

**ALASKA STATE LEGISLATURE  
HOUSE RESOURCES STANDING COMMITTEE**

March 26, 2013

6:07 p.m.

**MEMBERS PRESENT**

Representative Eric Feige, Co-Chair  
Representative Dan Saddler, Co-Chair  
Representative Peggy Wilson, Vice Chair  
Representative Mike Hawker  
Representative Craig Johnson  
Representative Kurt Olson  
Representative Paul Seaton  
Representative Geran Tarr  
Representative Chris Tuck

**MEMBERS ABSENT**

All members present

**COMMITTEE CALENDAR**

COMMITTEE SUBSTITUTE FOR SENATE BILL NO. 21(FIN) AM(EFD FLD)

"An Act relating to the interest rate applicable to certain amounts due for fees, taxes, and payments made and property delivered to the Department of Revenue; providing a tax credit against the corporation income tax for qualified oil and gas service industry expenditures; relating to the oil and gas production tax rate; relating to gas used in the state; relating to monthly installment payments of the oil and gas production tax; relating to oil and gas production tax credits for certain losses and expenditures; relating to oil and gas production tax credit certificates; relating to nontransferable tax credits based on production; relating to the oil and gas tax credit fund; relating to annual statements by producers and explorers; establishing the Oil and Gas Competitiveness Review Board; and making conforming amendments."

- HEARD & HELD

**PREVIOUS COMMITTEE ACTION**

BILL: SB 21

SHORT TITLE: OIL AND GAS PRODUCTION TAX

SPONSOR(S): RULES BY REQUEST OF THE GOVERNOR

01/16/13 (S) READ THE FIRST TIME - REFERRALS  
01/16/13 (S) TTP, RES, FIN  
01/22/13 (S) TTP AT 3:30 PM BELTZ 105 (TSBldg)  
01/22/13 (S) Heard & Held  
01/22/13 (S) MINUTE(TTP)  
01/24/13 (S) TTP AT 3:30 PM BUTROVICH 205  
01/24/13 (S) Heard & Held  
01/24/13 (S) MINUTE(TTP)  
01/29/13 (S) TTP AT 3:30 PM BELTZ 105 (TSBldg)  
01/29/13 (S) Heard & Held  
01/29/13 (S) MINUTE(TTP)  
01/31/13 (S) TTP AT 1:00 PM BUTROVICH 205  
01/31/13 (S) Heard & Held  
01/31/13 (S) MINUTE(TTP)  
02/05/13 (S) TTP AT 3:30 PM BUTROVICH 205  
02/05/13 (S) Heard & Held  
02/05/13 (S) MINUTE(TTP)  
02/07/13 (S) TTP AT 3:30 PM BUTROVICH 205  
02/07/13 (S) Moved SB 21 Out of Committee  
02/07/13 (S) MINUTE(TTP)  
02/08/13 (S) TTP RPT 1NR 4AM  
02/08/13 (S) NR: DUNLEAVY  
02/08/13 (S) AM: MICCICHE, GARDNER, FAIRCLOUGH,  
MCGUIRE  
02/08/13 (S) LETTER OF INTENT WITH TTP REPORT  
02/09/13 (S) TTP AT 10:00 AM BUTROVICH 205  
02/09/13 (S) -- MEETING CANCELED --  
02/11/13 (S) RES AT 3:30 PM BUTROVICH 205  
02/11/13 (S) Heard & Held  
02/11/13 (S) MINUTE(RES)  
02/13/13 (S) RES AT 3:30 PM BUTROVICH 205  
02/13/13 (S) Heard & Held  
02/13/13 (S) MINUTE(RES)  
02/15/13 (S) RES AT 3:30 PM BUTROVICH 205  
02/15/13 (S) Heard & Held  
02/15/13 (S) MINUTE(RES)  
02/18/13 (S) RES AT 3:30 PM BUTROVICH 205  
02/18/13 (S) Heard & Held  
02/18/13 (S) MINUTE(RES)  
02/20/13 (S) RES AT 3:30 PM BUTROVICH 205  
02/20/13 (S) Heard & Held  
02/20/13 (S) MINUTE(RES)  
02/22/13 (S) RES AT 3:30 PM BUTROVICH 205  
02/22/13 (S) Heard & Held  
02/22/13 (S) MINUTE(RES)  
02/25/13 (S) RES AT 3:30 PM BUTROVICH 205  
02/25/13 (S) Heard & Held

02/25/13 (S) MINUTE(RES)  
02/27/13 (S) RES AT 3:30 PM BUTROVICH 205  
02/27/13 (S) Moved CSSB 21(RES) Out of Committee  
02/27/13 (S) MINUTE(RES)  
02/28/13 (S) RES RPT CS 3DP 1DNP 2NR 1AM NEW  
TITLE  
02/28/13 (S) LETTER OF INTENT WITH RES REPORT  
02/28/13 (S) DP: GIESSEL, MCGUIRE, DYSON  
02/28/13 (S) DNP: FRENCH  
02/28/13 (S) NR: MICCICHE, BISHOP  
02/28/13 (S) AM: FAIRCLOUGH  
02/28/13 (S) FIN AT 9:00 AM SENATE FINANCE 532  
02/28/13 (S) Heard & Held  
02/28/13 (S) MINUTE(FIN)  
03/01/13 (S) FIN AT 9:00 AM SENATE FINANCE 532  
03/01/13 (S) Heard & Held  
03/01/13 (S) MINUTE(FIN)  
03/01/13 (S) RES AT 3:30 PM BUTROVICH 205  
03/01/13 (S) -- MEETING CANCELED --  
03/02/13 (S) RES AT 10:00 AM BUTROVICH 205  
03/02/13 (S) -- MEETING CANCELED --  
03/04/13 (S) FIN AT 9:00 AM SENATE FINANCE 532  
03/04/13 (S) Heard & Held  
03/04/13 (S) MINUTE(FIN)  
03/04/13 (S) FIN AT 1:30 PM SENATE FINANCE 532  
03/04/13 (S) Heard & Held  
03/04/13 (S) MINUTE(FIN)  
03/05/13 (S) FIN AT 9:00 AM SENATE FINANCE 532  
03/05/13 (S) Heard & Held  
03/05/13 (S) MINUTE(FIN)  
03/05/13 (S) FIN AT 1:30 PM SENATE FINANCE 532  
03/05/13 (S) Heard & Held  
03/05/13 (S) MINUTE(FIN)  
03/06/13 (S) FIN AT 9:00 AM SENATE FINANCE 532  
03/06/13 (S) Heard & Held  
03/06/13 (S) MINUTE(FIN)  
03/06/13 (S) FIN AT 1:30 PM SENATE FINANCE 532  
03/06/13 (S) Heard & Held  
03/06/13 (S) MINUTE(FIN)  
03/06/13 (S) FIN AT 3:00 PM SENATE FINANCE 532  
03/06/13 (S) -- Public Testimony --  
03/11/13 (S) FIN AT 9:00 AM SENATE FINANCE 532  
03/11/13 (S) -- MEETING CANCELED --  
03/11/13 (S) FIN AT 1:30 PM SENATE FINANCE 532  
03/11/13 (S) -- MEETING CANCELED --  
03/12/13 (S) FIN AT 9:00 AM SENATE FINANCE 532  
03/12/13 (S) Bills Previously Heard/Scheduled

03/12/13 (S) FIN AT 1:30 PM SENATE FINANCE 532  
 03/12/13 (S) Heard & Held  
 03/12/13 (S) MINUTE(FIN)  
 03/12/13 (S) FIN AT 4:00 PM SENATE FINANCE 532  
 03/12/13 (S) Heard & Held  
 03/12/13 (S) MINUTE(FIN)  
 03/13/13 (S) FIN AT 9:00 AM SENATE FINANCE 532  
 03/13/13 (S) Heard & Held  
 03/13/13 (S) MINUTE(FIN)  
 03/13/13 (S) FIN AT 1:30 PM SENATE FINANCE 532  
 03/13/13 (S) Heard & Held  
 03/13/13 (S) MINUTE(FIN)  
 03/14/13 (S) FIN AT 9:00 AM SENATE FINANCE 532  
 03/14/13 (S) Moved CSSB 21(FIN) Out of Committee  
 03/14/13 (S) MINUTE(FIN)  
 03/18/13 (S) FIN RPT CS 2DP 1DNP 1NR 3AM NEW  
 TITLE  
 03/18/13 (S) DP: KELLY, MEYER  
 03/18/13 (S) DNP: HOFFMAN  
 03/18/13 (S) NR: FAIRCLOUGH  
 03/18/13 (S) AM: DUNLEAVY, BISHOP, OLSON  
 03/18/13 (H) RES AT 1:00 PM BARNES 124  
 03/18/13 (H) Scheduled But Not Heard  
 03/19/13 (S) RLS AT 9:00 AM FAHRENKAMP 203  
 03/19/13 (S) -- MEETING CANCELED --  
 03/20/13 (H) RES AT 1:00 PM BARNES 124  
 03/20/13 (H) Scheduled But Not Heard  
 03/21/13 (S) TRANSMITTED TO (H)  
 03/21/13 (S) VERSION: CSSB 21(FIN) AM(EFD FLD)  
 03/22/13 (H) READ THE FIRST TIME - REFERRALS  
 03/22/13 (H) RES, FIN  
 03/22/13 (H) RES AT 1:00 PM BARNES 124  
 03/22/13 (H) Heard & Held  
 03/22/13 (H) MINUTE(RES)  
 03/25/13 (H) RES AT 1:00 PM BARNES 124  
 03/25/13 (H) Heard & Held  
 03/25/13 (H) MINUTE(RES)  
 03/26/13 (H) RES AT 6:00 PM BARNES 124

**WITNESS REGISTER**

DAN SECKERS, Tax Counsel  
 ExxonMobil Corporation  
 Anchorage, Alaska

**POSITION STATEMENT:** Testified on CSSB 21(FIN) am(efd fld).

SCOTT JEPSEN, Vice President External Affairs

ConocoPhillips Alaska, Inc.  
Anchorage, Alaska

**POSITION STATEMENT:** Testified on CSSB 21(FIN) am(efd fld).

BOB HEINRICH, Vice President Finance  
ConocoPhillips Alaska, Inc.  
Anchorage, Alaska

**POSITION STATEMENT:** Testified on CSSB 21(FIN) am(efd fld).

DAMIAN BILBAO, Head of Finance  
BP Exploration (Alaska) Inc.  
Anchorage, Alaska

**POSITION STATEMENT:** Testified on CSSB 21(FIN) am(efd fld).

#### **ACTION NARRATIVE**

[6:07:26 PM](#)

**CO-CHAIR ERIC FEIGE** called the House Resources Standing Committee meeting to order at 6:07 p.m. Representatives Seaton, Johnson, Tuck, Hawker, P. Wilson, Saddler, and Feige were present at the call to order. Representatives Tarr and Olson arrived as the meeting was in progress.

#### **SB 21-OIL AND GAS PRODUCTION TAX**

[6:07:48 PM](#)

CO-CHAIR FEIGE announced that the only order of business is CS FOR SENATE BILL NO. 21(FIN) am(efd fld), "An Act relating to the interest rate applicable to certain amounts due for fees, taxes, and payments made and property delivered to the Department of Revenue; providing a tax credit against the corporation income tax for qualified oil and gas service industry expenditures; relating to the oil and gas production tax rate; relating to gas used in the state; relating to monthly installment payments of the oil and gas production tax; relating to oil and gas production tax credits for certain losses and expenditures; relating to oil and gas production tax credit certificates; relating to nontransferable tax credits based on production; relating to the oil and gas tax credit fund; relating to annual statements by producers and explorers; establishing the Oil and Gas Competitiveness Review Board; and making conforming amendments."

[6:08:37 PM](#)

DAN SECKERS, Tax Counsel, ExxonMobil Corporation, stated he is not providing any slides or graphs because there is nothing he can produce that will be any different than what the committee has already seen from the [legislature's and administration's] consultants and others, which is that Alaska's fiscal regime is broken. He said he agrees with most everything the consultants have told this and other committees - under Alaska's Clear and Equitable Share (ACES), Alaska is not globally competitive and, more importantly, not globally attractive to bring needed investments to the state. In ExxonMobil's view, the most important issue facing Alaska today is the need for the state to develop a competitive, attractive, and stable fiscal regime that allows Alaska to attract the needed investments for the North Slope. Deciding whether it is time for Alaska to make a change rests with legislators, not his company. Do legislators want to continue under the uncompetitive and unattractive system of ACES, or do legislators want to make a step change to get the investment that Alaska needs?

[6:10:24 PM](#)

MR. SECKERS said ExxonMobil believes CSSB 21(FIN) am(efd fld) makes significant progress to improving Alaska's overall fiscal environment. Three features of the bill improve ACES and move Alaska forward in global competitiveness. First, eliminating progressivity represents significant improvement and this change alone significantly improves Alaska's global competitiveness. Progressivity is difficult and complicated to work with, plus it takes away all the upside. Upside is needed for investors that risk a lot in Alaska given its unique situation of high cost and other issues. Upside is what ExxonMobil is able to retain in the other places that Alaska is competing with. Eliminating progressivity fixes one of the most penalizing and crippling aspects of Alaska's fiscal regime. The second feature is the gross revenue exclusion (GRE). It is critically important for the state to stimulate exploration and development in resources yet to be discovered in new fields and increasing production from all fields, both new and existing. To be significant any reform to Alaska's fiscal structure must include the legacy fields and the GRE can do just that. However, as currently written it is unclear as to exactly how it will work and how it will be applied to the legacy fields. As a tax practitioner, he said, that level of uncertainty makes him nervous and when he gets nervous he must advise his client who then gets nervous, which then makes the decision under that revenue exclusion that much more hard to make. The third feature is the \$5 per barrel

credit. It is important to tie incentives to production because more production is what everyone wants. This is a very unique simple creative way to do that. However, ExxonMobil's concern is whether \$5 is enough to balance the other features of the bill, particularly the impact of the increased base tax rate.

[6:13:17 PM](#)

MR. SECKERS reiterated that CSSB 21(FIN) am(efd fld) makes Alaska more competitive, but said the real question is whether it makes Alaska attractive enough to get the investments the state really needs. Alaska's competitors - places like North Dakota and Texas - do not face the challenges that are faced in Alaska, such as high costs, remoteness, and distance to market, which are factors that investors have to overcome when wanting to invest in Alaska. While making Alaska more competitive is great, the question that should be before the committee is whether CSSB 21(FIN) am(efd fld) makes Alaska as attractive as it should be. In ExxonMobil's view, the bill's base tax rate of 35 percent is too high and reducing it should be considered. Alaska represents an important and critical component of ExxonMobil's worldwide global portfolio. ExxonMobil is committed to Alaska to help craft a fiscal environment that is stable, competitive, and attractive to bring new investments that will allow Alaska to develop its great resource potential now and in the future. The question now before the committee is whether CSSB 21(FIN) am(efd fld) makes Alaska as competitive as ExxonMobil thinks Alaska should be relative to the competition the state faces. Concluding, he said it is up to the policy makers to decide whether it is time to make a step change from ACES and whether to take CSSB 21(FIN) am(efd fld), improve it, and make Alaska what it can be - competitive and attractive for the investments that everyone wants.

[6:16:32 PM](#)

REPRESENTATIVE TUCK asked what new projects could be expected over the next five years if CSSB 21(FIN) am(efd fld) was passed.

MR. SECKERS replied ExxonMobil cannot speak for the legacy fields of Prudhoe Bay and Kuparuk because it is not the operator; he suggested the question be addressed to BP or ConocoPhillips Alaska, Inc. He added ExxonMobil is progressing Point Thomsen as best it can. ExxonMobil looks for every competitive, attractive investment in Alaska and that is why it is hoping legislators will make changes to increase the opportunities that are there in the legacy fields and elsewhere.

A small improvement in the recovery from legacy fields is likely to dwarf any new discovery on the North Slope. It is hoped this bill would attract other players as well as ExxonMobil to look at opportunities.

6:17:51 PM

REPRESENTATIVE HAWKER inquired what language could be used to remove the lack of clarity in the GRE relating to legacy fields.

MR. SECKERS responded he does not have any specific language. However, of concern are terms such as "accurately metered and measured," or something to that effect, because he is uncertain what that really would mean. More importantly, however, is what would actually qualify as one of the wells. Current language states the well would have to tap into either a new vein or part of a reservoir that was not contributing before, but it is uncertain as to what that exactly might mean. For example, if a well was drilled that produces 10,000 barrels a day, does it all have to be 100 percent new recovery, which is what ExxonMobil's engineers would probably argue, he asked. Would all of it be nullified if someone says 2 barrels out of the 10,000 are an acceleration, he further asked. From a tax practitioner's viewpoint, the clearer the language in a statute, the better off the state will be.

6:19:36 PM

REPRESENTATIVE TUCK asked what projects ExxonMobil would like to do that are currently uneconomical under the ACES regime.

MR. SECKERS answered he will get back to the committee because as a tax person he does not have an inventory of such projects. However, ExxonMobil is working with its partners to pursue every opportunity identified by the operators in the legacy fields. The goal is to make that inventory of projects being looked at grow even larger.

REPRESENTATIVE TUCK, with regard to progressivity, noted that [tax on] the upside can be significantly reduced by investing in Alaska. He asked whether Mr. Seckers, as a tax attorney, has looked at models to see how much more investment ExxonMobil could have made in Alaska that would have bought down that tax burden to make it even more profitable.

MR. SECKERS replied ExxonMobil looks at all the investments and tax is a key component to the analysis. A problem with ACES is

that progressivity relates all the way back to dollar one, so the marginal take is huge; even if a company makes investments, it is a huge impact to the economics. Because tax is calculated monthly, under progressivity there can be huge swings even though the tax is trued up on an annual basis. Any project that made the cut, ExxonMobil wanted to fund under ACES.

REPRESENTATIVE TUCK surmised that while ExxonMobil has been very profitable in Alaska, the issue is that it is not as profitable as ExxonMobil would like it to be competitively with other areas that the company is looking at investing in.

MR. SECKERS responded ExxonMobil has invested in Alaska, paid an enormous amount of taxes and royalties, and has enjoyed its time in Alaska. ExxonMobil is in the business to invest to make money and to produce oil and gas, and if it is attractive and viable to do so in Alaska, the company will do that and wants to do that for the long term. ExxonMobil wants to continue making investments in Alaska if the fiscal regime gets improved enough to allow that to happen.

[6:22:55 PM](#)

CO-CHAIR FEIGE inquired how the provision within CSSB 21(FIN) am(efd fld) for a Competitiveness Review Board might affect ExxonMobil's investment decisions.

MR. SECKERS answered such a board, in premise, might work but would create some concern about the stability of the tax regime because the board would be constantly looking at the regime year after year. While it is prudent for any taxing regime to make certain it remains competitive and attractive, he said he is unsure whether this is the best vehicle in which to do that. There is concern about what information the board would require companies to produce, how confidentiality would be retained, and the amount of interaction that would be necessary for companies to comply with the board's requests.

[6:24:28 PM](#)

REPRESENTATIVE P. WILSON noted concern has been heard over the past few years about why legislators cannot get guarantees. To enable listeners to understand why it is hard for Mr. Seckers to make a guarantee, she requested him to explain how ExxonMobil in Alaska must compete within its own company.

MR. SECKERS responded he does not know of any regime where the host government considering making changes demands guarantees, and he would be surprised if the consultants could identify one. Continuing, he said investments undergo much scrutiny and are tested under a number of different metrics in terms of which projects get funded. The decision is not his to make, it is done in Dallas by people way above his pay grade. It is competitive and looked at worldwide; ExxonMobil has businesses in virtually every country and every state, so an investment has to pass a lot of tests. However, ExxonMobil is bullish on Alaska and wants to invest in Alaska, so it hopes the changes the legislature makes will allow that to happen.

[6:26:15 PM](#)

REPRESENTATIVE SEATON understood the United Kingdom's brownfield development to be a case in which there is a guarantee.

MR. SECKERS replied his understanding is that a guarantee was not demanded per se. While a company would have to invest there to get that allowance, he does not believe the United Kingdom said investors had to tell what they would invest for the government to make this adjustment. Generally, market economics dictate an investment is attractive and competitive to make, and that is what ExxonMobil does and that is where it will invest.

REPRESENTATIVE SEATON understood the United Kingdom's brownfield situation to be one in which a challenged development will go forward when an agreement is reached between the government and a company that a tax reduction or large credit will be received. He inquired whether Mr. Seckers believes the first two elements of the GRE - new units and new participating areas - are clear. He agreed with Mr. Seckers that the third element could be very contentious because any company drilling in a legacy field would claim the oil is new in order to have 20 percent of the gross revenue excluded.

MR. SECKERS responded the first two provisions of the current GRE language are much clearer than is the third. However, the third provision is more critical because it is intended for legacy fields which, in ExxonMobil's view, are where the state's economic future lies. No other resource can stem the state's production in the near term than can the legacy fields, he said.

[6:29:38 PM](#)

REPRESENTATIVE SEATON believed the new participating area is very definitely targeted for within legacy fields. Not talking about guarantees, he asked how long ExxonMobil anticipates it would take to see results if the changes made are significant enough to change behavior.

MR. SECKERS concurred the second element of the GRE could apply to legacy fields. However, ExxonMobil's engineers have said there are no projects in the legacy fields in the near-term or mid-term range that would qualify for that element, which is why he focused on the third element. Regarding the time it would take to see results, he said he cannot speak for other companies, but recalled that Mr. Pulliam, [the administration's consultant], anticipated it would be rather quickly. ExxonMobil is committed to Alaska and wants to invest here, so to the extent that a law is passed that significantly changes ACES, the company would be looking at it as quickly as it can.

REPRESENTATIVE SEATON believed Mr. Pulliam's estimate was the effects would be seen within three years.

MR. SECKERS answered he cannot remember Mr. Pulliam's exact words and the best he can recall is that Mr. Pulliam said it would be sooner rather than later.

[6:32:13 PM](#)

CO-CHAIR SADDLER inquired whether there are other regimes that tax new oil differently than old oil.

MR. SECKERS suggested asking this question of the consultants, but said some regimes offer certain holidays and exemptions for stripper wells, if one considers that new oil. The concept itself is similar to holidays and things of that nature, but he would have to get back to the committee as to whether it is specifically targeted to new oil per se. In further response, he explained a holiday concept is where a company gets relief from a taxing provision, either entirely or a portion, for a period of time based on the happening of certain events; for example, exemption from a tax for a certain period of time in return for drilling a well or for drilling a certain type of well or for doing a certain type of activity. A holiday is also very common with property tax when a company receives exemption for a period of time for constructing an office building.

CO-CHAIR SADDLER recounted Pedro van Meurs telling the legislature a year or so ago about the concept of establishing a

baseline of decline, and where oil produced above that predicted decline line would be taxed as new oil and below that line is existing oil that would have been produced anyway. He asked whether Mr. Seckers has heard of such a tax regime in practice.

MR. SECKERS responded none come to mind.

CO-CHAIR SADDLER inquired whether ExxonMobil reports proven reserves to the Securities Exchange Commission (SEC).

MR. SECKERS answered that is not his job to do but imagines the company does, although he does not know the extent of the report that is filed.

CO-CHAIR SADDLER asked how it is determined what a proven reserve is, explaining that he is trying to find out whether this is a method for identifying old oil versus new oil.

MR. SECKERS replied he will have to ask a company engineer as to what the exact criteria is.

[6:35:26 PM](#)

CO-CHAIR SADDLER requested Mr. Seckers to ask an ExxonMobil reservoir engineer the following question: "Would the difference between what is proven reserves this year and what might be seen as proven reserves in future years be seen as one possible mechanism for identifying what is new oil versus old oil?" He explained the reason for his asking this question is Mr. Seckers' statement that the mechanism proposed by the Department of Natural Resources (DNR) is not real clear, so he is searching for something that might be clearer.

MR. SECKERS responded he will have to give that some thought. Proven reserves, unproven reserves, and static reserves are not an exact science. He recalled there was concern about the decline curve and where that is measured from. He offered his hope for a simpler result, such as having the Alaska Oil and Gas Conservation Commission (AOGCC) certify a well that is drilled, as opposed to having to barrel-track it or making it more complicated. In further response, he offered his belief that when a well is drilled and starts to flow it is in the purview of the AOGCC to make certain that it is, in fact, a producing well. He concurred with Co-Chair Saddler that the AOGCC does not determine whether it is new or old oil; however, he added, he is not 100 percent certain.

6:37:12 PM

CO-CHAIR SADDLER inquired whether Mr. Secker's would like to propose a better way under the third element of the GRE to determine what is new oil that would have not been produced absent the changes in tax law.

MR. SECKERS answered he would have to give that some thought, but he knows from talking to ExxonMobil's engineers that the only way for wells to get funded is if it is to bring on new reserves, not to accelerate production. Therefore, he is not certain the split that Co-Chair Saddler is looking for is actually necessary. The better test might be that if the well is drilled and it flows, then some sort of relief to make it more attractive could be in order.

CO-CHAIR SADDLER understood Mr. Seckers to be saying, then, that it is not an incentive to maximize production within the parameters of the health of the reservoir when profits from drilling are higher at high oil prices.

MR. SECKERS replied the version of the bill before the committee is clearly a significant improvement. The goal now is to make it as attractive as possible by having it apply to the legacy fields - which are the state's lifeblood - so that investments occur there. ExxonMobil has an inventory of items it hopes to expand when they become competitive to do so. In further response, he agreed to take Co-Chair Saddler's aforementioned question to ExxonMobil's reservoir engineers.

6:39:15 PM

REPRESENTATIVE TARR noted Point Thomsen is the only project Mr. Seckers mentioned as something that will be adding new oil soon. Since that oil is the result of a court case, she said she cannot imagine that Mr. Seckers is suggesting the best way to get to new production is through litigation. She asked whether Mr. Seckers has any additional information about what projects are potentially coming on line. Regarding the gross revenue exclusion, she pointed out that some legislators have concern that it is inappropriate for already-planned activities to be eligible for the GRE.

MR. SECKERS responded his comments on Point Thomsen were in response to a question about what ExxonMobil is currently doing. He said it is inappropriate for him to speak to projects at legacy fields because ExxonMobil is not the operator. He

suggested the question be asked of the operators when they testify today. In terms of the gross revenue exclusion, he said ACES does not make Alaska attractive or competitive. It is ExxonMobil's view that legislators want to make Alaska competitive as well as attractive and incentivize all production, whether from new or existing fields. To get to production, to stem the decline in the near term, ExxonMobil believes the legacy fields should be part of that target. Incentivizing as many opportunities as possible is a critical component of any major change to the fiscal regime.

[6:41:20 PM](#)

REPRESENTATIVE TUCK understood tax breaks in the legacy fields will help in the short term, but inquired whether ExxonMobil would be looking at doing new exploration if the bill passes.

MR. SECKERS answered ExxonMobil looks at every lease sale that comes up and has bid on some in recent times. While people like to refer to ExxonMobil as "harvesting" - which his company thinks is an inappropriate comment - the company is exploring every opportunity to expand the legacy fields to get as much improvement into those fields as possible. He is unable to say whether ExxonMobil would look into long-term exploration opportunities because he is not on the exploration side of the company. However, ExxonMobil is looking at Alaska all the time and if any competitive opportunities present themselves the company would be very interested in them.

REPRESENTATIVE TUCK asked what years in Alaska were the most profitable, or the heyday, for ExxonMobil.

MR. SECKERS replied ExxonMobil provides all its information to the Department of Revenue. As a matter of course, the company does not talk about profits.

[6:43:18 PM](#)

CO-CHAIR FEIGE opined that a wide range of different things could be done in this legislation, pointing out that over the last year legislators have investigated many different options. He inquired what type of incentive, in Mr. Seckers' best estimate, would result in the most production the soonest.

MR. SECKERS responded policy change affects many taxpayers, so different buttons affect different people different ways, making it a difficult question to answer. If members stay within the

structure of CSSB 21(FIN) am(efd fld), he would suggest that the base rate is too high and is an area that ExxonMobil thinks should be lowered. Clarity around the GRE would be important. The \$5 per barrel is a simple and good concept, but members should check with consultants as to whether \$5 is the right number. Of those three areas, he said the base rate is the most critical.

[6:44:42 PM](#)

CO-CHAIR SADDLER asked how ExxonMobil would deal with the third category of GRE provisions if they became law.

MR. SECKERS answered clarity could be added by regulation should the statute become law as currently written, in which case ExxonMobil would be active in providing guidance. However, his personal perspective is that he would much rather see it in statute where it is clearer.

CO-CHAIR SADDLER inquired whether ExxonMobil would wait until there was clarity through regulation before the company factored this provision into calculating its investment decisions.

MR. SECKERS replied he would have to check with his company's engineers before he could answer. On a general sense, he said, it is hard to make investments when it is uncertain how the law is going to operate. It is hard to advise a client to take an action in the hope that a regulation will be drafted a certain way. However, ExxonMobil does have faith that the regulations would be drafted to provide the clarity that would be required.

CO-CHAIR SADDLER surmised ExxonMobil would hang back until there was more certainty.

MR. SECKERS responded ExxonMobil would definitely take a cautious look because it would not know for certain what the outcome might be.

[6:46:56 PM](#)

CO-CHAIR SADDLER asked whether the timing of the decision about the GRE qualification, i.e. if that decision was made closer to the front end or towards the end of a decision to invest, would have any bearing.

MR. SECKERS answered the most clarity upfront the easier it is to make a decision. It is no different than for a person trying

to make decisions when there is a tax impact. The sooner one can get that clarity, the better the investment decision would be and the more certainty one would make that decision under.

CO-CHAIR SADDLER inquired how much trust ExxonMobil would have that the Department of Natural Resources (DNR) will make a decision the company could live with should the GRE provisions pass as currently written.

MR. SECKERS replied both the Department of Natural Resources and the Department of Revenue do the best job they can and he thinks they do a great job. One would hope the intent of this provision is for them to provide the certification that one can rely on. Guidance to that effect, clarity in terms of what information a company needs to provide to get that certification and the timeframe the director or commissioner has to issue that, are critical and one would hope they would be addressed in the regulations. He offered his belief that the administration would operate in good faith, as it always has, and that if DNR issued certification that both departments would respect that.

[6:48:47 PM](#)

CO-CHAIR SADDLER asked whether there is anything about the consultants' views or representations of the GRE, as it is defined and would be applied, that ExxonMobil would like to answer or to correct.

MR. SECKERS responded all of the consultants, including Mr. Marks, have done a great job and have represented the state of Alaska's competitiveness accurately. He said he cannot question the data the consultants used because he does not have access to that, but he believes what they presented is fair and objective and he sees no fault in what they have provided thus far.

[6:49:43 PM](#)

REPRESENTATIVE P. WILSON understood Mr. Seckers to be saying that ExxonMobil would act quicker if clarity was provided in the bill itself rather than waiting for regulations to do so, given that putting regulations into place can sometimes take years.

MR. SECKERS answered the more concise and specific the language, the better. He suggested DNR be asked how long it expects it will take to create the regulations that it would want companies to operate under should the bill pass, given there are a lot of missing pieces. To the extent the information is known in

advance, the easier the decision to work under that provision becomes.

6:50:55 PM

REPRESENTATIVE OLSON thanked Mr. Seckers for his testimony, stating that in a number of meetings the only testimony from ExxonMobil was on paper or lasted less than five minutes. He noted ExxonMobil has been tied to the history of Alaska for an event that had more to do with the name of a vessel than something the company was directly responsible for, but which has had a negative impact on relationships between Alaska and the company. He said he has been told throughout his 30 years of involvement with the industry that ExxonMobil is the toughest of the three companies in Alaska to deal with when it comes to putting together a deal, but once the deal is put together and signed ExxonMobil is the easiest because it does not micro-manage. He inquired whether that is an accurate assessment.

MR. SECKERS replied the aforementioned event was a tragic accident that ExxonMobil regrets. That event, he continued, made ExxonMobil look at its internal operations, improvements were made, and the company is now an industry leader in operational safety. When ExxonMobil says something it says what it means and it means what it says. It is unfortunate that people say ExxonMobil is hard to deal with, but it is because ExxonMobil likes to make certain the answer is right and is the best answer for all parties involved. Once that cut is made, ExxonMobil will do things to the best operational safety standards possible.

REPRESENTATIVE OLSON added he was not making a negative comment, just trying to get to the chase without taking half an hour.

6:53:42 PM

REPRESENTATIVE TUCK, regarding the instability that ExxonMobil fears a Competitiveness Review Board might cause, requested Mr. Seckers' opinion on whether the legislature should continue with its approach of making decisions based on what it hears from the experts it hires rather than establishing a board. He further asked how more stability could be created to give ExxonMobil more confidence going forward.

MR. SECKERS responded stability is important but only works if it is not at too high of a price. The Competitiveness Review Board could work, but to require by law that an analysis and

reporting be done every single year adds an element of concern because that means it is likely to change or could be changed. While ExxonMobil understands the legislature is free to change a law whenever it wants, putting in statute that the legislature will constantly look at a law makes it concerning.

[6:55:41 PM](#)

REPRESENTATIVE TUCK recalled that during the 2012 special session, PFC Energy stated that the decline curve could be looked at and negotiated to incentivize anything above the curve. Regarding the GRE and the question of what would constitute old oil versus new oil, he asked whether Mr. Seckers thinks it would be better to look at all oil as being the same.

MR. SECKERS answered he was aware of the proposals made last year regarding the decline curve idea. While he is personally unaware of any current regime that employs this, that is not to say there are none. The legacy fields represent the only known resource that is able to stem the production decline in the near-term or mid-term and it is ExxonMobil's view that the goal should be to make that as attractive as possible. The idea he mentioned before - [giving some relief] if a well is drilled and it flows - would make it simpler under the GRE and would be an attractive incentive. It is hard to distinguish; it is not an exact-measurement science. ExxonMobil's engineers do not drill wells to accelerate, they drill wells to add production, to add recovery, and therefore it should qualify. So, to the extent clarity can be made in the GRE and make it apply to the legacy fields, that is a step forward in the right direction.

[6:58:14 PM](#)

REPRESENTATIVE TARR referenced Mr. Seckers' statements about the proposed base tax rate being too high and about overall competitiveness. She asked whether Mr. Seckers has seen the chart provided by Mr. Janak Mayer of PFC Energy showing that Alaska would be well below many other oil producing areas, particularly for new development. She requested that he elaborate on what he means in terms of competitiveness.

MR. SECKERS replied he has seen the chart but does not have it committed to memory. He said his reference to the base rate and competitiveness was in regard to whether this proposal makes Alaska more competitive, which it unquestionably does. And it is absolutely better than ACES because it cannot get much worse than ACES. While CSSB 21(FIN) am(efd fld) would make Alaska

more competitive and put Alaska's regime in the middle of the pack, he would like to see Alaska become more attractive. He wants Alaska to beat North Dakota and Texas. To the extent that Alaska can make itself as attractive as it can be, the more investments are likely to flow. He said ExxonMobil believes the base rate is too high - it affects the effective tax rates. Look at all of the other issues that Alaska faces. For example, a slide produced by Mr. Mayer for the Senate Special Committee on TAPS Throughput shows how Alaska compares cost-wise and the cost in Alaska is staggering. ExxonMobil suggests consideration be given to making Alaska more attractive than these other places that do not have such high costs and distance to market. Addressing the base tax rate, which ExxonMobil thinks is too high, is one way to do that.

REPRESENTATIVE TARR offered to share a copy of the chart, saying that in the example she is looking at Alaska would be more competitive than North Dakota under CSSB 21(FIN) am(efd fld). Responding to Co-Chair Feige, she said she is referring to the chart the committee was given yesterday. She further confirmed the example is under the GRE fields.

[7:01:00 PM](#)

CO-CHAIR SADDLER noted there are a number of other provisions in the bill besides the GRE, base rate, and \$5 [credit] per barrel. He asked Mr. Seckers to provide ExxonMobil's opinion regarding the proposed change in interest rate, the carry forward loss, and the Alaska manufacture credit.

MR. SECKERS responded ExxonMobil encourages Alaska to make itself as competitive and attractive as possible. Reducing the interest rate is a critical step and something ExxonMobil has endorsed for years. While the manufacturing credit would help make Alaska more competitive in terms of more jobs and more investment, it is hard to say whether it would impact ExxonMobil per se. Regarding the tax loss carry forward provisions, he remarked that if ExxonMobil found itself in a loss, everyone would be hurting. But, he continued, from the perspective that the rate was changed to match the proposed new base rate, it is probably incentive to many companies, and smaller companies in particular. Some of these provisions may be very critical to encouraging other companies to come to Alaska, and ExxonMobil supports these changes being made for them.

CO-CHAIR SADDLER, regarding Mr. Seckers' statement that a 35 percent base tax rate is too high, inquired what number would not be too high.

MR. SECKERS declined to say, stating it is up to legislators to decide how attractive Alaska should be. He suggested asking this question of the legislature's consultants.

[7:03:32 PM](#)

REPRESENTATIVE P. WILSON observed that the chart mentioned by Representative Tarr only mentions the government take and therefore does not tell overall where Alaska is at. She asked whether ExxonMobil just looks at government take or looks at the overall package when making its decisions.

MR. SECKERS answered government take is a key component to any investment decision that ExxonMobil makes. It is just one gauge that is used, but not the only one; a number of measurements are used that are proprietary to ExxonMobil.

REPRESENTATIVE P. WILSON inquired whether other changes, such as allowing permanent roads so that work could be done year-round instead of only certain times, would make a difference.

MR. SECKERS replied it clearly would make a difference in respect to access to resources, but he cannot say how that would relate in terms of making Alaska more competitive and attractive for investment dollars. He suggested this question be asked of the legislature's consultants.

[7:05:42 PM](#)

SCOTT JEPSEN, Vice President External Affairs, ConocoPhillips Alaska, Inc., began his PowerPoint presentation by framing the issues within Alaska that pertain to the kind of investments ConocoPhillips Alaska, Inc. ("ConocoPhillips") is currently pursuing [slide 2]. The easy oil is gone, he said; the easy oil being the type of development that was had when Kuparuk and Prudhoe Bay were first developed. Those were high rate wells that were relatively simple, although at the time those wells were pushing technology. There was very little or no water with those wells, the kind of development that every engineer strives to be in on the front end. As they mature, however, continuing to increase production, increase recovery, becomes a more complex problem, which is where things are right now in the North Slope legacy fields of Alpine, Kuparuk, and Prudhoe Bay.

Although Alpine is younger, it still has its own particular challenges.

MR. JEPSEN pointed out that ConocoPhillips is currently drilling very complex wells, such as the octa-lateral, and the wells being drilled tend to be very high cost. Drilling inexpensive wells is pretty much not done in the "oil patch" these days, but in Alaska they tend to be higher than average. ConocoPhillips is targeting smaller reserves and fault blocks that take a lot of technology to identify, as well as drilling around the flanks of the fields where oftentimes the sands are thinner, rates are lower, and sand quality is often not as high. ConocoPhillips has developed satellites and will continue doing so, but they tend to be capital intensive because most of the satellites require roads, pads, new wells, pipelines, and power lines. Viscous oil is also being looked at, but the billions of barrels of viscous oil on the North Slope are challenged by relatively poor reservoir quality, thick oil, and low rates. Accessing much of the viscous oil will require infrastructure investments, not just drilling off of existing pads.

[7:08:40 PM](#)

MR. JEPSEN said a technique being used by ConocoPhillips to maximize recovery in these aging fields is water flood, which produces more and more water as the oil is produced. Right now, about three times as much water as oil is being produced, which drives up the operating cost per barrel and is a trend that will probably continue. However, he emphasized, there is tremendous resource potential in the legacy fields. A few years ago, the Department of Revenue (DOR) put out a forecast of over 4 billion barrels of oil to be recovered from the legacy fields for the years 2010-2050. In that same study, DOR looked at the recovery from the fields of Nikaitchuq, Oooguruk, Point Thomsen, and Liberty, and the total from these fields was less than a quarter of the legacy fields. He said he is not diminishing the significant accomplishments of the companies that have been exploring and developing these other opportunities, but in the near-term the greatest opportunities for increased production, increased reserves, are in the legacy fields.

[7:10:19 PM](#)

BOB HEINRICH, Vice President Finance, ConocoPhillips Alaska, Inc., began by reviewing the issues that ConocoPhillips sees with Alaska's Clear and Equitable Share (ACES) [slide 2]. He said the primary issue is the high average and high marginal tax

rates. The top right graph on slide 2 illustrates the effect of marginal tax rates by the state and federal governments and the producers across a range of prices, he continued. Marginal share is the incremental cash that is generated by a \$1 increase in price and how that incremental dollar is split between those three parties. At today's price environment of roughly \$110, less than \$.20 on every incremental dollar is actually retained by the producer; the other \$.80 is split among the state and federal authorities. The red bars on the graph represent the State of Alaska, he explained, and their increasing height as prices increase is wholly a function of the progressivity surcharge under ACES. As prices increase, this progressivity eliminates the upside from prices that producers typically see when working in other oil-producing regions.

MR. HEINRICH said the effects of progressivity and the high marginal tax rates are best illustrated by looking at the bottom right chart on slide 2 which depicts earnings by ConocoPhillips Alaska, Inc. From 2007-2011, oil price movements were between \$60 and \$110 per barrel [ANS West Coast], but the earnings of ConocoPhillips Alaska hardly moved - staying between \$22 and \$25 per barrel. Nearly all of that upside was paid to the State of Alaska through the progressivity feature of ACES. The tax credits, however, do help offset a small part of the high tax rates that result from ACES and they serve a purpose in helping to offset the high cost environment and difficult conditions of Alaska. Another positive aspect of those ACES tax credits is that they do apply to all fields; they are providing incentives to improving production in the legacy fields as well as the new developments. However, those tax credits in the structure of ACES are not enough to offset the high average and high marginal tax rates that result from the progressivity feature of ACES.

[7:12:52 PM](#)

MR. HEINRICH turned to discussing his company's point of view on CSSB 21(FIN) am(efd fld) [slide 3]. He said ConocoPhillips has advocated for elimination of progressivity due to its impact at the high price environment, the prices of today and above. Also, creating a flatter tax rate over a broad range of prices is a positive approach to taxation, he continued. The proposed bill achieves both of those.

MR. HEINRICH drew attention to the upper right graph on slide 3 that compares ACES and CSSB 21(FIN) am(efd fld) from a producer share basis across a range of prices using industry data from the Department of Revenue. He explained that producer share

calculations depend on many factors, including assumptions like cost structure - operating and capital expenditures - which vary from field to field and producer to producer and person to person doing the analysis. The resulting producer share under CSSB 21(FIN) am(efd fld) is basically flat across a range of prices [\$60-\$120], which ConocoPhillips likes because it represents a consistent split of results across this range of prices between the state and the industry. It means as the pie gets bigger the industry and the state share a portion in the same tax rate. At an ANS West Coast price of \$60 per barrel and below, the gross minimum tax kicks in under both ACES and CSSB 21(FIN) am(efd fld). That eventually results in situations where the producers are paying taxes despite their negative cash flows from their operations. Below a price of \$91, the Senate bill represents a tax increase compared to ACES, while above \$91 it represents a benefit to the producers. The loss in producer share [at prices between about \$61 and \$91], is a result of the elimination of tax credits, which provide a significant portion of the benefit at lower prices. The combination of the higher base rate of 35 percent, offset in part by the \$5 per barrel of produced oil credit, is not enough to offset the loss of the tax credits at these low prices.

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MR. HEINRICH stated ConocoPhillips supports establishing a tax structure that creates an attractive investment climate for an overall competitive tax rate helping offset the high cost of Alaska's operating environment and that incentivizes both the existing fields and new fields for new production. He reiterated that CSSB 21(FIN) am(efd fld) represents a tax increase at lower prices. While it is a good improvement, it still puts Alaska at the upper end of its competitive peer group and that does not differentiate enough to offset Alaska's high cost and difficult operating environment. Lastly, the GRE concept, as currently structured, does not appear to do much for the legacy fields.

MR. HEINRICH moved to bar chart on slide 4, noting it is similar to the one shown earlier by Representative Tarr, but is instead from PFC Energy's [March 12, 2013,] testimony before the Senate Finance Committee. He explained the chart shows the effective tax rates of different fiscal structures in different oil producing areas at the four different crude prices of \$80, \$100, \$120, and \$140 per barrel. The red arrow on the far right of the chart points to Alaska's current system under ACES for an existing producer, which essentially is the legacy fields and

which, in these scenarios, do not get a benefit from the GRE. Here, the effects of the progressivity surcharge under ACES can be seen - the [percent] government take increases as prices increase. However, as shown by the bars to the left of the ACES arrow, the majority of the more competitive structures actually have slightly regressive systems. He noted that the blue arrow located in the middle of the pack for competing jurisdictions represents Alaska at a 30 percent base rate with a \$5 per barrel of oil produced credit, a provision that was considered for a point in time in the Senate Finance Committee. The left red arrow, labeled 65 percent, was pulled from a another slide that PFC Energy showed in its [March 12, 2013,] presentation for the bill's current provision of a 35 percent base rate with a \$5 per barrel of oil produced credit. At the 65 percent government take level, CSSB 21(FIN) am(efd fld) positions Alaska at the high end of the middle of the pack. While ConocoPhillips expects the activity levels to increase, at that tax rate it may not be as high everyone would like to see.

[7:18:34 PM](#)

MR. JEPSEN then addressed the gross revenue exclusion (GRE) provision, saying ConocoPhillips' comments echo much of what was said by Mr. Seckers. While the GRE by itself does provide a mechanism to incentivize investment, ConocoPhillips sees a couple of problems with it. The currently proposed criteria for how a well would qualify states that it cannot be contributing to production. As mentioned earlier, ConocoPhillips is searching its legacy fields for fault blocks, isolated fault blocks that are not being drained very effectively. In many instances these fault blocks may not be completely sealing. ConocoPhillips is going back and developing reserves that will not produce into the life of the field if another well is not put there. From a strictly rigorous reservoir engineering point of view, it might be very tough to convince the Department of Natural Resources (DNR) that this particular location has not been contributing to production, even though at the end of field life a lot of oil will be left behind and even though by drilling the well it will book additional proven developed reserves. As the GRE is currently written, ConocoPhillips is greatly concerned as to whether it will be able to convince DNR that many, if any, of its legacy field projects qualify for the GRE. It could be that DNR's intent is different than what is seen in the written words, but it would make ConocoPhillips feel better if there was greater clarity around that.

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MR. JEPSEN stated that the GRE language of "accurately metered and measured" is also a potential issue. However, he continued, there is precedent for statutory language of this nature and still making it work within the fields. ConocoPhillips does not meter and measure every single well in the field. It tests the wells on a periodic basis and compares that to how much oil is actually being put down the pipeline for a particular field. For example, oil going into the Kuparuk pipeline is allocated back to the individual fields, individual drill sites and wells, based upon the well tests. While this allocation methodology sounds a bit complicated, it is one that ConocoPhillips has used in the past when there were the separate economic limit factors (ELF). ConocoPhillips is using this allocation methodology for leases that have different royalty rates and how much oil comes from each lease. Thus, it is not without precedent, but from ConocoPhillips' point of view, the company would feel more confident if the issue about what qualifies for a GRE can be solved and there is something either on the record or in the statute that clarifies what is meant by "accurately metered and measured."

MR. JEPSEN provided ConocoPhillips' suggestions for changes to the GRE. He said one suggestion is that production from any new well (whether a sidetrack, a coil tubing drilling well, or a grassroots well) that meets the criteria for qualified capital receives the GRE. The reason for using qualified capital is because the term is defined under ACES as part of the calculation for determining the net profit per barrel. Generally speaking, when a company is going to capitalize the well, new reserves are being produced - additional recovery is being produced - versus what the company is getting out of the field. From the viewpoint of ConocoPhillips, using that as criteria for what qualifies will be clearer. A company would understand going into it that a particular well qualifies for the GRE. It would make it a greater incentive, particularly for the legacy fields, and would bring more investment and drilling rigs into those fields. If the intention is that it is not going to apply to the legacy fields, then the language as written probably accomplishes that.

[7:22:31 PM](#)

MR. JEPSEN reiterated that it is ConocoPhillips belief that the greatest opportunities for incremental investment, production, proven developed reserve additions, are within the legacy fields. He urged the committee to take a look at the

aforementioned suggestion as an option for the GRE. Making it simple and clear is going to be the key to making it work. The more complicated it is, the more retrospective the analysis is. The more technical it is, the less applicable it is probably going to be. The less of an impact, the less of a factor it is going to be in making investment decisions.

MR. JEPSEN concluded by stating that CSSB 21(FIN) am(efd fld), as currently proposed, is an improvement over ACES and would lead to incremental and more investment. It would put Alaska at the high end of places that are taking the lion's share of ConocoPhillips' investment right now. For example, in the Lower 48 the company's investment between the years 2010 and 2012 has gone from \$1.5 billion to \$4.8 billion. That investment is partly because of the resources and partly because of technology, as well as because of the favorable tax framework. Alaska has many of the same characteristics, but under ACES it does not have the same kind of favorable tax framework. While CSSB 21(FIN) am(efd fld) is a positive step, if Alaska wants to see the kind of investment it would like, then ConocoPhillips would ask the committee to consider reducing the base rate to move Alaska into a regime that is more attractive than under the bill as currently written. Modifying the GRE so it can be counted on for legacy field investments would be another significant improvement.

[7:24:47 PM](#)

REPRESENTATIVE TUCK asked what the decline curve is today within ConocoPhillips' legacy fields.

MR. JEPSEN replied the curve is a function of the maturity of individual wells and individual patterns. For a new well coming on stream, the base natural decline without water flood, without enhanced oil recovery (EOR), is about 18 percent. A mature well that has been on stream for 30 years might have a decline of 8-9 percent. In addition to being a function of that particular well's maturity, the decline curve is also a function of the kind of processes being used to enhance recovery. The decline rates seen in these fields generally are not what he would call natural decline rates because ConocoPhillips has a lot of enhanced oil recovery processes going on.

REPRESENTATIVE TUCK inquired where the legacy fields belonging to ConocoPhillips Alaska, Inc. currently stand.

MR. JEPSEN responded he does not have handy the actual decline rate for the Kuparuk field, but will get back with that number.

REPRESENTATIVE TUCK asked how many of ConocoPhillips' operations in its legacy fields require collective decisions with the other two producers.

MR. JEPSEN answered in the Kuparuk Field it takes ExxonMobil, BP, and ConocoPhillips Alaska, Inc. to approve the majority of the investments.

REPRESENTATIVE TUCK inquired whether ConocoPhillips has some projects it would like to get released as soon as ACES is fixed.

MR. JEPSEN replied if a change to ACES is seen, ConocoPhillips will factor that into investment decisions; a range of options has been discussed during this legislative session. If the bill passes as currently written, his company will push for some additional investments, but it may not be as much investment as the company thinks it could potentially fund in these fields if it had a more robust tax framework.

[7:27:19 PM](#)

REPRESENTATIVE HAWKER understood ConocoPhillips has had two significant oil exploration successes in the Gulf of Mexico. He asked whether those successes could be discussed to illustrate a difference in productivity and the economic competitiveness of the Gulf of Mexico compared to Alaska.

MR. JEPSEN responded he probably cannot give the granularity being looked for because he is not that familiar with deepwater Gulf of Mexico. However, as seen on the far left side of the [slide 4] chart, the Gulf of Mexico is the most competitive place in the world to invest. That is generally true on federal offshore waters because there is no severance tax and the royalty rate is usually about 12.5 percent. ConocoPhillips is one of largest lease holders in deepwater Gulf of Mexico, the reasons being that it is resource rich and a very competitive place to invest.

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REPRESENTATIVE HAWKER noted that while much is included in CSSB 21(FIN) am(efd fld), he is also interested in things that may not be in it. A perennial issue for him is where the state can remove impediments that make it possible for everyone to better

administrate Alaska's tax code. He inquired how important or helpful it would be if state auditors were able to place a reasonable and tested reliance upon joint interest buildings.

MR. HEINRICH answered ConocoPhillips supports that concept that joint interest buildings do represent a reasonable approach in identifying costs that are audited among the partners as well. Responding further, he said it may help streamline the process of the state's audits. For example, ConocoPhillips Alaska, Inc. is still waiting for its first audit under ACES.

7:30:05 PM

REPRESENTATIVE HAWKER stated that in the definition of lease expenses he believes the legislature has abrogated its ability to write statute, and to write very clear statute, when it allows the Department of Revenue to adopt regulations as well as to establish additional standards for purposes of carrying out this section. He asked whether giving that extraordinary latitude to the Department of Revenue has caused the industry any problems with the surety of being able to go through the code and know what can and cannot be claimed.

MR. HEINRICH responded the clarity of the regulations has been a challenge for ConocoPhillips in terms of not knowing how they are going to be interpreted and applied in practice. Some of that clarity will happen over time as audits are concluded and a history is developed.

7:31:53 PM

REPRESENTATIVE SEATON, regarding testimony by ConocoPhillips and others about the complexity of the GRE when applying it to existing producing areas and where those determinations will be made, said he anticipates the determinations will be challenged and result in administrative appeals and court cases. However, he continued, the two provisions of the GRE for new units and new participating areas are clear and simple. He recounted that at ConocoPhillips' February 28, [2013,] analysts meeting, it was stated that the company is working hard to develop and produce every last barrel it can get at economically and is trying to get to hard-to-reach pockets of oil that have been bypassed and are not being produced by existing wells, and to do it without spending a lot of money. It was said that accessing these pockets using conventional drilling was not economic, which resulted in use of the lower cost method of coil tube drilling. He recounted that the House and Senate resource committees just

returned from an excellent tour of ConocoPhillips' facilities on the North Slope where members saw that this coil tube drilling is neat and clean and does not require bores, casing, or blowout preventers. Given there are more economic ways than conventional drilling to get to that oil, he asked why the legislature would try to apply a very complex GRE to determine which oil was participating rather than taking ConocoPhillips' word that this is a very economical way to get at those and enhance that production. He requested an explanation of the reasoning for why ConocoPhillips would be supporting something that is going to be very administratively complex.

[7:34:42 PM](#)

MR. JEPSEN, regarding the GRE itself, answered ConocoPhillips is advocating something that is considerably simpler than what is in the current bill. ConocoPhillips would urge the committee to change that so it is not so difficult to interpret. Regarding the analysts' presentation, ConocoPhillips was talking about how to apply technology to its worldwide portfolio to help increase production and increase recovery. What was being discussed during that presentation is what is being done day in and day out at Kuparuk; it is nothing new, it is not an incremental stream of investment, it is not a new project, it is not a new initiative. ConocoPhillips has been doing essentially that same kind of work - that same level of investment - in those same kinds of projects for the last five years under ACES. So, if ConocoPhillips is going to do that, the question being asked is why apply for a GRE. One reason is that even under CSSB 21(FIN) am(efd fld), Alaska is still at the top of the middle of the pack. ConocoPhillips anticipates what it will do in the future and the disclaimers at the front end of all these presentations is, "investor make your own decisions about ... what the company's performance might be." The world could change, so no plans are cast in stone. If things remain as they are today in terms of the company's capital situation and other opportunities for investment, this is what the company will probably do. To be clear - ConocoPhillips could do more in Alaska. If Alaska was in a place where it could attract more investment, ConocoPhillips would do more of those types of activities. If the question is whether the status quo is okay so nothing needs to be done to secure it or whether the state would like to see more, he would argue that as a state he would like to see more - more jobs, more oil down TAPS, a long-term healthy economy - and that can be done if substantial changes are made to ACES.

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REPRESENTATIVE SEATON appreciated that global look, but argued the problem is that there is a substantial change to ACES under CSSB 21(FIN) am(efd fld). The biggest change is SB 21, not the GRE applied to the third category, which is very complex. Something legislators have been told all along is to make it simple. But this one element is being said to be very complex; therefore, companies will apply for everything, which he presumes will mean the state is going to have a lot more decisions and frustration on everyone's part. He said he can understand a company wanting to have 20 percent of a field's gross revenue excluded, but asked why stimulate a very complex system that has an indeterminate measurement that nobody will agree on, whereas the other two portions of the GRE are pretty cut and clear. He requested a response to the coiled tubing drilling and other things that ConocoPhillips is currently doing in the field and why that should have the extra incentive of a gross revenue exclusion.

[7:39:18 PM](#)

MR. JEPSEN replied, "This is not a global answer, this is a specific answer. If you change ... the tax framework in Alaska, it will attract more investment. ... This gets back to ... where we stand in other places we are investing money, we are at the high end of ... the government share in those other places where we are investing a lot of money right now." To put Alaska in a more competitive position, one of the few things in legislators' control is the tax rate. Getting to the middle of the pack would be a better position for Alaska and one way to get there is to apply the GRE to new wells that have production, have reserves, in the legacy fields. But, it will take time to get there. Regarding the second part of the GRE that applies to participating areas (PAs), he said he thinks it would be hard to administer in the existing fields for several reasons. First, he does not see a lot of opportunities for new PAs, which means talking about expansion of existing PAs, and the vagaries currently seen in the [proposed] statute make it uncertain as to whether that is something that a company can count on. It has the measurement issues and whether the Department of Natural Resources might say that at least a portion of the expansion was probably contributing to production in some way. So, even the second item in the GRE will have little applicability. If the purpose of the GRE is to bring new investment and see more production in the next 5-10 years, then it needs to be applied to legacy fields, otherwise no one will be qualifying for a GRE for quite some time. Lastly, ConocoPhillips is advocating for

making it simple. As currently written, the GRE will be very complicated and may not have the desired consequences because ConocoPhillips may not bother trying to pursue one. It is the job of the Department of Natural Resources and Department of Revenue to protect the state's interests; so, if written in such a fashion that they can deny the GRE, he anticipates that they will and he cannot fault them. ConocoPhillips might test it once or twice and if it is applied in a very conservative fashion, he would just decide it is as suspected. He therefore thinks it needs to be simpler and should apply to the legacy fields, and the suggestions that ConocoPhillips has laid on the table would make it simple and clear.

[7:42:10 PM](#)

REPRESENTATIVE HAWKER, regarding ConocoPhillips' suggestion for new wells that meet the criteria for qualified capital, inquired whether ConocoPhillips is suggesting it be linked back to the definition of a qualified capital expenditure under the [AS 43.55.023] credits section, where as long as it meets the state's criteria for a lease expense and is essentially incorporated into the internal revenue code, that this be the basis for the determination.

MR. HEINRICH responded correct, saying a reason ConocoPhillips came to that particular metric is because it is already in the existing structure. The company is familiar with how it is calculated, the company's returns are filed on a monthly basis, and it is already going through the audit process. It is a metric ConocoPhillips can use to file its federal income taxes that then feed in to the determination under the qualified capital under ACES.

[7:43:31 PM](#)

REPRESENTATIVE TARR recalled that about a week ago in the Senate Finance Committee, ConocoPhillips stated it could not say how much it would do differently if this bill were to pass. She asked whether that is still the company's position.

MR. JEPSEN answered correct, ConocoPhillips feels it is going directionally the way it should go. Projects are looked at on a case-by-case basis and he thinks they will fare better than they would under ACES.

[7:43:58 PM](#)

REPRESENTATIVE TARR recalled seeing a legislative research report showing the per-barrel profits and, except for the Asian Pacific Region, Alaska was at the top and had record profits over the last several quarters. If that is not a situation that allows ConocoPhillips to invest in Alaska, then where is the company investing, she inquired, and what would give the committee reason to believe that ConocoPhillips would invest, then, under a situation where it does not have record profits.

MR. HEINRICH replied he may not speak specifically to the data points, but said the aforementioned material looks like it may be coming from ConocoPhillips' recent Form 10-K report outlining the metrics from the different regions in which the company is producing. What cannot be seen from the numbers, he explained, is the type of production in those different areas. In the Lower 48, where the company's profits are probably on the lower side of the different regions, almost 70 percent of production is natural gas. In recent times natural gas has been at historical low prices, which affected the company's earnings for the last several years, particularly in 2012. In Alaska, over 95 percent of ConocoPhillips' production is oil, with Alaska being about as pure of an oil area as the company has. So, when trying to compare oil producing regions to areas that include natural gas or are predominantly natural gas, it is very hard to get much information because it is an apples and oranges comparison. When comparing ConocoPhillips' activities in Alaska versus other places where it is making new investments, the data point to look at is the cash margin because the earnings reported in the Form 10-K represent the company's historical investments. In the last 12 years ConocoPhillips has invested over \$25 billion in Alaska, so earnings are generated from activities that have been done in the past. When looking at where ConocoPhillips is putting its new money, the company's cash margins in Alaska are currently in the range of \$30-\$35, but in the Eagle Ford and Bakken plays they are in the range of \$40-\$50; so, 40-50 percent higher margins from places like the Eagle Ford and Bakken where a significant part of ConocoPhillips' investment capital is going.

[7:47:23 PM](#)

REPRESENTATIVE TARR asked where cash-margin basis information could be found.

MR. HEINRICH responded analyst presentations done over the last couple of years are available on the Internet, but said he could

provide them. In further response, he confirmed they are from ConocoPhillips' presentations.

MR. JEPSEN added that ConocoPhillips' investor presentations are available on its public web site.

[7:47:56 PM](#)

REPRESENTATIVE TUCK noted Alaska is trying to figure out the sweet spot for itself in comparison to other places. Referring to [slide 4], he surmised fewer investments are happening in Norway and Indonesia than in Canada-Nova Scotia and Brazil.

MR. JEPSEN answered ConocoPhillips has invested in Norway for more than 30 years and has significant assets there. It would not be farfetched to say, he continued, that ConocoPhillips would make more investments there if Norway had a different tax regime. Alaska's tax framework is comparable to Norway's and ConocoPhillips still makes investments and is not walking away from Alaska. But a different type of tax framework is needed if Alaska wants to see more investment.

[7:49:08 PM](#)

REPRESENTATIVE TUCK recalled the 2001 [Gerking study] in Wyoming which concluded that doing anything with the production tax is inelastic in making changes in investments in that area. He understood that ConocoPhillips testified before the Senate that it planned on spending \$2.5 billion over the next 5 years. Given this, and what is being proposed under CSSB 21(FIN) am(efd fld), he asked how much more investment can be expected in Alaska.

MR. JEPSEN disagreed that taxes do not matter, pointing out that everyone has experience with his/her own taxes and it does make a difference. The ACES environment of being at the very top does make a difference and is a factor that determines the economics of individual projects. While he is unfamiliar with the aforementioned study, he said his opinion is that it makes no sense to say that taxes do not matter. The \$2.5 billion mentioned in the analysts meeting is the continuation of what ConocoPhillips has been spending for about the last 5 years on those same types of activities. How much more ConocoPhillips would invest would be a function of where the proposed bill actually ends up. Where the bill is right now is a positive start, he said, and he thinks some additional investment will be

seen. Any projects will have to be taken to the company's board for consideration along with other projects the company has.

MR. HEINRICH added that the roughly \$500 million referenced about ConocoPhillips' development projects in Alaska is only a part of its overall capital budget. In the last 3-4 years, ConocoPhillips has spent \$700-\$900 million and expects to spend similar levels with the current fiscal structure. The [spending above \$500 million] is going into maintenance and asset renewal work that is viewed as important to keeping existing production in a safe state as facilities reach ages of 30-40 years. Thus, ConocoPhillips has been spending much more than \$500 million.

[7:52:46 PM](#)

REPRESENTATIVE TUCK allowed he can see how the third portion of the GRE could be problematic. He asked whether there would still be the same amount of hesitation with ConocoPhillips' future projects as under ACES should CSSB 21(FIN) am(efd fld) be passed as currently written

MR. JEPSEN replied part of the message that ConocoPhillips has been trying to convey is that more investment would probably be seen with the changes on the table today. However, it would probably not be as much investment as everyone would like to see. He said he thinks changes could be made to this bill that will put Alaska in a more favorable position for investment and that will bring more investment.

[7:53:41 PM](#)

REPRESENTATIVE TUCK understood that ConocoPhillips, unlike other producers, separates out Alaska in its taxes. He inquired which years were the most profitable for ConocoPhillips in Alaska.

MR. JEPSEN responded the price of oil in the early 1980s was \$40 per barrel and ConocoPhillips was producing an awful lot of oil out of Alaska. To do that comparison he would have to go back and make some inflation adjustments; so he cannot readily answer the question as to what year has been the most profitable.

REPRESENTATIVE TUCK asked whether the question could be answered by which years in Alaska had the best cash flow.

MR. JEPSEN said his answer would be the same - prices and profits cannot be compared from one point in time to another

point in time 30 years later and have it be an apples-to-apples comparison.

7:55:16 PM

REPRESENTATIVE P. WILSON requested a description of what ConocoPhillips Alaska, Inc. goes through, what areas in the world it is up against, when it presents projects in Alaska to the board for consideration.

MR. HEINRICH answered the process has many metrics, some of which are confidential, but it is not just rates of return. The slate of opportunities is ever-changing, so on any given day it depends in part on what other opportunities the company can work itself into that may require capital. It is a changing process because ConocoPhillips comes into different opportunities and exits different areas as they get into different phases of their lifecycle.

REPRESENTATIVE P. WILSON requested further elaboration on where those other opportunities might be located throughout the world.

MR. HEINRICH replied his response is more around portfolio management. When looking at West Africa or Australia, the company is trying to balance many things, such as oil versus gas exposure and whether to shift the portfolio to being more oil in nature versus gas. Today, those investment dollars are going into liquid rich oil plays around the world as opposed to gas, which ConocoPhillips had made a conscious effort to get into through the mid-2000s and some of the company's projects in Australia came about during that timeframe. It depends on what the view is of the direction of the industry, prices, opportunities, and how ConocoPhillips wants its portfolio to evolve over time. Dispositions resulting out of that portfolio management also drive some of that.

7:57:50 PM

REPRESENTATIVE P. WILSON inquired whether portfolio management is the reason why ConocoPhillips cannot make a commitment about exactly what is going to happen. She said she is asking this question for the record given that some people have said they want certainty that things will increase in Alaska and are unwilling to do something unless there is a commitment.

MR. HEINRICH responded the recent analyst discussions show that ConocoPhillips' strategy is about increasing its exposure in oil

and increasing its overall margin contributions. That margin contribution is driving some dispositions for areas that are not generating high returns and driving investment into places that are. So, those two things actually favor the types of things that ConocoPhillips could do in Alaska.

MR. JEPSEN added the more Alaska is positioned to favor investment, the better it is going to fare in all those kinds of discussions. Even though a commitment cannot be made, it can be said that ConocoPhillips just had two major discoveries in the U.S. Gulf of Mexico, one of the best places in the world for investment. Those places are going to fare well no matter how the rest of the world changes. An idea he would put to the committee is to position Alaska such that investment is favored here over other opportunities.

[7:59:43 PM](#)

CO-CHAIR SADDLER asked whether ConocoPhillips can guarantee to anyone - its shareholders, its managers - that X amount of spending will result in Y amount of increased production.

MR. JEPSEN answered that is certainly talked about at analyst presentations. "We talk about we are going to make this kind of investment, we anticipate this kind of production. To say that that never happens is probably not accurate, but that is done in a very methodical basis after much review with our board of directors, with our executive committee. We are not here in a place today where we can say that, nor do we take these projects and have them matured to the point where we could say to our board or to our executive management 'this is something you ought to commit to doing.' So the things that you typically see in those presentations are things that we are pretty confident about. Right now, Alaska has been in a place where, quite frankly, I do not think as much effort has been put into trying to mature projects as you might have seen if we had a different tax framework."

CO-CHAIR SADDLER noted he has often heard that if Alaska reduces its taxes, the money that would be retained by the oil industry will be spent elsewhere. He inquired whether money is fungible or if investment in Alaska is made with Alaska-earned dollars.

MR. HEINRICH replied he does not believe ConocoPhillips actually tracks money in/money out, but said it is very natural in this industry that money moves across geographic boundaries. Forty

years ago, for example, the money to fund development of the assets in Alaska came from somewhere.

[8:01:42 PM](#)

CO-CHAIR SADDLER commented the committee has heard lots of dollar figures tossed around about the amount of spending on the North Slope that is currently taking place to keep the rate of decline at a certain point. He asked what ConocoPhillips' level of investment is to keep the decline rate at its current level.

MR. JEPSEN responded ConocoPhillips has invested around \$1 billion a year for about the last 3-4 years, and it can be seen the kind of declines that have resulted from that.

CO-CHAIR SADDLER inquired whether Mr. Jepsen or Mr. Heinrich is familiar with any taxing regimes that are predicated on new oil or that might have a better way of identifying new oil that the GRE exclusion could be applied to.

MR. JEPSEN answered nothing comes to mind that mimics the GRE.

[8:02:53 PM](#)

CO-CHAIR SADDLER asked how ConocoPhillips would deal with the third category GRE if it became law as currently written.

MR. JEPSEN replied he is "guesstimating" as to ConocoPhillips' behavior because there have been no conversations with the Department of Natural Resources as to how the department would try to apply it. But, he would say that it would be reasonably difficult for ConocoPhillips to prove or live up to the standard currently written into the bill. His guess is that it would not stimulate a whole lot of litigation - if ConocoPhillips found out that the interpretation of the Department of Natural Resources and Department of Revenue was such that the type of wells the company is planning on drilling would not qualify, then that is probably where the company would leave it.

MR. HEINRICH added that from an economic analysis perspective it would be real hard for ConocoPhillips to factor it into a decision-making process until there is clarity in the likely outcome. At best, it might get a footnote in the company's analysis until a point where there is confidence it is something that can be counted on for a particular type of project.

CO-CHAIR SADDLER surmised the ambiguity would cause a chilling factor.

[Response inaudible.]

8:04:35 PM

CO-CHAIR SADDLER inquired whether any of the other less critical provisions of CSSB 21(FIN) am(efd fld) raise any concerns.

MR. JEPSEN responded he concurs with ExxonMobil about the Competitive Review Board, adding it would take some time to see how that is going to work. He said the consultants advising the committee about how Alaska fares in terms of competitiveness are highly experienced and highly educated experts and the board, as currently set up, would not consist of those same people. There are also the issues around confidentiality and whether that board could make that judgment without the breadth of experience had by PFC Energy or Econ One Research. If it becomes an issue every year it becomes the center of at least the first 30 days of every session waiting for this report, which throws some uncertainty into it. While it may be just fine, he said there are certainly questions in his mind as to how it would work. He added that the other provisions mentioned earlier by Co-Chair Saddler generally do not apply to ConocoPhillips, so the company is relatively indifferent to those.

8:05:58 PM

CO-CHAIR SADDLER understood ConocoPhillips generally supports the work that the [legislature's and administration's] consultants have done. He asked whether there is any particular thing the company would like to draw attention to, highlight, dispute, or correct.

MR. HEINRICH answered he does not believe there is much disagreement, but the one area in which differences are seen is around the modeling work that goes into looking at the producer take. Because there are different assumptions there are differences between the different consultants, but it is not because ConocoPhillips does not understand potentially what those are. Generally speaking, the consultants have represented the case very well. Responding further, he confirmed the differences are in the assumptions used for the producer share or government take analyses. He said those analyses are very much dependent on the assumptions used for operating and capital expenses, tax rates, and effective tax rates. Some assumptions

might use a theoretical asset. ConocoPhillips uses the data from the Department of Revenue's sources book to model the industry. It is not to say any of the approaches are wrong, they just give slightly different variances.

[8:07:18 PM](#)

REPRESENTATIVE SEATON read from the aforementioned February 28, 2013, analysts meeting [report] in which it was stated that: there are numerous development opportunities in Alaska in and around the ConocoPhillips' existing assets from Prudhoe Bay to Kuparuk to Alpine and associated satellite fields; the company is applying high technology drilling capabilities so that investment results in an incremental 35,000 barrels a day by 2017, which mitigates the base decline in Alaska to about 3 percent a year; and this does not include the Alpine West major project, but when Alpine West is added the base decline is mitigated to about 2 percent a year. Because he heard 9 percent mentioned earlier, Representative Seaton said he would like to ask Mr. Jepsen and Mr. Heinrich whether they agree with the analysts meeting that this is what ConocoPhillips is currently projected to be doing.

MR. JEPSEN pointed out the previous answer was to a question dealing with natural decline in the fields when nothing is done after a well is drilled. Instead, ConocoPhillips is doing quite a bit more to maintain production in these fields by working over wells, fixing broken wells, and stimulating wells. New wells are also being drilled. A base of investment goes on to keep the decline from being at the rates talked about earlier; enhanced oil recovery (EOR) is a big component in trying to maintain production. He explained Mr. Fox was representing the agglomeration of all of ConocoPhillips' interests across the North Slope, and he does not take exception to what Mr. Fox said. It is a function of the performance that is being seen today and the historical investments the company has made and, hopefully, will be making in the future.

[8:09:26 PM](#)

REPRESENTATIVE TARR noted that during the time of the economic limit factor (ELF), some areas basically had no tax yet there was no explosion in investment. When asked about this before, people have responded that it had to do with the price of oil at that time. She requested Mr. Jepsen to comment on that in the context of what is being thought about today.

MR. JEPSEN presumed Representative Tarr is talking about the time period between 1996 and 2006. Displaying a chart that used data from the Department of Natural Resources to plot all the new fields brought on stream during that time frame, he said it amounts to about 260,000 barrels a day of production by the year 2005 or so. During that time frame, considerable investment was going on and considerable new production came on stream. Additionally, in existing fields like Kuparuk, ConocoPhillips was investing in wells and investing in EOR. The EOR project in Kuparuk was started in 1996 or 1997 and moved from being a small-scale project to field-wide, adding 25,000-30,000 barrels per day production. So, the comment that ConocoPhillips was not doing anything when ELF was low is simply wrong. A reason this may not have been seen in the decline is that Prudhoe Bay and Kuparuk are gigantic fields and their base decline is pretty steep. A million barrels a day naturally declining at 10 or 15 percent a year is a pretty steep hill to climb when it is doing that year in and year out. Given where things are at right now, there is probably the opportunity to offset the decline pretty significantly because the field rates are lot lower than they were back in that time frame.

[8:11:58 PM](#)

REPRESENTATIVE TARR requested the aforementioned chart be provided to the committee. She asked Mr. Jepsen to comment on the following statements from the study in Wyoming [2001 Gerking et al, abstract, page 1]:

A production tax rate increase is shown to decrease early period exploration effort, affect little change in reserve additions and future production, and substantially increase discounted tax revenue. Policy implications of this outcome suggest that state officials may consider raising production tax rates as a way to increase revenue while risking little in the way of loss to future oil activity.

MR. JEPSEN replied he will look at the study and get back to the committee with comments.

[8:13:28 PM](#)

CO-CHAIR FEIGE observed that slide 3 of yesterday's Econ One Research presentation shows the crossover between ACES and CSSB 21(FIN) am(efd fld) for government take to be about \$80 per barrel while the chart provided today on slide 3 by

ConocoPhillips shows it at approximately \$90 per barrel. He asked why this difference.

MR. HEINRICH responded that is what he was referencing earlier today when he said a lot depends on the assumptions used for operating costs, capital costs, state tax rates, and federal income taxes. ConocoPhillips modeled this data using the Department of Revenue's sources book information for the industry taxpayers, which he believes represents essentially producers and production on the North Slope. So, it may be a different set of data than the different consultants have used in constructing their models. Additionally, the ConocoPhillips chart specifically represents fiscal year 2014 as though CSSB 21(FIN) am(efd fld) were in effect for the whole fiscal year; it is not a five-year average or a full field-wide average. The reason for choosing to represent 2014 is because it is much nearer in time and therefore more accurate and a better portrayal of what can be expected in a given year as opposed to a five-year average or some other metric that does not relate to a specific year.

MR. JEPSEN pointed out that oil price inflated over time and then discounted back drives that crossover point lower; doing the discounted cash flow economics leads to a lower current oil price for a crossover point than if it is done as shown here in today's presentation. While it is complicated, it is part of the issue in terms of how different presenters present this data.

[8:16:33 PM](#)

REPRESENTATIVE SEATON understood, then, that in ConocoPhillips' modeling and decision making, the company is not looking at inflation factors and if the discount rate is used it is just the discount rate based on the nominal rate/nominal dollars.

MR. HEINRICH answered [the chart on slide 3] is an undiscounted view of the world for fiscal year 2014.

The committee took an at-ease from 8:17 p.m. to 8:27 p.m.

[8:27:36 PM](#)

DAMIAN BILBAO, Head of Finance, BP Exploration (Alaska) Inc., thanked all legislators for addressing the shortcomings of ACES and "working hard to meet the governor's principles of a simpler, fairer, more durable tax policy that attracts the

needed investment Alaska requires." These efforts indicate a common understanding of the seriousness that production decline presents to Alaska, most notably evidenced by the Trans-Alaska Pipeline System (TAPS) flowing three-quarters empty. He said CSSB 21(FIN) am(efd fld) is a step change from the current ACES policy and signals to investors that Alaska is serious about attracting investment to the state. However, while it is a step forward in making Alaska more attractive to investment, Alaska's geographic, technical, and cost challenges are such that the state may not want to be satisfied with settling on the upper end of average on the competitive scale. He urged the committee to consider opportunities for improving the bill's first two elements of base rate and credit per barrel, which he said cannot be decoupled, and its third element providing of gross revenue exclusion (GRE).

MR. BILBAO, referring to the only slide in his PowerPoint presentation, discussed what BP Exploration (Alaska) Inc. ("BP) believes the bill does well. Elimination of progressivity is a game changer, he said, and puts Alaska back in the game of competition of competition for investment. Progressivity has made Alaska noncompetitive for rate-adding investment that is needed to create a different decline curve than what is seen today and over the last several years. While BP recognizes that non-rate-adding investment, or rate sustaining investment, has continued, the large rate-adding investments that are necessary to create a different production profile going forward have gone elsewhere. Removing progressivity should make for a more productive discussion with potential investors in the Lower 48 who are not currently investing in Alaska and have found the tax policy to be complex and difficult to model. If one considers the number of players operating in areas like the Bakken and Eagle Ford relative to the number of investors in Alaska today, at today's prices this should be an item of both surprise and concern for the people of Alaska.

[8:32:06 PM](#)

MR. BILBAO pointed out that CSSB 21(FIN) am(efd fld) raises the base rate from 25 percent [as originally introduced] to 35 percent, but offsets this with a \$5 per barrel credit. He said it is important to recognize that those two elements are inextricably linked. The balance between the base rate and the credit is critical and must be maintained or the bill loses its effectiveness for investors. Furthermore, the focus of the credit shifts from being linked to investment to instead being linked to production - a clear message on policy priorities.

This shift in policy encourages a near-term focus on developing new production. The gross revenue exclusion provision could have a positive impact on near-term and long-term economics, he continued. Changing the GRE component to include the legacy fields was a significant shift because it targets where the opportunity is greatest.

MR. BILBAO added that an important point is CSSB 21(FIN) am(efd fld) simplifies Alaska's fiscal system, allowing for greater certainty around planning and analyzing projects. For example, inefficient elements of administering ACES are removed. He reminded members of testimony provided by Tom Williams, former commissioner of the Department of Revenue, in which Mr. Williams explained how calculating the progressivity tax under a price that changes over the course of the year may result in a tax payment more than 50 percent higher than a payment where the average price is actually the same but with less volatility throughout the year. It makes it very difficult to plan BP's business when something entirely beyond BP's control such as the volatility of price, much less the change of it, can so significantly impact the company's cash profile. Continuing, he said CSSB 21(FIN) am(efd fld) proves to board rooms worldwide that Alaska is serious about competing and attracting investors. When investors look at where to invest, they consider not only the fiscal climate, but also the commitment to be competitive, which is something this bill signals very clearly. Lastly, the bill levels the playing field and moves away from picking winners and losers by providing a more level playing field and encouraging all the players to pursue all the projects that are economically competitive.

[8:35:43 PM](#)

MR. BILBAO next addressed where BP believes the bill can be improved, saying the [35 percent] base rate would be challenging at lower prices. He recounted testimony in which [the administration's consultant], Barry Pulliam [of Econ One Research], stated that at \$80 per barrel, CSSB 21(FIN) am(efd fld) is less competitive than ACES. In 2010, ANS West Coast prices averaged around \$80 per barrel; given this was not very long ago, BP encourages the committee to consider the impact of the bill at prices below \$100. The current GRE is an improvement to the original bill, he continued, because its focus now includes the development of resources inside the legacy fields. However, BP would encourage the committee to improve how the GRE is applied and how parties can rely on it when they run their economics. The GRE applies at the

discretion of the Department of Revenue and the Department of Natural Resources. It must be considered that it takes many years for a project to make its way through the conveyor belt of opportunity - from when BP first decides to dedicate resource to the project to when it actually gets sanctioned. As currently written, it is uncertain whether the project can benefit from the GRE. Whether that decision is made earlier on when the resources are dedicated to begin to look at a project or later on when the project is sanctioned, which may be years, it is important that those two decisions remain consistent even though many years have passed in between both points. More certainty is needed in this provision so BP can have confidence that the GRE assumption should be included in its economic modeling.

MR. BILBAO concluded by stating that BP believes CSSB 21(FIN) am(efd fld) puts Alaska back in the game and creates a simpler and more balanced system. He encouraged members to consider BP's suggestions for improving the bill and said BP looks forward to supporting the committee as this process continues.

[CSSB 21(FIN) am(efd fld) was held over.]

[8:39:13 PM](#)

#### **ADJOURNMENT**

There being no further business before the committee, the House Resources Standing Committee meeting was adjourned at 8:39 p.m.