

**ALASKA STATE LEGISLATURE
SENATE RESOURCES STANDING COMMITTEE**

April 19, 2012

3:34 p.m.

MEMBERS PRESENT

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

MEMBERS ABSENT

All members present

OTHER LEGISLATORS PRESENT

Senator Bettye Davis
Senator Joe Thomas
Senator Johnny Ellis
Senator Dennis Egan
Senator Cathy Giessel
Representative Beth Kerttula
Representative Berta Gardner

COMMITTEE CALENDAR

SENATE BILL NO. 3001

"An Act relating to adjustments to oil and gas production tax values based on a percentage of gross value at the point of production for oil and gas produced from leases or properties north of 68 degrees North latitude; relating to monthly installment payments of the oil and gas production tax; relating to the determinations of oil and gas production tax values; relating to oil and gas production tax credits including qualified capital credits for exploration, development, or production; making conforming amendments; and providing for an effective date."

- HEARD & HELD

PREVIOUS COMMITTEE ACTION

BILL: SB3001

SHORT TITLE: OIL AND GAS PRODUCTION TAX

SPONSOR(S): RULES BY REQUEST OF THE GOVERNOR

04/18/12 (S) READ THE FIRST TIME - REFERRALS
04/18/12 (S) RES, FIN
04/19/12 (S) RES AT 3:30 PM SENATE FINANCE 532

WITNESS REGISTER

BRYAN BUTCHER, Commissioner
Department of Revenue
Juneau, Alaska

POSITION STATEMENT: Introduced SB 3001 on behalf of Governor Parnell.

BRUCE TANGEMAN, Deputy Commissioner
Department of Revenue
Juneau, Alaska

POSITION STATEMENT: Provided information during the discussion of SB 3001.

ACTION NARRATIVE

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CO-CHAIR JOE PASKVAN called the Senate Resources Standing Committee meeting to order at 3:34 p.m. Present at the call to order were Senators French, Stedman, Stevens, McGuire, Wielechowski, Co-Chair Wagoner, and Co-Chair Wagoner.

SB 3001-OIL AND GAS PRODUCTION TAX

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CO-CHAIR PASKVAN announced that the first order of business would be a presentation by the Department of Revenue, Commissioner Bryan Butcher, who would introduce SB 3001 and the fiscal note. He said that the bill was introduced at the request of the governor. He noted that yesterday he had made a request for modeling or analysis or evaluation of the bill, and that the committee had only recently received today's presentation.

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BRYAN BUTCHER, Commissioner, Department of Revenue (DOR), apologized for the lateness in providing the presentation. He began by stating the goals of the bill: to incentivize production on the North Slope, both within and outside existing

units; to generate additional jobs and activity for the Alaska economy, to build on work already undertaken in legislative committees during the regular session, to maintain existing structure of ACES, with slight modifications, and to maintain alignment of working interest owners by not tying incentives to individual companies to fields as a whole.

COMMISSIONER BUTCHER addressed the five key provisions of the bill. He termed it a hybrid bill. The first provision is a 30 percent gross revenue exclusion for calculating base tax and progressive tax for qualifying new North Slope fields. He said that language is identical to the language the Senate had in HB 276. The second provision is a 40 percent gross revenue exclusion for calculating progressive tax for other North Slope fields. That is the tax structure taken from the new fields in HB 276 and applied to the rest of the North Slope.

CO-CHAIR PASKVAN asked if there was an advisor, economic or otherwise, that DOR has relied upon to determine the rate for existing fields.

COMMISSIONER BUTCHER said no. The work that has been done has been between the governor and DOR.

CO-CHAIR PASKVAN asked if there will be an economic advisor to present information to the committee.

COMMISSIONER BUTCHER replied that there may be, depending on the topic. He explained that a lot of the department's understanding of these provisions is as a result of discussions with the Senate's consultant, PFC Energy.

CO-CHAIR PASKVAN concluded that the administration does not have an economic advisor to present components of the bill to the committee.

COMMISSIONER BUTCHER reiterated that it depends on the topic. The Department of Revenue will speak to most of the bill.

CO-CHAIR PASKVAN asked who the advisor would be.

COMMISSIONER BUTCHER said it would be Gaffney, Cline and Associates.

CO-CHAIR PASKVAN asked if Gaffney, Cline could be made available to the Senate Resources Committee.

COMMISSION BUTCHER thought it might be a possibility.

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SENATOR FRENCH asked if DOR has had access to the PFC Model.

COMMISSIONER BUTCHER said they had.

SENATOR FRENCH asked if DOR was able to put their calculations into the PFC Model.

COMMISSIONER BUTCHER said yes.

SENATOR FRENCH asked which members of the legislature have that model.

COMMISSIONER BUTCHER did not know.

SENATOR FRENCH repeated the question regarding if DOR has access to the PFC Model.

COMMISSIONER BUTCHER said yes.

SENATOR STEDMAN commented that PFC Energy is the consultant to Legislative Budget and Audit and was the consultant hired by the legislature. It is common for the consultants of the legislature to work with the administration and with industry on what data goes into their models and what comes out for the purpose of policy discussions. However, he stated that he was confused on the interaction between the administration and PFC Energy on this bill. He requested clarification about the type of interaction the administration had with PFC Energy. He asked if PFC modeled SB 3001 for the administration.

COMMISSIONER BUTCHER explained that PFC Energy has not run any models for DOR. They just provided information for DOR's economists so the outputs would be the same.

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BRUCE TANGEMAN, Deputy Commissioner, Department of Revenue, provided information on the process of making the model. He added that it was not DOR's intent to present PFC's model, but rather to align input and output of the models. PFC and DOR will each be presenting their models.

SENATOR STEDMAN said that was a little bit different than what he had heard earlier. He said he understood the process of sharing data. He wanted to know what interaction the legislative

consultants have had with the administration on the credit issues.

COMMISSIONER BUTCHER said there has been no interaction between PFC and the Department of Revenue when crafting the bill. He explained how the provisions were developed. He listed various ways a more meaningful tax reduction could be attained. He said HB 110 was the administration's attempt to do so, but it was not the only way.

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CO-CHAIR PASKVAN asked if it was a fair statement to say that no economic advisor has provided information to DOR in determining the 40 percent allowance.

COMMISSIONER BUTCHER said the economists in DOR provided that determination.

CO-CHAIR PASKVAN asked what government take the administration believes is a reasonable range for existing fields.

COMMISSIONER BUTCHER explained that the presentation would show that. The amount is in the general vicinity of HB 110's numbers and was a result of work done by DOR along with the governor's office.

CO-CHAIR PASKVAN asked if any advisor has advised the administration about what a reasonable range for government take is for existing fields.

COMMISSIONER BUTCHER listed a number of consultants, such as Pedro Van Meurs, Gaffney & Cline, and others, as well as the legislature's consultants, Mr. Marks, Mr. Dickinson, and PFC Energy. He stated that no one consultant made that determination.

CO-CHAIR PASKVAN asked if the administration believes that a 70 percent to 75 percent government take, including state and federal, is a reasonable range for existing fields.

COMMISSIONER BUTCHER explained that it was in the general area of one-third each.

CO-CHAIR PASKVAN requested a yes or no answer.

COMMISSIONER BUTCHER replied that there is no "yes or no answer" unless the dollar amount is known. He gave an example 70 percent

to 75 percent government take at \$200 oil and pointed out that is is considerably different than at \$60 oil.

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CHAIR WIELECHOWSKI asked about a legislative contract with PFC Energy for \$750,000, which was supposed to provide a model. He questioned if such a model had been provided.

COMMISSIONER BUTCHER replied that he was not aware if PFC had made that available to the legislature.

CHAIR WIELECHOWSKI asked who the consultant was for SB 3001.

COMMISSIONER BUTCHER replied that different pieces of the bill required different consultants. He gave as an example provision four, extending the 40 percent well lease expenditure credit to the North Slope, which was developed prior to the 2010 legislative session. He did not know who the consultant was.

CHAIR WIELECHOWSKI asked if Commissioner Butcher had consulted with the oil industry to see if they would support the bill.

COMMISSIONER BUTCHER reported that the department had not talked to any individual companies.

CO-CHAIR PASKVAN asked if DOR had the PFC Energy model in hand.

COMMISSIONER BUTCHER did not know. He added that the department did have a version of the PFC model that was run for validation.

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SENATOR FRENCH stated that he was extremely unhappy that the department had received the model before the Senate did. He protested that the consultant the legislature hired provided information to the department first.

COMMISSIONER BUTCHER responded that he had not seen the model. He explained that the department took what the Senate prepared regarding new fields and used it to run the model.

CHAIR WIELECHOWSKI said he was extremely disappointed with PFC Energy and had lost confidence in its ability to advise the legislature.

CO-CHAIR PASKVAN turned to the advice from Pedro Van Meurs regarding reasonable government take, in the range of 75

percent, for existing fields. He asked if the department was accepting or rejecting that advice.

COMMISSIONER BUTCHER said he disagreed with that advice.

CO-CHAIR PASKVAN asked how much he disagreed.

COMMISSIONER BUTCHER offered to provide that breakdown but stated that there was no magic percent. He gave an example of a consultant in Albert giving advice on changing their version of ACES.

CO-CHAIR PASKVAN asked if any consultant had advised the department that 70 percent to 75 percent is not reasonable. He emphasized that the legislature's consultant maintained that it was a reasonable rate.

COMMISSIONER BUTCHER replied that most of the advisors, including presentations by PFC Energy, have shown Alaska to be among the highest tax regimes in North America and in the world. He maintained that that designation was playing a major role in Alaska's not receiving major investment. He said that Russia has worked to reduce their extraction and export taxes to a level below Alaska's taxes, and hoped to receive up to \$500 billion in investments as a result.

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SENATOR STEDMAN commented that the state's ranking globally changes when the price of oil changes. The fiscal terms that the state operates under are only half of the equation; the other half is the prospectivity of the basin - how much oil resource is available. He maintained that it is more complex than saying Alaska is one of the highest tax regimes in the organized, economically developed countries.

CO-CHAIR PASKVAN reiterated the question regarding if any consultant has said that 70 percent to 75 percent government take in existing fields is unreasonable.

MR. TANGEMAN opined that the number the department should focus on is the number that brings more investment to the state. He referred to capital investment in 2010 to 2012 and pointed to a downward trend.

CO-CHAIR PASKVAN argued that the charts the department has prepared regarding capital expenditures show an increase through 2016. He asked Commissioner Butcher if that was correct.

COMMISSIONER BUTCHER replied that it is as accurate as a forecast can be.

CO-CHAIR PASKVAN said those numbers had been relied upon by the department in recent presentations.

COMMISSIONER BUTCHER said that was correct.

SENATOR FRENCH brought up the issue of the legislature not having access to capital investment numbers by the industry. He asked if the department has access to those confidential numbers.

COMMISSIONER BUTCHER said no.

SENATOR FRENCH asked if Commissioner Butcher ever worried that the state might be getting "squeezed by the industry with respect to investment."

COMMISSIONER BUTCHER agreed that was a concern, but that every factor must be weighed.

SENATOR FRENCH restated the question to ask whether it's possible that the industry would look at their capital expenditures from last year and decide to spend less in order to benefit from a big tax break.

COMMISSIONER BUTCHER did not think there was a conspiracy among oil companies to do something like that.

SENATOR FRENCH said he did was not suggesting a conspiracy. He restated his question to ask if one company might reduce its capital expenditures in order to convince the state to lower taxes.

COMMISSIONER BUTCHER said he could not imagine an oil company doing that.

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SENATOR FRENCH reported that BP did under invest in their flow lines to the point of a criminal offense, so it is known that oil companies will under invest from time to time. He read an email from a retired North Slope worker which said that it was absurd to think that the oil companies are going to do anything other than what they have already planned, regardless of the tax rates. He reported being in meetings where the oil companies

have come very close to admitting that they are currently bluffing for better tax treatment.

COMMISSIONER BUTCHER related that he did not have any inside information.

MR. TANGEMAN added that he could not imagine a situation where that discussion could take place, due to shareholder oversight.

SENATOR STEDMAN expressed frustration and recalled a discussion by the department on capital expenditures. The department reported capital expenditure decline when it was, in fact, increasing. He maintained that the same thing is happening today and it is hard to return to "re-plow old ground." He said the legislature should be able to rely on the information presented by DOR. He stated he was "gun shy."

CO-CHAIR PASKVAN agreed with Senator Stedman. He stated that it is startling to receive information again that directly contradicts other statements from the department.

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MR. TANGEMAN explained that the department did present numbers that show an incline in capital expenditures for FY 2010 - FY 2012.

CO-CHAIR PASKVAN asked if there was disagreement within DOR regarding those numbers.

MR. TANGEMAN said absolutely not.

SENATOR STEDMAN inquired if the discussion today is that capital expenditures are going to decline.

MR. TANGEMAN referred to FY 2010 - FY 2012 and said the department provided charts that show an increase in capital expenditures in the forecast. The production forecast shows 50 percent of oil produced will be from new oil.

SENATOR STEDMAN pointed out that the forecast for FY 2015 is \$3.890 billion and it is currently at \$3 billion. He voiced concern about sound bites by some legislators that are opposite of this forecast. He inquired if forecast numbers were submitted twice a year to the department.

MR. TANGEMAN reported on a fall forecast and a spring forecast by DOR.

SENATOR STEDMAN recalled testimony from the industry that they were comfortable with their forecasts and expenditures delivered to the department, after the question was asked of the industry whether or not there was a directional change between when the information was submitted to the department and a month ago.

SENATOR WIELECHOWSKI shared in that recollection. He understood that capital expenditures have increased to record highs every year since ACES was instigated. If that is not true, he said he wanted to know where the decline has been and what fields have been projected to increase, but didn't, and what projects have been projected to increase, but didn't. He requested an economic analysis of each decline, because companies have a duty to produce under the terms of their leases.

MR. TANGEMAN said Senator Wielechowski was correct in that the companies have a duty to produce; however, there is a difference between duty to produce and duty to invest. The department is looking for additional investment in order to increase production. There are incredible investments going on outside of Alaska, which is capital the department will go after by lowering taxes. The department wants companies to exceed their duty to produce by making a more favorable investment climate in the state by lowering taxes.

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SENATOR WIELECHOWSKI disagreed that the duty to produce and duty to invest are different. He maintained that the administration's belief that companies do not have a duty to invest is doing the state a disservice and putting it at risk. He opined that it was not legally accurate. He also wanted to know of any project or field that is not economic under ACES and that would become economic under SB 3001.

COMMISSIONER BUTCHER said those are questions best asked to individual companies. He hoped the companies could provide their insight on the bill.

SENATOR WIELECHOWSKI pointed out that the duty to manage Alaska's resource belongs to the state of Alaska, and it's not up to the industry to determine what is economic, it's the state's job and the department needs to figure it out. The state can't push billions of dollars across the table without having any idea if projects are economic or not. If projects are economic, there is an obligation to produce and to develop. That

determination should not be left up to the oil industry, because that would be turning the state's sovereignty over to them.

COMMISSIONER BUTCHER maintained that DOR does not have that information; the Department of Natural Resources and the companies would have information about what is economic or not.

SENATOR STEDMAN noted previously during similarly-related major legislation, the administration had consultants to provide an economic analysis on different field sizes. He asked if that would be done for this bill regarding the legacy fields. He suggested that Gaffney Cline had done that in the past and had provided an updated analysis during the regular legislative session, including capital costs, current oil prices, and net present values.

COMMISSIONER BUTCHER replied that the department would be happy to do that.

CO-CHAIR PASKVAN asked who would be the advisor to do so.

COMMISSIONER BUTCHER reported that it would be the department and Gaffney Cline, depending on the issue.

CO-CHAIR PASKVAN suggested that the administration has no intention of providing an advisor to the committee for economic information.

COMMISSIONER BUTCHER offered to do that.

CO-CHAIR PASKVAN asked if the 30 percent exemption for new fields was reasonable.

COMMISSIONER BUTCHER said yes.

CO-CHAIR PASKVAN described those who would be exempted as the areas outside the legacy fields that don't have roads or pipelines or treatment facilities.

COMMISSIONER BUTCHER agreed.

CO-CHAIR PASKVAN asked why there would be a greater exemption for the legacy fields rather than those without infrastructure.

COMMISSIONER BUTCHER clarified that there is a lesser exemption for legacy fields.

MR. TANGEMAN explained how the exemptions were applied. The 30 percent exemption is applied to the base rate and the progressivity rate, whereas the 40 percent exemption is applied only to the progressivity rate.

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CO-CHAIR PASKVAN noted that the governor's letter had no fiscal impact at \$110 per barrel in FY 12 and FY 13. He pointed out a negative fiscal impact to the state of about a \$1.5 billion at \$110 per barrel in the bill.

MR. TANGEMAN replied that under the scenario if SB 3001 were to pass and no new production was brought on line, the fiscal impact would be a negative \$1.5 billion. That figure was based on the Revenue Sources Book forecast. He restated the governor's goal, which is to make a meaningful change to the tax regime in order to spur investment.

SENATOR FRENCH recalled the first Resource Committee hearing of the session when he pointed out that it was hard to change oil taxes. He asked if Commissioner Butcher agreed.

COMMISSIONER BUTCHER agreed.

SENATOR FRENCH suggested that it is far harder to raise taxes than it is to lower them. He opined that it was unlikely that oil taxes would be lowered in the face of industry inaction. He asked why oil companies didn't have to earn the tax break. He related that the state has been involved in the oil industry since before statehood. He suggested that the state and the oil industry become partners with mutually enforceable obligations.

COMMISSIONER BUTCHER opined that if taxes are lowered and the oil companies don't do what they say they are going to do, it will be far easier to raise taxes than it would be under normal circumstances. He suggested that current taxes are high.

CO-CHAIR PASKVAN asked if the commissioner knew the existing fields' net present value, internal rates of return, and other core financial information under SB 3001.

COMMISSIONER BUTCHER said he did not know that information.

CO-CHAIR PASKVAN asked if that was important information to have before considering a tax change.

COMMISSIONER BUTCHER said it was.

CO-CHAIR PASKVAN asked why the administration's consultants are not providing that information. He suggested it was DOR's responsibility to provide that information.

COMMISSIONER BUTCHER related this was the first chance DOR has had to present to the committee since 2011. He offered to work with the committee on providing that information. He noted that the DOR's economists agree, in general, with what the legislature's consultants have been saying.

SENATOR WIELECHOWSKI discussed a model from Gaffney Cline that the administration used during ACES which showed at \$80 per barrel in Prudhoe Bay, assuming CAPEX increases at 300 percent, an internal rate of return of 123 percent. He wondered if the legislature could have copy of that model.

COMMISSIONER BUTCHER said he would check and see.

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SENATOR STEDMAN provided an estimation for FY 2013 of gross stock just under \$23 billion in the "oil patch," with costs of about \$7.5 billion, and royalties of about \$3 billion, yielding a total of \$11 billion. He suggested when discussing economic starvation it be thought of "in scale." He maintained there is a difference between existing production and incremental production in the legacy fields.

He requested an economic analysis by the administration of incremental production, capital costs being at risk under the current tax structure, and how the tax structure would need to change in order to get incremental production up. He opined that would be an easier discussion than dealing with legacy fields that will continue to produce regardless of what the legislature does. He reminded the committee that previous testimony from Exxon stated that they would do in-field drilling in the legacy fields because it is profitable, regardless of what the legislature does. He suggested separating the two discussions.

COMMISSIONER BUTCHER stressed the he was not suggesting that companies were experiencing economic starvation, rather that the administration was looking for ways to make the economics for marginal fields and in-field fields, more economic and leave less oil in the ground.

MR. TANGEMAN addressed Senator Wielechowski's comment on modeling during the ACES discussion that showed certain fields

economic at \$60 or \$80. He pointed out that oil is \$60 higher now and there are more fields that are economic, but he questioned if they were competitive. He debated Senator Wielechowski's comment that "it is the state's job to set the rate." He questioned what the economic threshold was, and stressed the importance of Alaska's having a competitive rate.

SENATOR STEDMAN maintained that the rate depends on the price of oil or the economic environment. He stated that the conversation must be cognizant of the public's interest and how they perceive this issue. It is more accurate to say that the state has a fiscal system that is extremely "elastic" and as oil prices advance, it puts Alaska at a competitive disadvantage. The question is "at what point does the adjustment need to be made."

COMMISSIONER BUTCHER agreed. High oil prices were not expected when ACES was implemented.

CO-CHAIR PASKVAN asked if there is a target internal rate of return that the administration is trying to achieve.

COMMISSIONER BUTCHER said no. The administration is focusing on what would make Alaska more competitive. Even with the passage of SB 3001, Alaska would still be among the most expensive producing countries. Companies reported that HB 110 would have made a difference and resulted in billions of dollars more in investment. The administration is aiming for a tax level that is more reasonable and meaningful and would bring more investment.

CO-CHAIR PASKVAN asked what the current internal rate of return is for production.

MR. TANGEMAN asked if Co-Chair Paskvan meant actual rate of return. If so, he said it would be company specific and the administration is not privy to that kind of information.

CO-CHAIR PASKVAN restated his question to say, "With respect to existing production, are you trying to achieve a greater internal rate of return than currently exists."

COMMISSIONER BUTCHER replied that lower taxes would result in an improved internal rate of return.

MR. TANGEMAN shared an example of Russia's plan for \$500 billion of investment due to a lower tax rate and an improved internal rate of return.

CO-CHAIR PASKVAN questioned how the department would know that lower taxes would result in an improved internal rate of return if they were not privy to what the current internal rate of return is.

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SENATOR FRENCH said he had the same rhetorical question. He noted there were also problems in Russia, like forced takeovers as experienced by ConocoPhillips. He gave another example of companies having their assets nationalized in Argentina.

He pointed out that the focus should be on the numbers in Alaska. He wondered why the state does not yet know companies' internal rates of return. Internationally recognized tax attorneys have suggested that the state have access to those numbers before making tax decisions. He suggested obtaining a subpoena to find out those numbers.

COMMISSIONER BUTCHER said that is proprietary information and he was not aware of any state having access to companies' internal books. He suggested it would not be "business friendly" to force companies to open their books.

SENATOR FRENCH disagreed. He stated that it does not make Alaska un-business friendly, but rather a partner. He suggested that DOR might want to have access to that information before it comes to the legislature to suggest a change in taxes.

COMMISSIONER BUTCHER countered that Senator French used the word "subpoena," not "ask."

SENATOR FRENCH inquired if DOR had asked for the information.

COMMISSIONER BUTCHER replied that DOR has not asked for proprietary information.

SENATOR FRENCH suggested DOR try asking.

MR. TANGEMAN wondered if that question was asked during the ACES debate, which lasted only three-and-a-half weeks. He pointed out that taxes can be changed in a short amount of time. He concluded that tax changes were made without that information.

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SENATOR FRENCH asked if Mr. Tangeman had reviewed the transcripts from ACES.

MR. TANGEMAN said not all of them.

SENATOR FRENCH encouraged Mr. Tangeman to do so. He reported that the legislature had a consultant who used every piece of public information available to build a model which was presented to the oil industry to analyze, with the invitation to come back to the legislature if there something that was inaccurate. The oil companies never came back because the model was not inaccurate. He emphasized that the legislature did as much homework as possible in open session, without issuing a subpoena, with an invitation to the companies to correct errors in the model.

SENATOR STEDMAN added that the Senate spent some time dealing with this issue during the regular legislative session and came out with a targeted rate for new oil and changes to ACES to try to fix some of the structural problems. There was not enough political support for that work. At the end of the session the Senate came up with a structure that would leave ACES intact, but deliver an economic adjustment for new oil. Two options were considered, one of which was removing progressivity. The consultants provided a better way of doing that in the form of an exclusion allowance for new oil that would not create cost allocation issues and reduce government take. He described the process the Senate went through to arrive at their conclusions.

He asked how DOR arrived at SB 3001. He stated that the bill contains cash flow projections in FY 13 found in HB 110 at \$1.5 billion at \$110 per barrel oil. He inquired if DOR "backed into that to get to that number or was there another methodology that created it."

COMMISSIONER BUTCHER agreed that it was close to HB 110; a couple hundred million different. He explained that DOR took the structure the Senate worked on for the new fields and began working on it internally for the existing fields.

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SENATOR WIELECHOWSKI related the economic analysis done during ACES consisting of seven hypothetical fields with internal rates of return, net present value, satellite fields, legacy fields, and heavy oil. He discussed the model created by Gaffney Cline, as well as presentations by Roger Marks, Dan Dickenson, and the oil industry, all of which were made public. He suggested using that model to determine information about legacy fields.

He recalled a conference call last year by ConocoPhillips where the company said they were investing hundreds of millions of dollars in Alaska all at "very good rates of return" and Alaska offered "strong cash margins." He inquired if Commissioner Butcher thought those statements were inaccurate.

COMMISSIONER BUTCHER replied that ConocoPhillips could provide that information.

SENATOR WIELECHOWSKI asked if the commissioner disagreed with ConocoPhillips' statement that they are investing hundreds of millions in Alaska at very good rates of return last year.

COMMISSIONER BUTCHER said he did not know the details. He maintained that the company has said that a tax change will result in billions of dollars more investment than they currently are investing in Alaska.

CHAIR WIELECHOWSKI asked if his previous statement showed ConocoPhillips' support for a tax break.

COMMISSIONER BUTCHER reiterated that it would involve talking to the companies themselves to find out.

MR. TANGEMAN pointed out that Alaska is only one part of ConocoPhillips' portfolio. He returned to the discussion of the Gaffney Cline model used during ACES and commented that it was a very good model; however, it was based on theory and assumptions. He suggested when looking at what has occurred since then, the numbers used were not positive enough.

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CO-CHAIR PASKVAN asked if the information DOR is presenting to support SB 3001 is superior to information used to support ACES.

COMMISSIONER BUTCHER predicted that if DOR has a month to lay out information it would contain equal detail.

CO-CHAIR PASKVAN asked if the commissioner believed it was possible to have a high internal rate of return with the current tax structure, with respect to the existing fields.

COMMISSIONER BUTCHER said yes.

MR. TANGEMAN asked what Co-Chair Paskvan would consider a high rate of return.

CO-CHAIR PASKVAN noted that Commissioner Butcher's answer was "yes." However, he previously stated he did not know what the internal rate of returns was.

SENATOR STEDMAN pointed out that the effects of the mechanics in the bill are different than what the Senate expected on incremental oil. The mechanics used with legacy fields don't work with incremental oil. He requested a sensitivity analysis run on the 40 percent exclusion as it drops to zero. He questioned how rapidly \$1.5 billion, the negative number, approaches zero. The Senate spent a lot of time trying to hold current production cash flow change at zero, at \$100 oil, on the recommendation of one of the consultants.

CO-CHAIR PASKVAN asked about page three of the fiscal note, the columns that address the "forecast plus 10 percent." He inquired where the 10 percent comes from - existing, new, or federal fields.

MR. TANGEMAN reported that the tables are based on hypothetical numbers. The analysis was done last year and was based on certain types of fields coming on line.

CO-CHAIR PASKVAN asked if the top chart on 10 percent is from existing fields.

MR. TANGEMAN replied that it is just 10 percent above the forecast by the department. It is just more oil in the pipeline.

CO-CHAIR PASKVAN asked if any of this is for new fields.

MR. TANGEMAN said the department does not make projections on new fields.

CO-CHAIR PASKVAN assumed then that there can be a 10 percent increase above current production on existing fields. He voiced concern that the director of the Division of Oil and Gas testified less than a year ago to the U.S. Senate that "the natural field declines cannot be replaced without access to production from federal lands in the OCS. There are no known conventional sources on state or native lands that are likely sufficient to replace the decline in the existing production rates." He asked who was right.

MR. TANGEMAN replied that the NPRA could be factored into the 10 percent.

CO-CHAIR PASKVAN clarified that if production is increased 50,000 to 60,000 barrels a day for an entire year the state still receives \$400 million less in revenue.

MR. TANGEMAN said that is correct due to the generous tax credit system.

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CO-CHAIR PASKVAN requested that the chart be shown, in dollar terms and in volumes, the difference between the current tax system and the proposed tax system.

MR. TANGEMAN restated the request.

CO-CHAIR PASKVAN clarified the request.

MR. TANGEMAN said he would run the numbers and get back to the committee.

SENATOR STEDMAN related that it has been said that there are \$5 billion worth of projects that the industry would go forward with if the tax was changed for the legacy fields. He shared that there was testimony from Exxon about what it would take to stem the decline of their fields. He requested to know what the department's estimate is on what it would take in dollars of capital investment per year to stem the decline.

COMMISSIONER BUTCHER said it was a difficult question to answer because the department doesn't have that information. He said he would talk to DNR.

SENATOR STEDMAN recalled testimony from Mr. Pittman from Exxon which gave the committee a feel for the magnitude of what it would take to stem the decline, roughly \$3 billion to \$5 billion a year; not \$5 billion over 8 years, but a larger number. He questioned what the break even analysis would be and what was in the best interest for the state of Alaska.

COMMISSIONER BUTCHER agreed that more investment would be needed.

[5:01:07 PM](#)

SENATOR WIELECHOWSKI asked the administration to address provision 4 on page 4 of the fiscal note. He suggested the \$400 million loss in FY 13 and a \$400 million gain in FY 14 should probably be changed to zero. Also, in provision number 5, the loss of between \$200 million and \$400 million should be changed

to show an increase every year reflecting the yearly CAPEX increase.

CO-CHAIR PASKVAN concluded that it was important for the committee to find out when they will be hearing from an advisor to the administration in order to find out information about internal rates of return, net present values, reasonable ranges of government take, and opinions on investments needed. He said he was not interested in myths of declining production, capital expenditures, and employment numbers.

[SB 3001 was held in committee.]

[5:03:10 PM](#)

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