated a production tax. The state is experiencing a peak oil crisis, and that factor will serve as a driver to keep the price of oil high. That will make capital available, which is what the legislature is looking for; it's a good bet to assume that the availability of profits from oil sales will render incentives unnecessary.

CHAIR HUGGINS said that some members of the committee were familiar with the peak oil idea, and agreed that and it is very important.

[6:41:52 PM](#)

TOM LAKOSH, representing himself, said he wanted to see focus on what lessees are required to develop in the ground; there's no correlation between tax breaks and oil a company hopes to produce. There should also be focus on how the Department of Natural Resources (DNR) and the Alaska Oil and Gas Conservation Commission (AOGCC) will regulate hydrocarbons. He recommends

setting rates of parity with the industry in Norway and to focus on providing an infrastructure that will help all Alaska. He noted that the termination of the Point Thomson leases was a good example; there shouldn't be a "scatter-gun" approach in giving out more money. He also suggested the legislature pursue a carbon tax.

[6:48:12 PM](#)

MERRICK PEIRCE, representing himself, said he's pleased the governor had the courage to call the special session to question how the sale of oil is taxed. Article 8 of the State Constitution requires that the state's oil and gas be sold such that they return the maximum benefit to the people; clearly that isn't happening now. It was frustrating to testify last year because of the things that have since come to light, and it was frustrating that the legislature killed a bill that would have allowed the DOR to offer competitive salaries to hire tax auditors. Currently, \$23.5 billion worth of the state's oil resources are leaving the state annually without anything to show for it. Fairbanks has high property taxes and high prices for heating oil, and the state infrastructure is failing. Clearly Alaska is not getting a reasonable rate of return. He said he would like the committee to answer the following questions that hadn't been addressed:

1. Where are the core comparisons that show net profit is better for the state and development than a gross tax with simple price escalators and capital credits, and how solid is the data for those comparisons?
2. Oil production is declining from the North Slope, has been declining for decades, and is continuing to decline under PPT. According to the consultants that are working on the bill, fifteen-year forecast levels are even lower than in prior forecasts. With world conditions unfavorable to oil investment in other areas and prices remaining high, where is the data showing Alaska is getting fair value?
3. Everyone knows that TAPS tariffs increased substantially after PPT was passed. This increased big oil's tax burden to the state while at the same time diminishing incentive for independent oil companies to develop on the North Slope due to higher tariffs. Does it make sense to give away production taxes before correcting that disincentive for independents to develop fields on the Slope?

MR. PEIRCE said he looked forward to hearing the committee discuss how the state will diversify the economy and create well-paying jobs by stopping the give-away of billions of dollars every year by underselling and under-taxing the state's oil. He added that he didn't hear anyone standing up for Alaska when the producers run propaganda advertisements that the state is actually paying for through tax deductions. The producers are claiming that allowing billions of dollars to leave the state to multinational corporations is somehow good for the Alaskan economy. That's not true and that propaganda must be challenged.

CHAIR HUGGINS asked if Mr. Peirce had attended the recent administration's presentation on this bill up in Fairbanks. One of its tasks was to give an overview with emphasis on why they selected a net component versus a gross component for the tax concept.

MR. PEIRCE replied that he did. He said the presentation by the administration was "didactic." It was advanced that the issue was very complex and the average member of the public just was able to fathom it. He share that an acquaintance in the oil industry who really cares about Alaska said if you come up with a complicated scheme such as a net profit system of taxation, the oil industry will always have better talent - whether it be lawyers or tax auditors - that the State of Alaska will have. It doesn't really matter to the oil industry if the rate is 22.5 percent or 25 percent; it would always find a way to profit from tax laws more than the state.

[6:57:22 PM](#)

SENATOR GREEN questioned an explanation in previous testimony that advertising was not deductible.

MR. PEIRCE recalled that in part of that discussion an amendment was offered on the House floor that made it illegal for the oil industry to deduct lobbying expenses under PPT; and that measure failed. He didn't know about advertising.

SENATOR GREEN remembered that both advertising and media aren't allowable deductions.

[6:59:01 PM](#)

TOM MALONEY, representing himself, described his background in accounting and finance, and said that lots of discussion centers around the taxation of legacy fields such as Prudhoe Bay and Kuparuk. He said that 100 percent of the capital costs for the infrastructure were paid for by private funds. Some fields have

become uneconomic, so those owners took on all the risk. New fields will be required, and for that to happen there needs to be more tax relief. If the state wants to tap heavy oil, it must recognize that those fields cost more and produce less than the legacy fields. The legislature needs to define tax rules for new investments. He asked the committee to think about what can be done to stem production decline, and said he'd like the existing producers to continue to bring capital investment to the state; PPT would encourage that.

[7:03:54 PM](#)

PAUL KENDALL, representing himself, said he wanted to thank the governor because AGIA opened up discussion that had been neglected. He said he has been watching the development of the hydrogen industry closely, and believes there is some interest there. Hydrogen fueling stations are being built around the world so there should be caution in terms of the oil pipeline. The state should think about what it would do if the oil companies decided to pull out and prepare for the worst-case scenario. The workers like him in the oil field have little impact or reward, and there is a small number of people that reap all the benefit. He said he would prefer to see a gross tax.

CHAIR HUGGINS announced an at-ease at [7:14:01 PM](#) and called the meeting back to order at [7:20:06 PM](#).

[7:20:07 PM](#)

TONY TENGS, representing himself, questioned whether everyone who says they're representing themselves actually is because the oil companies are making a full-court press; he said he hopes the committee factors in that possibility. He said he is for simplicity and a gross tax and hoped the legislature comes up with a fair deal for the state.

CHAIR HUGGINS said that it is always nice to hear from citizens, and agreed that the system isn't perfect. There being no further business to come before the committee, Chair Huggins adjourned the meeting at [7:26:42 PM](#).