

ALASKA STATE LEGISLATURE
SENATE RESOURCES STANDING COMMITTEE

February 22, 2012

3:33 p.m.

MEMBERS PRESENT

Senator Joe Paskvan, Co-Chair
Senator Thomas Wagoner, Co-Chair
Senator Bill Wielechowski, Vice Chair
Senator Lesil McGuire
Senator Hollis French
Senator Gary Stevens

MEMBERS ABSENT

Senator Bert Stedman

OTHER LEGISLATORS PRESENT

Senator Cathy Giessel
Senator Joe Thomas
Senator Dennis Egan

COMMITTEE CALENDAR

SENATE BILL NO. 192

"An Act relating to the oil and gas production tax; and providing for an effective date."

- HEARD & HELD

BP EXPLORATION (Alaska) OVERVIEW BY CLAIRE FITZPATRICK

- HEARD

PREVIOUS COMMITTEE ACTION

BILL: SB 192

SHORT TITLE: OIL AND GAS PRODUCTION TAX RATES

SPONSOR(S): RESOURCES

02/08/12	(S)	READ THE FIRST TIME - REFERRALS
02/08/12	(S)	RES, FIN
02/10/12	(S)	RES AT 3:30 PM BUTROVICH 205
02/10/12	(S)	Heard & Held
02/10/12	(S)	MINUTE(RES)

02/13/12	(S)	RES AT 3:30 PM BUTROVICH 205
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02/22/12	(S)	RES AT 1:30 PM BUTROVICH 205
02/22/12	(S)	RES AT 3:30 PM BUTROVICH 205

WITNESS REGISTER

CLAIRE FITZPATRICK, Chief Financial Officer
 BP, Alaska
 Anchorage, AK

POSITION STATEMENT: Commented on BP's historical role in Alaska and how SB 192 would affect it going forward.

DAMIAN BILBAO, Head of Finance: Developments and Resources
 BP, Alaska
 Anchorage, AK

POSITION STATEMENT: Focused on future implications of SB 192 on BP's production and profits.

ACTION NARRATIVE

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CO-CHAIR JOE PASKVAN called the Senate Resources Standing Committee meeting to order at 3:32 p.m. Present at the call to order were Senators Wielechowski, McGuire, French, Stevens and Co-Chair Paskvan.

CO-CHAIR PASKVAN stated for "housekeeping" purposes that he meant to adjourn the 1:30 Senate Resources meeting instead of recessing it.

SB 192-OIL AND GAS PRODUCTION TAX RATES
OVERVIEW: BP EXPLORATION (ALASKA)

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CO-CHAIR PASKVAN announced the consideration of SB 192 and a presentation from BP on how the state tax rates affect its Alaska activities.

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CO-CHAIR WAGONER joined the committee.

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CLAIRE FITZPATRICK, Chief Financial Officer, BP Alaska, said she will be moving on to a new role after five years in Alaska and a decision was made that Damian Bilbao would be the most appropriate person to take over her position.

She said that the Trans Alaska Pipeline (TAPS) is two-thirds empty and production continues to decline. More investment is needed to increase production and they intended to discuss options to improve investment climate. BP supports the governor's policy of having a meaningful change in tax policy and the 1 million barrel goal; they would like to see lots of things done to see Alaska achieve that goal.

MS. FITZPATRICK said Alaska has great resource potential and much of it is within existing fields. However, the financial environment is not as competitive internationally as it could be and therefore it isn't attracting the level of investment that is needed to put more oil in the pipe. She said, "The state's biggest lever for increasing production is meaningful ACES tax change."

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MS. FITZPATRICK said she wanted to address three outstanding questions: one was that the GHX equipment is not in the state, but in warehouses in Houston. The second was relative to the status of I-pad for which they are doing a number of studies to address four primary technical challenges based on how to process large quantities of solid-laden viscous oil (primarily in the GC-2 area) and how to improve the artificial lift of viscous wells - removing more subsurface uncertainties and focusing on how to build a well pad of the future.

The third question was whether the challenges are technical or economic; and her answer to that was resolving technical challenges helps solve the economic challenges. She said the

state has an opportunity to help resolve those technical challenges, which are also economic, in how it deals with its fiscal policy.

SENATOR WIELECHOWSKI said the committee has heard that if they pass some tax breaks BP is committed to developing the multi-billion dollar I-pad project, and he wanted to hear more about those challenges. And they also just heard from the director of the Division of Oil and Gas that that project had been in a plan of development for the past five years; and when he asked if it was being held up for economic or technical reasons, the director didn't hesitate to say "technical reasons." He asked Ms. Fitzpatrick is she was disagreeing with him.

MS. FITZPATRICK answered that she is not disagreeing. Technical challenges include more than just engineering, they include commercial challenges as well. She wants to do any project as efficiently and effectively as possible and will always seek to drive efficiencies through technology, costs and the fiscal environment. On the I-pad project the technology is out of her control, but she can encourage fiscal change, which is in the state's control.

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SENATOR WIELECHOWSKI asked if the project is being held up by the ACES tax structure and if it would go forward under the governor's proposed tax structure.

MS. FITZPATRICK replied:

The pace at which we would progress projects would increase, because we would have the ability to take more resource onto them. But there are a lot of projects that we have which we refer to as kind of a hopper of opportunities and we keep a number of them warm. It's like an incubator waiting for when it's the right time.

CO-CHAIR PASKVAN asked the maximum realistic throughput they could expect from I-pad.

MS. FITZPATRICK said she would need to find that out.

CO-CHAIR PASKVAN asked, assuming investment is made in I-pad, if the intent is to slow the rate of decline or increase the rate of throughput for FY12.

MS. FITZPATRICK replied I-pad will not generate volumes in this year or next, because a lot of facilities will have to be built and that will take several years, but the faster they can move on some of that, the faster it will come through.

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CO-CHAIR PASKVAN asked when it becomes operational if it would increase BP's throughput numbers over FY11 or FY12.

MS. FITZPATRICK replied yes, in addition to whatever production is at that point in time.

CO-CHAIR PASKVAN asked if the incremental production would result in a continuing decline curve but one continuing at a smaller percentage.

MS. FITZPATRICK replied, "Maybe not growing, but certainly flattening off."

CO-CHAIR PASKVAN said that would be well received.

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MS. FITZPATRICK said she would provide some context around BP's track record of developing Alaska's natural resources to date and what they are doing to prepare for Alaska's next 50 years of oil and gas development, highlight some of the opportunities that remain within existing fields and the technical challenges to progressing some of them, as well as how the state can help in reducing some of those challenges.

CO-CHAIR PASKVAN noted that Senator Thomas joined the meeting.

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MS. FITZPATRICK responded said that BP has recovered over 12 billion barrels from Prudhoe Bay that is the largest field in North America and one of the top 10 fields in the world. Development of Prudhoe Bay enabled the construction of the TransAlaska Pipeline; the existence of both the pipeline and Prudhoe Bay enabled developed of the other fields on the North Slope. She said 187 Society of Petroleum Engineers technical papers have been written about Prudhoe Bay. It is an absolutely amazing "subsurface set of rocks" and BP uses it with great pride.

MS. FITZPATRICK said the ability to develop Prudhoe Bay the way they have has required working interest owner alignment and that is what will underpin their ability to achieve activity in the

future. BP is a minority owner and operates Prudhoe Bay on behalf of ExxonMobil and ConocoPhillips (35 and 36 percent respectively) and Chevron that has a small interest (1 to 2 percent). It is a mature field that has been in production for over 35 years. They have gone from producing volumes of mainly oil to producing the same volumes but now they consist mainly of water.

CO-CHAIR PASKVAN asked what the dotted line is intended to represent.

MS. FITZPATRICK answered that it is a visual representation of the fact that the volumes haven't dropped that much, but that the oil content has dropped significantly. She noted that they also handle large volumes of gas, which is recycled and re-injected with the water to keep the pressure up in the reservoir. This is one of the reasons recovery is higher than originally anticipated.

CO-CHAIR PASKVAN asked if the recycling was done because of constraints in the treatment facilities in the Prudhoe Bay area.

MS. FITZPATRICK answered no; the facilities were designed to handle it.

CO-CHAIR PASKVAN said the facilities have to handle three streams - oil, gas and water - and asked if the throughput decline is a result of treatment facility constraints when you have higher WOR or GOR values.

MS. FITZPATRICK answered no, and added that BP always looks for opportunities to maximize their ability to handle fluids to maximize the oil recovery.

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She related that Prudhoe Bay isn't the only field BP operates in Alaska; it operates three other major fields and is a 39 percent owner in the ConocoPhillips-operated Kuparuk field. All are mature; the main ones are Milne Point, Endicott and North Star. BP previously had Badami, but transferred operatorship to Savant as a means of allowing others to access value where they see more than BP does. This is a part of the natural cycle of insuring that other people are being able to bring forward their opportunities. She said they, like at Prudhoe Bay, are seeing increasing challenges in handling water and the resulting high operating costs combined with declining production. She said efficiently executing activities and developing new technology

maximizes each field's ultimate recovery and extends its useful and economic life as long as possible, and a good tax policy would help do the same.

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MS. FITZPATRICK said since 1995 many material sources of oil have offset the decline (referring to graph 5 depicting the initial producing area (IPA)). Investments in those fields were made possible by a fiscal environment that supported investment at scale.

SENATOR FRENCH asked if Alaska tax rates were competitive internationally before ACES and PPT.

MS. FITZPATRICK replied yes; probably at times more attractive than needed to be, but now they have gone the other way.

SENATOR FRENCH asked what the decline curve of Prudhoe Bay production was in those years.

MS. FITZPATRICK replied that it was different in different years depending on when various fields came in; it was also impacted by the extent of well work-over and drilling. The decline varied between 3 and 6 percent, but she would have to check.

SENATOR FRENCH asked where the greatest opportunity is for BP - inside of the Prudhoe Bay reservoir or outside of it.

MS. FITZPATRICK replied both. There are still great possibilities inside of greater Prudhoe Bay as well as significant opportunities in other areas further west and heavier oils. She is always hopeful that there are opportunities in areas where people are exploring and looking for new things.

CO-CHAIR PASKVAN asked why the decline from the central North Slope started in 1989.

MS. FITZPATRICK replied that she would be making wild speculations on physics to answer that, but most of the decline was driven by subsurface issues and a subsurface person could better answer that.

SENATOR WIELECHOWSKI said he was responding to her statement that there are times when Alaska has not been internationally competitive, and asked who Alaska's international peers are and at what levels the tax structure is broken.

MS. FITZPATRICK replied that Alaska should be competing with itself in terms of how much investment they want, what sort of production rate they want in the pipe, what sort of investment climate they want (from exploration to mature fields) and what is needed to achieve it.

SENATOR WIELECHOWSKI said he thought that was the best answer to that question and added that he thought the state's lease terms require development when it's reasonably economic for a company to make a profit. He asked what fields, projects and developments are not economic under ACES that will be economic under another tax structure.

MS. FITZPATRICK replied, "It's a lot more complicated than just an incremental project that I'm looking at." When she looks at an incremental project she looks at the cost of that activity and the volumes it brings in. This concept assumes that existing production (which is currently declining) pays for everything else. This is not a good place to be in in terms of price and cost structure and BP continually challenges itself to find the "best place to do some of this stuff." In 2007 when ACES passed, they said they weren't going to stop doing things, but they had to weigh getting funds to do more there.

SENATOR WIELECHOWSKI asked if they could look forward to having a specific field or project on line if oil taxes were rolled back.

MS. FITZPATRICK replied they could expect to see a change in the level of drilling activity, and "high grading" of BP's best projects to move forward. It would encourage another \$5 billion of investment, which would crack the technology to move forward, but she said, "It needs the two together."

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CO-CHAIR PASKVAN asked if she is talking about conventional oil development in the next five or six years.

MS. FITZPATRICK replied yes; but BP is also moving into the viscous oil with one heavy oil pilot and two years of funding for it.

CO-CHAIR PASKVAN asked a reasonable timeframe in which to expect heavy oil production.

MS. FITZPATRICK replied if she had complete success and the pilot completely "blew me away," if these wells flowed and were

sustained and she could figure out how to do that economically, it would take 10 years to get 10,000 barrels a day (MBD) more. But it's worth going for, because the numbers ramp up after that.

CO-CHAIR PASKVAN remarked that would stem the rate of the decline in the hyperbolic curve.

MS. FITZPATRICK said she thought it would flatten the curve, but keeping production at 600,000 MBD rather than dropping to 300,000 MBD would be very good. And she hoped others would be equally successful.

MS. FITZPATRICK stated that BP is committed to Alaska buying and Alaska hiring; over the last three years it has spent over \$7 billion, \$5.6 billion (75 percent) of which has been with Alaska companies. She noted that the price environment had increased due to inflation in 2007, so the level of activity is similar but it had cost more to do.

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SENATOR FRENCH asked if she had the 2011 numbers.

MS. FITZPATRICK replied that she would get them, but they're probably similar to 2010. She said, "We expect everyone to be competitive, but if Alaskan companies can be competitive, we have a bias."

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CO-CHAIR PASKVAN asked how their numbers correspond to the 2008 economic collapse.

MS. FITZPATRICK replied that industry and BP make commitments for buying things well in advance and their ability to stop things is "relatively limited."

SENATOR WIELECHOWSKI said ConocoPhillips has stated Alaska has strong cash margins and very good rates of return (ROR) and that the company had made \$10 billion in profits since ACES passed, and asked if BP had a similar experience.

MS. FITZPATRICK replied over the years she has seen her cash flow deteriorate significantly and stated that she pays her employees and contractors with cash, not profit.

SENATOR WIELECHOWSKI asked if the ROR and profits had been good.

MS. FITZPATRICK replied that her profits are not where they should be.

SENATOR WIELECHOWSKI asked if they were \$2 billion last year.

MS. FITZPATRICK replied that she couldn't remember and that BPXA, Inc., numbers include data that has to do with locations that are not in Alaska. Alaska numbers are not published separately.

SENATOR WIELECHOWSKI asked if the BP royalty trust looks at Prudhoe Bay returns.

MS. FITZPATRICK replied that the BP royalty trust files a 10K, as it is a debt-registered entity, and looks purely at the element of the IPA, which is subject to the royalty trust.

SENATOR WIELECHOWSKI asked if she had any idea of the returns they had gotten in the last five or ten years.

MS. FITZPATRICK replied no.

CO-CHAIR PASKVAN interjected that he had those numbers. Because the BP Royalty Trust is a publicly traded company, it files documents indicating that over the last 10 years the total return had been 2,248 percent on top of a 600-plus percent capital gain. He asked what that indicated about the financial strength of Prudhoe Bay over the last 10 years.

MS. FITZPATRICK replied that she would have to get out the 10K and brush up her knowledge on exactly how the trust accounting works as distinct from company accounting. But the Prudhoe Bay trust is not a true representation of the BP business in Alaska.

CO-CHAIR PASKVAN restated that they are saying that over the last 10 years a \$5,000 investment in the BP Royalty Trust is worth \$117,000 today and that seems rather remarkable given the world's economic collapse.

MS. FITZPATRICK replied that the trust is tied to royalty on the oil; therefore it is linked to oil prices as opposed to world economics, but with that piece of financial advice she would be making a phone call to change her investments.

CO-CHAIR PASKVAN referenced a 2004 BP document indicating: "Alaska's role in BP's portfolio is to provide a stable

production base and cash flow to fuel growth elsewhere," and asked if that was true.

MS. FITZPATRICK responded that Alaska has an important role in BP, but it does not provide a significant amount of cash flow versus what was produced in 2004, because production volumes, tax structures and cost structures are very different. BP's group strategy involves two tenets: enhancing and maximizing recovery of the oil from giant oil fields and gas value chains; and Alaska plays prominently in both of those areas. Alaska is the third largest resource base in the BP portfolio and they want to work out how to maximize that for the benefit of the state as well as the benefit of BP. She said emphatically that Alaska is not viewed as a large cash generator within the BP portfolio.

CO-CHAIR PASKVAN asked if that statement was true in 2004.

MS. FITZPATRICK replied that she didn't have the document in front of her and couldn't answer that. She knows they were generating a lot more in 2004 than now.

SENATOR WIELECHOWSKI asked if she had any idea what her profit per barrel is in Alaska.

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MS. FITZPATRICK replied that she doesn't look at a profit basis, but rather her cash break-even basis (how much money she would have to make before she could afford to pay the next new employee) which is pretty high - in the \$70s or \$80s.

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She pointed out that the spend graph includes third parties and doesn't include costs associated with their 2,126 employees. She related that over the past five years BP has provided internships for 54 University of Alaska (UA) students, extended full-time offers to more than 100 UA graduates and over the last 10 years has hired 275 students from the UA process tech programs in Fairbanks, Kenai and Anchorage. While their spend has increased from 2005, a lot of it hasn't been on activities that put barrels in the pipe as opposed to keeping up with inflation and activities that are setting them up for the next 50 years.

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She remarked that the markets changed in the 2008 timeframe that resulted in a fundamental shift in the price environment and if

the state wants BP to attract the amount of investment that would put barrels in the pipe, investments need be higher like what they are in Texas or North Dakota.

SENATOR WIELECHOWSKI asked why from 2002 to 2006 the price of oil went from \$20 to \$60 and yet BP's Alaska investments appear to have declined.

MS. FITZPATRICK replied that the actual rate of spend has declined and some of that would have depended on what rates were locked in along with a lot of other factors. The level of activity has remained fairly flat.

SENATOR FRENCH asked her explain what the bars on the chart represented.

MS. FITZPATRICK said one chart had gross numbers of spend on activities that put barrels in the pipe and the following one was net - as opposed to maintenance and infrastructure and things like that.

SENATOR FRENCH asked how she differentiates between a dollar spent putting oil in the pipe versus maintaining a vessel.

MS. FITZPATRICK replied they capture it separately. Well work, drilling and associated activities are directly putting volumes in the pipe. Other things are maintenance and things that have to be spent to keep the facility functioning.

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SENATOR FRENCH asked if this slide was an internal BP accounting category.

MS. FITZPATRICK replied it's an industry standard category where people will talk about what they are spending on well work, workovers and direct activities associated with that as distinct from facilities, infrastructure and logistics.

SENATOR FRENCH said it's surprising that despite a tripling of the price of a barrel of oil from 2002 to 2006 that BP reduced the money it spent on producing more oil in Alaska. He thought it went to the document Senator Paskvan referenced that they are making lots of money in Alaska but investing it somewhere else in the world. It might be good for BP, but it doesn't help the state produce more oil or employ more people.

MS. FITZPATRICK said she didn't doubt Senator Paskvan's document about 2004, but she was concerned about how to get more money spent on more activities to progress more oil today, tomorrow, and the year after versus what may have been business drivers in 2004.

SENATOR FRENCH said the problem everyone is struggling with is the history of seeing BP taking its money and investing it elsewhere. How do they make sure if they go back to tax terms that are internationally competitive, that produce large amounts of cash for BP that it gets spent in Alaska. "How do we make sure?"

MS. FITZPATRICK said she understood his question and sentiment, but in 2003 they didn't see line of sight to some of the technology that is being implemented and heavy oil wasn't even thought about then. The resource base they see now is larger. Alaska's strategic place has changed in their portfolio, plus they do see about \$5 billion worth of activity and a lot of people want to see those projects move as much as the state does.

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SENATOR WIELECHOWSKI said Senator French hit on the key question; they all want more production, but the state has a 30-year history of low taxes. In 2002 through 2006, tax rates were declining because of ELF. In 2006, 15 out of 19 fields on the North Slope were paying zero taxes. There were record high oil prices, tripling within four or five years and BP's investment was declining; Prudhoe Bay had a 12.5 percent gross tax rate. He said:

Put yourself in our shoes, as those who are designated to make sure we get the maximum benefit for our resource. We've got to make sure that if we push across billions and billions of dollars to you we want something in return, for sure. And we had a system like this just a few years ago and it didn't work - for decades it didn't work. So, what's changed?

MS. FITZPATRICK replied there was a lot of activity in those decades, a lot of fields were brought on line over and above the IPA. Technology has enabled them to renew their view of their resource base in Alaska to a point they didn't have in the early 2000s. They are viewing Alaska as a huge opportunity; their view and strategy is totally different now.

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The chart on slide 8 indicated the shift in oil markets, in-pipe production and what has happened in the Lower 48 relative to Alaska (recognizing Alaska is a long way from the market and has different challenges). It indicated that although the various taxes across the different jurisdictions are fairly similar, the marked difference is in the production tax rates.

CO-CHAIR PASKVAN asked if her chart reflected barrel of oil equivalent (BOE).

MS. FITZPATRICK answered yes.

CO-CHAIR PASKVAN said he assumed because of the shale gas explosion in the Lower 48 in 2006 that you would expect to see an explosion of onshore BOE production in 2008 and asked if that was included.

MS. FITZPATRICK replied if she understood the question correctly, the fact that it is labeled "MBD" would make her think of it as oil as opposed to oil equivalent, but she must confirm that. However, she said shale oil activity is going up.

CO-CHAIR PASKVAN said he wanted to make sure that they are talking about apples to apples, because Eagleford is producing a lot of shale oil, the Bakken is all shale oil and Marcellus is essentially all shale oil.

MS. FITZPATRICK said it wasn't the intent to have apples and oranges, but she would have to double check how data was pulled from the EIA. From her point of view she is trying to figure out how to get Alaska on that same curve. And that is when a more competitive fiscal environment comes in to change the trend. BP will continue to drive efficiencies, but the state can choose to set a policy to drive an outcome of more oil and more investment.

CO-CHAIR PASKVAN said another way of looking at that chart is to hope for the unconventional oil extraction process to come to Alaska soon whether it's BP unconventional oil or shale or both.

MS. FITZPATRICK responded that they should also be hoping for more continued conventional light oil production, because there is an awful lot of that and basically, "You want it all." Meaningful tax change is something that will make a significant difference to start turning the trend the other way.

SENATOR WIELECHOWSKI asked how she would define "meaningful change."

MS. FITZPATRICK replied she would describe it as some of the key elements in HB 110 around lowering the progressivity; introducing brackets makes a significant difference in actually being able to understand, administer and plan for it. Taxing incremental profits at a higher rate is a much fairer mechanism as opposed to the current structure where as soon as the price goes up a dollar it goes all the way back to the start. That is what creates the uncompetitive aspect.

She said BP also thinks the base rate is too high; it's something that new entrants look at as well. A number of other aspects in the regulations - joint interest billings, interest rates, statute of limitations - aren't meaningful in the pure financial sense, but can make a big difference administratively.

CO-CHAIR PASKVAN noted that Senator Egan joined the meeting.

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MS. FITZPATRICK said it was time for Mr. Bilbao to take over and talk about the present and the future.

DAMIAN BILBAO, Head of Finance: Developments and Resources, BP Alaska, said he would share a little bit of what they would be doing in 2012 focusing on a couple specific technology items. It's the combination of efficiencies, technology and the correct fiscal environment that allows BP to progress these projects.

He said 2012 will be another busy year on the North Slope with on average of 6,000 employees and contractors. It is a year that will see a "significant level of activity," a record level of turnarounds, a new Northstar operating center, significant progress in safety systems and quite a bit of work around sustaining reserves to production efforts (five rigs going forward).

He said Prudhoe Bay has always been and continues being a great training ground for technical staff. This developing technology has allowed them to see a higher total recovery from Prudhoe Bay than ever anticipated. One example is the bright water technology, an enhanced oil recovery technique, the application of which will be doubled from 2011. Another example is a seismic acquisition plant at Milne Point in 2012.

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MR. BILBAO explained that BP's proposed (Milne Point) Simpson Lagoon Seismic Program will identify additional infield drilling opportunities, expand existing pads and leverage development of certain reservoirs in a different way than in the past.

CO-CHAIR PASKVAN asked him for a clearer idea of what a very mature field is compared to just a mature field, because he has heard that although some are 80 percent "water cut" they still have a lot of production left.

MR. BILBAO replied that some fields have been very well developed, but continue to offer significant opportunities even though they have moved past the initial stages of development.

SENATOR WIELECHOWSKI said he also wanted to hear his thoughts on gas-to-liquids potential at some point.

MR. BILBAO said he would be prepared to get that information and talk about it at another date. He agreed with Ms. Fitzpatrick that it's great to see new companies exploring on the North Slope, but to keep in mind that many of the remaining large-scale opportunities are found within areas that are already producing, one of them being the Sag River Reservoir on the west side of Prudhoe. It is an area where BP is working to understand some light oil opportunities. In a success case they are looking at a full scale development of over 180 wells and over 150 million barrels of resource. But what makes it challenging is that over 275 wells are already producing out of that reservoir. Slide 12 indicated locations for the (2012) wells that would extend for 1.5 miles through a reservoir that is no more than 20 feet thick. What makes it complex is that it's heavily faulted. So you might cross through a fault and outside of the reservoir and have to work back in. The technology would allow recovery from a lower number of well bores. The first pilot well has reached a depth of 6,700 feet and the folks back at the office are quite eager to learn more from it.

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CO-CHAIR PASKVAN said BP can deduct the qualified CAPEX in 2012 for Sag River even if it's on their operations elsewhere on the central North Slope. He asked him to more fully explain how the state will participate in those OPEX and CAPEX expenditures in 2012.

MR. BILBAO responded that the taxable base would be reduced by the amount of those expenditures and their payment would be determined on the remaining amount.

CO-CHAIR PASKVAN said they don't just deduct their operating expenditures; if they invest \$1 billion in capital expenditures, they can deduct 100 percent of the qualifying from the production tax.

MR. BILBAO replied that was correct to the best of his knowledge and he wasn't a tax expert.

CO-CHAIR PASKVAN said in addition to deducting 100 percent of the qualified capital expenditures, another 20 percent credit of the same dollar goes to the bottom line.

MR. BILBAO replied that was correct, but when they decide to go forward with a project they look at the investment profile for a full 20 to 30 years beyond the pilot program.

CO-CHAIR PASKVAN said they heard in an earlier meeting that one of the significant benefits Alaska provides (that other jurisdictions don't) is the forward funding that significantly increases a BP project's net present value.

MS. FITZPATRICK replied that in terms of calculating their taxable value, he was correct, but in looking at a project, she looks at the production profile that may last 10 or 20 years; she also looks at the total cash that will be generated from that first couple of years of upfront investment.

CO-CHAIR PASKVAN asked if it was fair to say that the state provides front end help to industry.

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MS. FITZPATRICK replied yes, and that all oil taxes in the oil industry around the world work the same way.

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MR. BILBAO said significant subsurface drilling challenges remain ahead of any at-scale development in the Sag reservoir and he realizes the state participates upfront, but ACES significantly impacts the long-term discounted cash flow particularly in a high price environment.

CO-CHAIR PASKVAN said the bi-partisan working group intends on looking at progressivity and how "high priced" is balanced in the context of economic and political discussions.

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SENATOR MCGUIRE said they recognize the proprietary challenge with revealing plans of development, but members still have questions about whether industry intends to develop more the progressivity rate is reduced. She couldn't emphasize enough that the committee needed to hear any information they can give about project economics and what a change to the progressivity rate at certain prices would mean to Alaska. "Take them into the board room so to speak..." and tell the committee how it will benefit Alaska, not just BP.

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MS. FITZPATRICK said she would see what can be done.

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CO-CHAIR WAGONER remarked that nobody has talked about the fact that it's unreasonable to want BP to spend all the money in Alaska that they make here. He also pointed out that from 1968 when oil was first discovered until 1977, the first date of production, the oil companies spent billions of dollars without putting a sheckle in their pocket. But he wanted to go back to her statement (referencing slide 8) that it would be nice if Alaska would look like the US onshore, and asked if there was any chance that they could even come close to getting there just with what's in Prudhoe Bay - without new technology to produce the viscous and heavy oils and new discoveries.

MS. FITZPATRICK replied that the status quo would not get them there; a lot can be done with conventional oil within Prudhoe Bay, but more would be needed for a dramatic change. Both are needed.

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MR. BILBAO said Alaska plays prominently in BP's global strategy. Getting more production comes back to a three-part equation: efficiency and technology that are in BP's control to progress and the fiscal environment that is in the state's control. The equation is similar for the Lower 48. At the end of the day, he said they will have to try to develop a balance of trust as these talks move forward. They must have dialogues in forums like this, and he said BP is fully prepared to do so.

CO-CHAIR PASKVAN asked if the 6.5 billion BOE is in the central North Slope region and what the boundaries are.

MR. BILBAO replied that is BP's net resource position in Alaska broken down by resource type or maturity: the proved resources

versus the opportunities in light and viscous oil, ultra-heavy oil and gas.

MS. FITZPATRICK added that it's all of their interest from Kuparuk across the North Slope.

CO-CHAIR PASKVAN clarified that it doesn't include ANWR, NPRA or the outer continental shelf no federal resources.

MS. FITZPATRICK said this purely represents BP's interest and they don't have things that are in the outer continental shelf yet.

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MR. BILBAO summarized that BP has a past of tremendous effort to get where they are now and that is the basis on which to build a strong future.

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CO-CHAIR PASKVAN said many Alaskans have heard the promise of \$5 billion in investment and many are concerned with the connection between investment and production. Assuming the \$5 billion investment in the next three to five years above the current CAPEX, he asked what increases above the FY11 or FY12 throughput industry can promise.

MS. FITZPATRICK replied that throughput wouldn't increase above the existing underlying decline. It would be on top of whatever the underlying decline is.

SENATOR FRENCH asked her to comment on the governor's goal of 1 million barrels more of production.

MS. FITZPATRICK said that increased production won't come just from existing fields on the North Slope, but she could get her production to flatten and start growing over time through the kind of projects they think are possible.

CO-CHAIR PASKVAN noted that state production taxes and royalties don't affect production from three miles off shore.

MS. FITZPATRICK remarked that the state legislature can influence what happens from a federal perspective. All of BP's assets are on state lands and therefore the state would get the most benefit.

SENATOR FRENCH asked if she could move just one aspect of the state's tax structure what it would be.

MS. FITZPATRICK answered progressivity.

SENATOR WIELECHOWSKI said the legislature's job is to do their due diligence and not push billions of dollars across the table without first insuring that this is really what they need to do. And he urged BP to tell them what fields they are going to invest in, specific projects and how they are going to move the needle by passing some major tax break.

CO-CHAIR PASKVAN thanked Ms. Fitzpatrick and held SB 192 in committee.

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CO-CHAIR PASKVAN and adjourned the Senate Resources Standing Committee meeting at 5:03 p.m.