

SENATE FINANCE COMMITTEE
March 5, 2013
9:07 a.m.

[9:07:18 AM](#)

CALL TO ORDER

Co-Chair Kelly called the Senate Finance Committee meeting to order at 9:07 a.m.

MEMBERS PRESENT

Senator Pete Kelly, Co-Chair
Senator Kevin Meyer, Co-Chair
Senator Anna Fairclough, Vice-Chair
Senator Click Bishop
Senator Mike Dunleavy
Senator Lyman Hoffman
Senator Donny Olson

MEMBERS ABSENT

None

ALSO PRESENT

Kara Moriarty, Executive Director, Alaska Oil and Gas Association; Damian Bilbao, Director of Finance, British Petroleum; Dan Seckers, Tax Counsel, ExxonMobil.

SUMMARY

SB 21 OIL AND GAS PRODUCTION TAX

SB 21 was HEARD and HELD in committee for further consideration.

#sb21

SENATE BILL NO. 21

"An Act relating to appropriations from taxes paid under the Alaska Net Income Tax Act; 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; relating to the determination of annual oil and gas production tax values including adjustments based on a percentage of gross value at the point of production from certain leases or properties; making conforming amendments; and providing for an effective date."

9:07:41 AM

Co-Chair Meyer discussed the agenda for the day. He noted that increasing oil production in Alaska was the top priority.

KARA MORIARTY, EXECUTIVE DIRECTOR, ALASKA OIL AND GAS ASSOCIATION (AOGA), introduced herself and shared information about the organization. She provided a PowerPoint presentation titled "Oil and Gas: Fueling Alaska's Economy" dated March 5, 2013 (copy on file). She read from a prepared statement titled "AOGA Testimony to Senate Finance on CSSB 21(RES)" dated March 5, 2013 (copy on file):

The industry's greatest challenge today, which we share with the State is the decline of oil production from the North Slope. We believe that the greatest, most urgent issue facing this Legislature in 2013 is how you will address this problem. We cannot fix the basic, inherent properties of any oil and gas field, that is that the resource is finite and production will eventually decline. We can fix some of the economic principles that drive the development of more and new resources. Corrections to the ACES tax regime will remove impediments to development and exploration and assist the industry in investing in projects that could both extend the life of TAPS and open up new resources to long term development. When we look to the future Alaskans see a robust industry on the North Slope growing like it is the rest of the United States. We want the jobs here and not in the Lower 48. We want to create developments that will last for decades more, creating jobs for our children and

opportunities for our communities to flourish. Alaskans want to see the industry continue to support the education and skills training that are needed to qualify for many of those jobs. A healthy oil and gas industry is one that sees the economic benefits of continuing to invest in projects in Alaska and keeping its employees here, where they volunteer their time, talent and treasure to make Alaska a better place to live for us all.

Ms. Moriarty addressed "The Tax "Give Away" Fallacy" (page 2 of the prepared AOGA statement):

We hear all too often of the \$2 billion dollars that will be a "give away" to the industry should the tax regime be changed. It is a simple and effective communication that completely misstates the reality of the tax structure and its impact on the industry. It is simple to calculate how a change in a tax rate will impact amount of taxes collected if all "other" things remain constant. For example, if production does not decline further, if lifting costs don't rise, if the \$2 billion dollars of annual investment by the industry to slow that decline continues, and if oil and gas prices do not shift. All of these "other" items seem to be considered a given in these calculations and it is assumed they will remain unchanged in the future - the pundits of the "give away" theory want you to believe it's that simple. But it is not.

However resourceful the State's revenue estimators are, they cannot control decline, lifting costs, future investment, or the price of crude oil. As the rest of the nation swims in new industry investment and development, Alaska languishes. The costs of operations continue to rise as North Slope fields decline. The \$2 billion a year of industry investment spent in wrestling decline must now compete with more lucrative projects elsewhere, and with growing US production and supply of oil and gas and the future price of that oil and gas is anyone's guess. Naysayers to these necessary and fundamental changes to our tax structure look only to the downside simple calculations they take from a Revenue Sources Book they forget is only a "guesstimate" of future revenue. The upside potential of that change, though, is very

real. If a restructuring and tax rate reduction make investments here more competitive, companies will want to make more investments here for that upside. Deciding to make long-term investments in Alaska's North Slope requires the industry to see potential upside to their investments and assessing the essential risks of those investments are offset by the opportunities afforded in success. Without that potential opportunity in Alaska, investment dollars will be spent elsewhere, where risks are less and opportunity is greater.

[9:12:21 AM](#)

Ms. Moriarty spoke to "Core Principles to Address North Slope Production Decline" on page 3 of the AOGA statement:

As you consider potential solutions to the challenge that production declines creates for Alaska, AOGA believes Governor Parnell's four "core principles" offer an excellent cornerstone for this:

- First, tax reform must be fair to Alaskans.
- Second, it must encourage new production.
- Third, it must be simple, so that it restores balance to the system.
- Fourth, it must be durable for the long term.

We believe the addition of a fifth such principle would be required to meet Alaska's goals, because the challenge is not that there are too many companies pursuing opportunities, but that there are too few. Alaska should therefore avoid tax changes that artificially create "winners" and "losers."

Ms. Moriarty shared that she would speak to several features of the CS and would outline some of the issues that it did not address.

[9:13:21 AM](#)

Ms. Moriarty discussed slide 6 of the PowerPoint presentation titled "CSSB 21(RES) Component: Progressivity" and continued reading from page 3 of the AOGA statement:

AOGA endorses the elimination of progressivity. The impact of Progressivity as part of the ACES tax rate in industry investment decision making is the single

most influential component of Alaska's tax structure negatively impacting investment decisions related to Alaskan projects. Taxes are paid by the industry in virtually every jurisdiction in which we function and so we are very familiar with how they work. But the uniformity and consistency in the application of tax impacts as they relate to investment decision making found in almost every jurisdiction is missing in Alaska. As my member companies have testified in the past, investment decisions are driven by combining high and low case scenarios where costs and revenues are estimated and best case cash flows and worst case cash flows are measured, risked and analyzed. Each potential project, in every jurisdiction, is measured and compared and only some are funded. As your consultant, Roger Marks pointed out yesterday, the international investment climate is characterized by plenty of opportunities, fluid capital, but finite capital. To choose what they can and cannot fund, companies have compared each potential project, no matter the jurisdiction, by application of a uniform investment decision measuring formula. When Alaska's tax system is quantified and added to this measure for proposed Alaskan projects the best cases are always burdened with an excessively high tax rate and as the assumed high cases get better, the burden only increases.

Progressivity brings extraordinary complexity to the tax, not only in calculating what the tax is, but also in analyzing what the amount of the progressivity is for any particular item that affects a taxpayer's Production Tax Value (PTV). This complexity exists because the tax rate for progressivity depends on the taxpayer's PTV per barrel, and then the resulting rate is applied to the very same PTV that set the rate. This circularity in the tax calculation leads to bizarre effects. For instance, simply the fact that oil prices fluctuate during a year instead of remaining perfectly flat increases the tax due even though the average of the fluctuating prices is the same as the flat price - and the greater the fluctuation, the greater the tax from progressivity becomes. There is no objective economic or financial reason for the tax to go up; instead, this occurs entirely because the progressivity calculation is circular.

The repeal of progressivity is consistent with all four core principles outlined above. Its removal improves fairness because operators that increase margins through efficiency would no longer be automatically penalized. Its removal encourages new production because it reduces the tax burden on investment, as discussed above. Its removal is a significant step toward simplicity. And, lastly, its removal enhances durability because it satisfies the three preceding core principles.

[9:16:54 AM](#)

Ms. Moriarty moved to slide 7: "CSSB 21(RES) Component: Increasing the Base Tax Rate" and read from page 4 of the prepared AOGA statement:

AOGA does not endorse increasing the base tax rate to 35%. Let's go back to the industry investment decision process again. Increasing the base tax rate, besides burdening every investment case with a higher tax rate, now adds an additional burden to the worst case scenarios when oil prices are low or project costs are high. When applying the current base tax rates to the investment cases for a proposed project, until one assumes a price collapse occurs and the minimum fixed rates apply, even when little revenue is assumed to be generated, the base tax applies. The burden of a 35% versus a 25% rate is easy to envision as every middle case and every worst case scenario is burdened with an additional 10% tax rate. This assumed cost will negatively impact the potential returns deemed available for any Alaskan project and drive investments to be made elsewhere. Increasing the base tax rate is contrary to the second core principle; there is not any reasonable argument that suggests increasing the base tax rate would encourage new production.

Ms. Moriarty added that beginning in 2007, AOGA had vocalized that the 25 percent base tax rate was too high. She turned to slide 8: "CSSB 21(RES) Component: Tax Credits" and read from page 5 of the AOGA statement:

In general, tax credits, because they act to offset a part of the costs of certain investments when the

expenditure is made are an important tool in reducing the deemed risks of those expenditures. Industry makes investments to seek returns. Costs of any kind, including taxes reduce those returns, so the offset of tax cost by a tax credit provides immediate benefit to the investment return calculation. Whether those costs are for drilling a well, building a facility to gather new oil, or installing a pipe to gather oil, a tax credit represents an immediate and direct reduction in the amount that a potential investor puts at risk in spending money on equipment and facilities that benefit production.

Those tax credits are directly related to production as investments must actually be made for the credit to be utilized and those investments will positively impact production. It is important to note that there is no tax credit liability for the State at all until an investor invests here. The investment has no other purpose than creating return by positively influencing production. So it costs the State nothing to offer the credit until the investment is made and at that point the tax credit has already succeeded in what it is supposed to do - namely to attract investment dollars here for investments that will act to increase production and reduce decline.

Ms. Moriarty discussed the proposal to repeal the Qualified Capital Expenditure (QCE) tax credit on page 5 of the prepared AOGA statement:

A. Repeal of the Qualified Capital Expenditure ("QCE") Tax Credit.

AOGA does not support the repeal of the Qualified Capital Expenditure Tax Credit. Even while the elimination of progressivity would improve the competitiveness of Alaskan investments from the present ACES tax, the elimination of the QCE Credit would claw back one important financial incentive and a part of ACES that actually acts to improve the competitive environment. The QCE Credit depends entirely on how much is invested here, and provides benefits for investments even when oil prices are lower. While the benefit from ending progressivity, which depends on the price of oil relative to a producer's lease expenditures, helps when oil prices

are higher the QCE provides benefits when prices are not. In this mid-range of oil prices the loss of QCE Credit would outweigh the benefit from the end of progressivity.

Repeal of the QCE credit is contrary to the second core principle. Furthermore, because every producer's costs are different and prices will impact them differentially AOGA, fears the repeal of the QCE Credit is worse than creating "winners" and "losers" because it only creates "losers" artificially among producers, and we see no sound tax policy justification for doing so.

For these reasons, AOGA believes the elimination of the QCE tax credits would be a mistake. Instead of that, one possibility might be to expand the scope of the "well lease expenditure" tax credit under AS 43.55.023(1) so it is available to producers on the North Slope. This credit has several meaningful advantages. First, it focuses investment incentives on subsurface intangible-drilling expenditures, which are a reasonable proxy for direct spending on well activity and, in turn, production. Second, the credit is clear because it uses already established concepts in the federal Internal Revenue Code. Third, it is fair because it applies equally to well-related spending in all areas of the state, without creating winners and losers merely on the basis of geography.

Ms. Moriarty noted that the well lease expenditure credit was used heavily in Cook Inlet.

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Ms. Moriarty detailed slide 9: "CSSB 21(RES) Component: Tax Credits" and read from page 6 of the prepared AOGA statement:

B. The \$5 dollar per barrel tax credit.

AOGA is not certain that the potential benefit of a \$5 dollar per barrel tax credit under AS 43.55.024(i) will be offset by other burdens.

There are multiple issues to balance when taking in the numerous proposed changes found in CSSB21. The

removal of progressivity, the increase in base rate, early sunset of the QCE credit all create interrelated issues and while a \$5 dollar per barrel tax credit would provide benefits both in real tax costs and in investment decision making, the weight of the benefit in respect to the other changes is hard to measure. AOGA applauds the concept of tying incentives to the goal of increased production and as such allowing a tax credit per barrel. One must consider, though, what the \$5/bbl credit will mean to a small producer with little production as opposed to the legacy producers that already have established large scale production. In view of the investment decision making process and the Alaskan tax structure's impact on it, we are not certain that this benefit is offset by the other burdens contemplated when striving for the goal of increasing production.

Ms. Moriarty addressed slide 10: "CSSB 21(RES)/Component: Tax Credits" and read from on page 7 of the prepared AOGA statement:

C. Small-Producer and Exploration Credits.

AOGA endorses the proposal to extend the small-producer tax credit under AS 43.55.024 and exploration tax credits under AS 43.55.025 from the present sunset dates in 2016 to a later date.

The State had sound policy reasons for creating these small producer and exploration tax credits, and those reasons are just as valid today as they were then. AOGA believes these credits have increased the likelihood of participation by new industry players and act to increase the opportunities that could be found by expanding exploration. The purpose of the small-producer tax credit was to attract new players to Alaska who might otherwise have been deterred from coming here by presumptions of increased risks and of higher-than-average costs and expenses. The success of the credit in attracting new participants is a fact that cannot be denied. AOGA sees this success in its own membership, and in other companies that have come here and are now active. Smaller producers often have a different perspective about the opportunities around them, and as such can bring with them new ideas and opportunities. New participants with new ideas can

only strengthen and improve the Alaskan petroleum industry and help the state stem the decline in production. We know from testimony that the small producer tax credit has made a material difference in individual companies' decisions to do business and invest in Alaska.

The purpose and justification for the exploration tax credits under AS 43.55.025 are equally clear. Huge parts of this state remain unexplored or underexplored. Again, these tax credits are only earned when actual expenditures for exploration occur. The credits tangibly reduce the risks faced by an explorer and as such incentivize them to go out and search for oil and gas that is much needed. Increased exploration leads to increased development and these credits act to increase exploration and should be extended as well. Just as with the QCE credits for capital investments, there is no exploration tax credit without real money having first been spent on exploration work that qualifies for these tax credits.

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Ms. Moriarty turned to slide 11: "CSSB 21(RES) Component: Tax Credits" and read from pages 7 and 8 of the AOGA statement:

D. Limiting the transferability of "carried-forward annual loss" tax credits.

AOGA does not support the limitation on transferability of these losses. We have some reservation about the proposal to bar almost completely the transferability of the current "carried-forward annual loss" tax credits under AS 43.55.023(b). New participants and new explorers are many times not yet producing in the state or only producing small volumes of oil and gas and as such have little or no production tax liabilities. The ability to transfer their losses to others allows them to monetize the investments they have already made, both reducing their cost exposure on the original expenditure and hopefully at the same time acquiring additional capital for more investment. These credits arise every year for any active explorer until it finds oil or gas and finally incurs production taxes

to apply the credit against. At present explorers can only realize immediate benefit from these credits by selling them to other taxpayers or cashing them in at the state Oil and Gas Tax Credit Fund established in AS 43.55.028.

Under the Bill as proposed, transfers would cease and explorers would have to hold on to losses for up to 10 years for possible use against taxes on their own production. The potential that a loss could not be offset against tax expenses or monetized in the near term places more risk on the decision to invest and as such makes such activities less likely to occur. If the transferability must cease, then the cost of the expiration of the loss carry forward after only 10 years, where on the North Slope exploration success to production can easily take longer, is another factor that negatively impacts investment decisions. Although the annual addition for interest will allow the losses to retain some value, we also believe that a 15 year period before expiration of the loss carry forward is the minimum timeframe that should apply if transferability is removed.

[9:27:29 AM](#)

Ms. Moriarty moved to slide 12: "CSSB 21(RES) Component: Tax Credits" and read from pages 8 and 9 of the AOGA statement:

E. The "Anti-stackable" section

AOGA does not think this new section is necessary. In Section 22 of the CS, AS 43.55.025 is amended by adding a new subsection to read:

(q) An exploration expenditure incurred after December 31, 2013, to explore for oil or gas located north of 68 degrees North latitude that is the basis for a credit under (a)(1), (2), or (3) of this section may not also be the basis for a credit claimed under AS 43.55.023 or this section.

AOGA does not understand why this new section is being proposed as it is our understanding the concern this

new language is to trying address is already covered in existing statutes.

F. New credit for Manufacturing

AOGA supports the new proposed manufacturing credit. Although this credit is directed to the incentivizing of development and manufacture of drilling and exploration methods and materials, it may not have a great impact on the reduction of the current production decline. However, it is a step in the right direction to incentivize jobs and additional investment, and having more jobs and investment in Alaska is never a bad thing.

[9:28:54 AM](#)

Ms. Moriarty discussed slide 13: "CSSB 21(RES) Component: Gross Revenue Exclusion (GRE)" and read from page 9 of the AOGA statement:

4. Gross Revenue Exclusion.

AOGA endorses the proposed 30% gross revenue exclusion or GRE, but has concerns on breadth of applicability. The GRE would, in calculation of the taxable Production Tax Value, exclude 30% of the Gross Value at the Point of Production of what we'll call "non-legacy" production. Thus the GRE provides incentive for finding new oil and getting it produced. As much as AOGA supports this proposal we are also concerned that it is too narrowly focused. This narrow focus and application to only certain areas, especially those outside existing Units where the best prospects of new oil are likely to be found, needlessly restricts the benefits that such a proposal could have on increasing production. Fields likely to lose out on getting any GRE are Prudhoe Bay, Kuparuk, Lisburne, Milne Point, Endicott, Niakuk, Point McIntyre, and Alpine; as well as the Prudhoe Bay satellite fields Aurora, Borealis, Midnight Sun, North Prudhoe Bay, Orion and Polaris and the Kuparuk satellites Meltwater, NEWS, Tabasco, Tam and West Sak.

Econ One Research, Inc. has previously provided this body a presentation entitled Analysis of Alaska's Tax System, North Slope Investment and The

Administration's Proposal, HE 72. In that presentation oil and gas resources described as "Economically Recoverable @ \$90/bbl" total 29.1 billion barrels of oil and barrel-equivalents of gas of which 3 billion are in the central North Slope where all the currently producing and therefore ineligible fields are. Of this 3 billion barrels, an estimated 2.5 billion or more stands to come from Prudhoe Bay, Kuparuk and other legacy fields already in production. The Governor's second "core principle" for tax legislation is that "it must encourage new production." But, in order to get results from such encouragement, the tax legislation must incentivize the best opportunities that Alaska has for getting results. The GRE as proposed may get some results but in terms of what it attempts to "encourage," it leaves out at least 80 - 90 percent of the 3 billion barrel opportunity in the central North Slope that Econ One has identified.

AOGA is continuing to search for ways to adapt the Gross Revenue Exclusion to include legacy fields in a way that might be acceptable to the Administration and the Legislature. It may turn out, however, that a different approach may be necessary to "encourage new production" from legacy fields.

[9:31:07 AM](#)

Ms. Moriarty pointed to slide 14: "CSSB 21(RES) Component: Competitiveness Review Board" and relayed that AOGA did not support the concept. She read from page 10 of the AOGA statement:

Oil and Gas Competitiveness Review Board

The proposed Board provides an oversight and review process that we believe would be burdensome to the industry and contravenes the Governor's principles relating durability in the long term. The perspective that the proposed changes found in the Bill would provide a long term solution to problems we know exist are placed in jeopardy because the very certainty that is required for sound investment decision making would be placed in question with each annual report of the Board. Instead of moving forward with projects that might help stem decline, industry resources would be used to assist the Board in collecting and

understanding complex information of long term consequence on a quarterly basis. Finally, the documentation and information the Board might request or require is of the highest proprietary value to oil and gas companies and confidentiality concerns and related complexities would hinder the efforts of the industry as well as the Board. While we appreciate the ability to represent industry on the proposed board, our concerns cause AOGA to question both the viability and the effectiveness of the proposed Board and as such we cannot support its proposed formation.

[9:32:44 AM](#)

Ms. Moriarty detailed slide 15: "Components Not Addressed in CSSB 21(RES)" and read from pages 10 and 11 of the AOGA statement:

There are several significant problems in the present ACES tax that are not addressed in CSSB 21, and I will address a few of them this morning.

A. Minimum tax for North Slope production. AS 43.55.011(t) sets a minimum tax that is targeted solely against North Slope production. That tax is based on the gross value of that production instead of the regular tax based on "net" Production Tax Value. The rationale for adopting it was to protect the State against low petroleum revenues when prices are low.

The minimum tax only complicates potential new investors' analyses of what their tax would be if they invest here instead of someplace else, and consequently it has, if anything, driven investments away. AS 43.55.01 1 (t) should be repealed or consideration given to significantly reducing the rate of the minimum tax.

B. Statute of limitations & statutory interest. Here we have two concerns that are interrelated, but not in an immediately obvious way.

The statute of limitations under AS 43.55.075(a) is six years from the date when the tax return was filed for the tax being audited, while the limitations period for other taxes under AS 43.05.260(a) is three years from the filing date of the tax return. Under

both statutes, the period may be extended by mutual consent of the taxpayer and the Department of Revenue (DOR).

The statutory rate of interest under AS 43.05.225(1) for tax underpayments is "five percentage points above the annual rate charged member banks for advances by the 12th Federal Reserve District as of the first day of that calendar quarter, or at the annual rate of 11 percent, whichever is greater, compounded quarterly as of the last day of that quarter[.]" Currently the Federal Reserve rate is very low, so 11% APR is the applicable rate.

We are asking that, if the Department chooses to not exercise its authority in providing certainty to the taxpayer to allow them to be able to calculate the correct amount of tax due, then the doubling-up of that uncertainty through statutory interest should be lessened - either by shortening the period for making Department "determinations" from six years back to the usual three, or by eliminating the 11% minimum interest rate on the statutory interest rate, or both.

C. Joint-interest billings. Our concern about joint-interest billings is also primarily a problem caused by the approach the Department has chosen to take with its tax regulations. Instead of starting with the joint-interest billings that participants in a unit or other joint operation receive from the operator, the regulations reflect an assumption that each non-operating participant has information, in addition to the operator's billings to them, that allows them to determine which expenditures are deductible as allowed "lease expenditures" under AS 43.55.165 and which are not. This assumption is wholly unrealistic. And even if there were some merit to it, the regulations opt to audit each participant separately regarding that participant's interpretation of which expenditures are deductible and which are not, instead of auditing the system of accounts used by the operator and telling all participants which cost items in that accounting system are deductible and which are not. In other words, instead of one audit of the expenses by a joint venture for any given period, the Department audits each participant separately for its respective share of the same pool of expenses.

We are not asking for legislation to put the Department's regulations on a different track. But there are some in the Department who believe that the repeal by the 2007 ACES legislation of AS 43.55.165(c) and (d) -which specifically authorized the Department to rely on joint-interest billings means the Department cannot legally rely on them now. While we disagree with this position (which is also at odds with what the Department testified to during the enactment of the 2007 ACES legislation), we do think it would be appropriate to restore language specifically authorizing the Department to rely on joint-interest billings if it chooses to do so.

[9:37:11 AM](#)

Ms. Moriarty concluded with slides 16 through 17: "AOGA Supports Components of CSSB 21(RES)" and "AOGA Concerns with CSSB 21(RES)." She read from page 12 of the AOGA statement:

We support the proposed elimination of progressivity, but we have great concern with the increase in the base tax rate to 35%, and with the mixed proposals for tax credits allowing a new \$5 per barrel credit but removing qualified capital credits. The trade-off between repealing progressivity and losing the QCE credit is not a net benefit for industry at low oil prices, and will create a greater barrier to investment from existing and new independent players.

We also agree with the comment by Roger Marks yesterday when in one slide he pointed out the tax system should not favor investing in certain cost fields over others, which in our view is the same as saying we encourage the legislature not to devise a tax system that creates "winners" and "losers".

The concept of the Gross Revenue Exclusion has considerable potential, but its narrow focus misses 80 -90 percent of the opportunity in the central North Slope described by Econ One. We will continue to work with you and the Administration to find a fair and reasonable way to expand its scope, or to find an alternative that will address the central North Slope appropriately.

The reasons that led the State to create the small-producer tax credit under AS 43.55.024 and the exploration tax credits under AS 43.55.025 remain valid today. We are pleased that CSSB21 will provide some minimum extension to the sunset date for the small-producer and exploration tax credits.

We believe it is up to you, and the Governor, to shape a competitive oil fiscal policy that is supported by strong principles that will work to arrest North Slope production decline and will lead Alaska towards a prosperous future for the long-term. Overall, the Bill represents a base for significant and crucial tax structure reform that move toward Governor Parnell's four "core principles" - fairness for Alaskans, encouraging new production, simplicity with balance, and durability for the long term, but as I have outlined today, AOGA members believe there is still many structural changes that should be included for this bill to truly change investment behaviors to the benefit of Alaskans. You have a difficult task ahead and AOGA stands ready to assist you throughout this process.

[9:38:39 AM](#)

Co-Chair Meyer recognized that AOGA did not support progressivity and surmised that the organization did not support a bracketed progressivity. He opined that progressivity was currently out of control. He asked whether AOGA would want a mechanism in place to address high oil prices. He believed the failure to address the issue currently meant it would need to be addressed at a later time, which may not be advantageous. He believed that oil companies would take comfort that Alaska had addressed prices on the high-end with the bracketed progressivity, showing that it had a more stable tax policy than other investment locations.

Ms. Moriarty responded that the challenge was for the state to create the policy it wanted for a range of prices. She stated that AOGA supported the elimination of progressivity, but the organization had supported bracketing in the past depending on the tax structure. She added that AOGA's preference would be no progressivity. She recognized that the policy call was difficult to make.

9:41:03 AM

Co-Chair Meyer asked which of AOGA's suggestions was more apt to achieve the goal of increasing oil in the pipeline. Ms. Moriarty responded that the best strategy was a more competitive tax system. She relayed that it was difficult to pick one component of a tax system and encouraged relying on the legislature's consultants. She shared that AOGA members had communicated the importance of competitiveness with other investment locations. She pointed to several challenges facing Alaska including distance-to-market, high cost environment, and other. She stressed that the most competitive environment would result in the most production.

Senator Dunleavy asked whether the AOGA membership had discussed other policies that may impact the desire to invest in Alaska. He wondered if AOGA members believed that the state's spending policy or any other behaviors were a deterrent to investment.

Ms. Moriarty responded that several factors were out of the state's control including the high cost environment, distance-to-market, and other; however, taxes and regulation were controllable. She relayed that AOGA member's felt that the current tax structure was the largest impediment to increasing investment and production. She noted that other issues could be improved, but increasing the competitiveness of the tax structure would make the most significant difference.

9:44:56 AM

Senator Bishop requested a copy of Ms. Moriarty's testimony. Ms. Moriarty replied that she would provide the testimony to the committee.

Senator Bishop asked for upcoming testifiers to show what increased investment and production would look like if competitiveness increased.

9:45:58 AM

Senator Hoffman discussed that most members felt the need to examine the progressivity aspects of the bill. He referred to prior testimony by PFC Energy that there were

jurisdictions looking at forms of progressivity, primarily to address times when oil prices were high. He believed there was value in considering the issue in order to avoid further deliberation about oil taxes in the future. He recalled that changes had been made to the tax structure many times in the past. He believed there was potential to consider progressivity; he was dismayed to see that AOGA did not support any forms of progressivity. He believed the option could help to avoid revisiting tax structure issues in the future. He pointed to numerous slides in the AOGA presentation that expressed various forms of opposition to the current and proposed tax structures. He wondered whether AOGA believed there were components in the CS that would work.

Ms. Moriarty replied that slide 16 summarized the components of the legislation that AOGA supported; slide 17 outlined its concerns. The organization recognized that the legislature would make changes and form what it felt was the best policy for the state.

Senator Hoffman observed that the governor and the Senate Resources Committee had both presented a bill that they believed represented the best policy for Alaska. He perceived that AOGA was vastly opposed to major portions of the current version of the bill.

Ms. Moriarty agreed that AOGA had concerns with some of the components included in the current bill. The organization believed that there were structural changes that would allow a more competitive environment for oil production in Alaska; AOGA did not believe the current bill would meet the legislature's expectation of a significant change in investment behavior. The organization had concern over portions of the original bill as well. She stated that AOGA looked forward to working with the committee and the legislature to create the best tax policy for Alaska.

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Senator Hoffman wondered whether AOGA had addressed how much investment would be required to increase oil production and what the range would be. He recalled that the legislature had discussed making similar changes to the tax structure on April 16 of the prior year. He relayed that Dale Pittman of ExxonMobil had testified; he cited a question that had been posed to Mr. Pittman:

Taking into consideration the bottleneck in the processing facilities and other technological challenges in recovering more oil regardless of the tax rate, how much investment do you believe is needed to increase production so we can stabilize the flow in the pipeline and if possible reach 600,000 barrels a day?

Senator Hoffman shared that Mr. Pittman had stated that it would require an investment of \$3 billion to \$5 billion per year to have enough new production to stabilize the flow rate.

Ms. Moriarty stated that AOGA was unable to weigh in on some issues on investment levels, price forecasts, and other due to antitrust reasons. She relayed that the two most recent fields (Ooguruk and Nikaitchuq) had cost approximately \$1 billion; the fields were producing 10,000 to 15,000 barrels per day. She had heard Mr. Pittman state that three or four fields like Ooguruk and Nikaitchuq would need to come online each year if the production decline was 40,000 barrels per day per year.

[9:53:22 AM](#)

Senator Hoffman believed that a cost of \$3 billion to \$5 billion in order to increase production to 600,000 barrels per day was a staggering number. He did not know if the amount would be achievable through any legislation.

Co-Chair Meyer offered that Senator Hoffman's questions would be good to pose to the industry during its testimony throughout the day.

Senator Olson discussed testimony from a consultant that the continuation of the 20 percent capital credit would provide more investment incentive than the GRE. He asked for AOGA's perspective. Ms. Moriarty replied that if the GRE was expanded it would work like a 20 percent tax credit in some ways. She stated that it was difficult to say which option would be preferable without seeing the other tax structure components as well.

[9:55:30 AM](#)

Senator Dunleavy stated that one of the cornerstones of the governor's proposal was to allow durability into the

future. He wondered how AOGA would construct a durable policy without some form of progressivity and flexibility.

Ms. Moriarty answered that it was important to take an entire policy into consideration. She stated that other tax regimes that AOGA's members competed against did not change from year to year. She referenced the effectiveness of a prior Econ One slide showing how current investments had changed in Alaska compared to the Lower 48 and internationally as the price of oil increased. She communicated that the other regions were seeing major new investment, whereas investment levels in Alaska had remained relatively flat. She stated that a durable tax policy would offer the industry a return on its investment and a steady cash flow to the state for the long-term.

[9:57:59 AM](#)

Co-Chair Kelly discussed slide 59 of a prior PFC Energy presentation that focused on reimbursing the royalty and ad valorem tax related to government take [PFC Energy presentation: "Senate Finance Committee: Alaska Fiscal System Discussion Slides" dated March 4, 2013]. He suggested that Alaskans wanted predictable and reasonable systems that allowed for a generous government take. He asked AOGA to analyze the slide and follow up with the committee.

Ms. Moriarty agreed.

[9:59:26 AM](#)

Vice-Chair Fairclough echoed an earlier request for a copy of Ms. Moriarty's prepared remarks. She pointed to slide [15] titled "Components Not Addressed in CSSB 21(RES)." She asked the department to provide its understanding of the reliance on the joint interest billing. She believed the goal was to save the department from reinventing the wheel every time it audited a particular section of findings. She spoke to statutory limitations and cautioned that DOR had provided an example related to the transition from the Petroleum Production Tax (PPT) to ACES; Federal Energy Regulatory Commission (FERC) findings and transportation costs had changed. Additionally, in 2010 structural changes related to amounts owed continued to result from the 2007 tax return. She communicated that if the system continued on a net profit tax, the auditing division needed

sufficient time for the work. She believed that unless there was a move to a gross system, moving the number was unadvisable.

Vice-Chair Fairclough addressed slide 14 related to the competitiveness review board. She wondered whether the Alaska Oil and Gas Conservation Commission (AOGCC) would be an appropriate venue for the board. She had envisioned that the entity would be an investment board that would look at beneficial partnerships for Alaska versus looking at the state's global competitiveness. She believed that AOGCC had the confidence of the industry and legislature in its review of oil and gas statistics and the function of how wells operate. She was interested to know whether varied production in the scenarios skewed data to make smaller producers less viable. She noted that the legislature had not been shown a significant number of models on various production levels. She wondered whether varied production levels would skew the 35 percent and \$5 per barrel credit scenario.

[10:03:39 AM](#)

Co-Chair Meyer stated that PFC Energy and Roger Marks, Legislative Consultant, Legislative Budget and Audit Committee would look at the issues raised by Vice-Chair Fairclough.

Senator Olson asked whether AOGA would support the competitiveness review board if it included an AOGA member. Ms. Moriarty responded that the current bill allowed AOGA to hold a seat on the board. She stated that the organization had too many concerns with the current structure of the board.

DAMIAN BILBAO, DIRECTOR OF FINANCE, BRITISH PETROLEUM, introduced himself and expressed appreciation to the committee for the invitation to participate. He presented the PowerPoint: "BP Testimony to Senate Finance" dated March 5, 2013. He relayed that the presentation would focus on how Alaska did or did not compete for investment in the global marketplace. He spoke to BP's history in Alaska; the company had operated production on the North Slope for over 35 years. He discussed the company's makeup and relayed that over 80 percent of its employees in Alaska were Alaska residents. He discussed that Prudhoe Bay continued to be the largest oil field in North America; when the field had

begun producing experts estimated that it contained approximately 9 billion barrels of oil. He furthered that the company had produced over 12 billion barrels from the area and saw potential for the production of an additional 2 billion barrels. He stated that the CS took a positive step forward in defining the policy that would allow the additional production to occur. He furthered that the CS provided an opportunity to increase Alaska's competitiveness by decreasing the base rate and including the GRE, which did not apply to legacy fields. He felt that SB 21 would make Alaska more competitive in the oil and gas market.

[10:07:57 AM](#)

Mr. Bilbao looked at slide 3 titled "Decline is Enemy #1," which showed DOR's December 2012 production forecast. He noted that production had declined at a rate of 6 percent to 8 percent since 2000. He stated that the graph depicted two different futures: the first showed a continued 7 percent decline in production, the second included new oil and production. He stressed that Alaska was not currently competing for investment on the global level; investment was flowing to other jurisdictions.

[10:09:19 AM](#)

Mr. Bilbao highlighted slide 4 from an Econ One presentation titled "Estimated Capital Spending for Exploration and Development Alaska North Slope vs. United States and Worldwide Spending 2003 - 2012." The graph compared total spending on the Alaska North Slope, the United States, and Worldwide from 2003 to 2012. The slide also included the WC ANS Crude index to show how the jurisdictions compared over time. He stressed that the price of oil had the greatest impact on investment. He pointed out that the different investment alternatives increased together as the price of oil increased between 2003 and 2007. He stated that investment in 2006 was approximately twice what it had been in 2003; the other jurisdictions were largely aligned at the time. He relayed that the alignment had stopped in 2007. He pointed out that the price of oil continued to increase in 2008, but as worldwide spending continued to increase, the spending in Alaska began to flatten. He communicated that when the price of oil dropped to an average of \$60 per barrel in 2009, global investment fell back into alignment; however,

as the price of oil began to increase investment in the Lower 48 and worldwide surpassed investment in Alaska. He reiterated that despite the increase in oil prices and increased investment globally, spending in Alaska had remained flat. He emphasized that BP looked for opportunities that delivered the greatest return when considering where to invest.

[10:12:33 AM](#)

Mr. Bilbao continued with slide 5 from an Econ One presentation titled: "Crude Oil Production Alaska North Slope vs. United and OECD Countries 2003-2012." The graph showed that production in the North Slope, the Lower 48, and Organisation for Economic Co-operation and Development (OECD) countries was all in alignment in 2003. Production began to decline over time; however, as the price of oil and investment increased, production and investment began to flatten and increase in the Lower 48 and OECD countries. Production in Alaska continued to decline at a 6 percent to 8 percent rate and was approximately half of the 2003 level. He addressed why Alaska had fallen behind. He emphasized that Alaska had rich resources and talent, but lacked competition because of current policy.

[10:14:59 AM](#)

Mr. Bilbao discussed a PFC Energy slide titled: "Alaska Peer Group Government Take at \$110/bbl Market Price" (slide 6). The slide showed various investment locations (e.g. U.S. Gulf of Mexico, Brazil, and other) compared by government take (including all taxes and royalties). The slide placed Alaska just behind of Norway as the location with the second highest government take. He stressed that the policy did not attract investment. He stated that when investment options were considered, Alaska was discussed last. He relayed that an average government take placed Alaska in the "middle of the pack," but did not overcome the unique geographic and cost challenges. He stressed that under the current circumstances Alaska failed to compete. He emphasized that Alaska needed to be in the top quartile in order for companies to consider investment in the state. He communicated that the conversation needed to center on the appropriate policy that would make Alaska a preeminent destination for investment.

Mr. Bilbao detailed slide 7 titled "In Summary":

- Alaska currently fails to compete globally for investment
- Positive shift in the conversation to a policy that focuses on Alaska's future
- The CSSB 21 (RES) structure could work, however:
 - the base rate is too high
 - the GRE does not apply to legacy fields

Mr. Bilbao elaborated that BP did not see any benefit to the proposed GRE in the current CS. He stated that the CS continued to reflect a tax increase in the prices BP used to model its business and opportunities.

[10:19:14 AM](#)

Co-Chair Meyer responded to Mr. Bilbao's statement that the base rate in the CS was too high. He pointed out that the base rate was tied to the \$5 per barrel tax credit. He stated that the finance committee model showed that the two items offset each other.

Mr. Bilbao responded that slide 4 showed the impact that a 25 percent base rate with the credits had on investment in Alaska relative to other jurisdictions. He stated that 25 percent was a high base rate; BP understood that it would be offset by credit. The company also recognized that under the CS the burden of earning the credits shifted to the producers related to production. He communicated that BP saw the CS as a tax increase.

Co-Chair Meyer asked for the dollar amount of investment in the state by BP and overall. He guessed the number was close to \$100 billion. Mr. Bilbao would follow up with the information.

Co-Chair Meyer believed the information would be valuable.

Senator Dunleavy asked if BP would increase investment in Alaska if the base tax rate was lowered and the proposed GRE was extended to legacy fields. Mr. Bilbao responded that the final legislation would be reviewed, the company's current model focused on the CS. He relayed that the base rate was the company's primary concern. He pointed to slide 4 and highlighted that the investment profile for Alaska was uncompetitive. He furthered that if a new policy made Alaska globally competitive, investment would flow to

destinations that competed most effectively for the capital.

Senator Dunleavy asked if BP would invest if the right policy was in place.

[10:22:28 AM](#)

Mr. Bilbao responded that BP would absolutely invest if Alaska was competitive. He stated that Alaska's subsurface certainty, talent, and infrastructure were not present in many global locations. He communicated that policy was the only reason Alaska was not competing with the rest of the world. He relayed that if the policy was corrected and Alaska became competitive, an increase in investment would occur.

Vice-Chair Fairclough had heard from media that capital investment on the North Slope was currently at an all-time high. She asked for comment on the statement.

Mr. Bilbao replied that the current level of investment and employment was very high on the North Slope. He detailed that 5 out of 6 people working on the North Slope were focused on projects that sustained rate rather than bringing on new rate. He furthered that the majority of investment was aimed at renewing the 30-year old infrastructure. He expounded that before ACES had been implemented, BP's rig fleet rate was approximately 11 rigs per year; subsequent to the implementation of ACES, BP's rig rate decreased to approximately 5 or 6 per year. He added that production levels had been impacted as a result.

[10:24:46 AM](#)

Vice-Chair Fairclough referred to BP's regular and contract employees in Alaska and Mr. Bilbao's testimony that over 80 percent of BP's employees were Alaskan residents. She wondered if the contract employees were included in the 80 percent figure.

Mr. Bilbao replied that the 80 percent figure applied to BP's employees. He stated that some of BP's contractors had a similar ratio, but others did not. He relayed that the company was committed to continuously improving the figures; contractors were encouraged to follow the company's lead.

Vice-Chair Fairclough asked about local hire related to BP's contractors. Mr. Bilbao responded that he would follow up with the information.

Vice-Chair Fairclough asked why the company's investment costs had increased, while production had remained the same. She referred to Mr. Bilbao's testimony that investment equaled production. Mr. Bilbao replied that inflation pressures were factored into costs of operating on the North Slope. He did not have a specific breakdown related to cost increases.

[10:27:14 AM](#)

Vice-Chair Fairclough asked whether the capital credits were part of the scenario. Mr. Bilbao replied that the spending reflected the direct contribution from the corporations. He expounded that there was a tax result related to where credits were obtained and how the company's tax payment was calculated. He did not know what percentage of the total spending was a capital credit. He explained that the company looked at its cash flow and spending on an absolute basis; BP looked at the total impact on the business of what it believed to be an excessively high tax.

Vice-Chair Fairclough wondered whether the company looked at the total take on a project, the base tax rate, or a spread on the tax rate when considering investment. Mr. Bilbao responded that BP looked at the economics of a project and the cumulative impacts of the tax policy on the project. The company also considered what the cumulative impact would be on the cash flow of the business. The company considered the quality of an individual opportunity and the impact to the overall business.

[10:29:10 AM](#)

Senator Dunleavy asked whether BP's ideal investment portfolio would consist of exploration or if a vast majority focused on accessing discovered oil. Mr. Bilbao responded that BP's focus was on legacy oil fields. He elaborated that most of the opportunity on the North Slope existed in currently producing areas. He stated that the greatest opportunity for locating a new oil field was in an existing field. He furthered that the company's rig fleet

produced the equivalent of multiple new smaller satellites each year. He communicated that it was important to include the continuing source of production in order to offset what otherwise would be a decline of much greater than 6 percent to 8 percent. He remarked that a significant amount of investment was needed to maintain the current decline rate.

Senator Dunleavy asked for verification that an exploration credit would not currently interest BP. Mr. Bilbao responded that BP did not engage in exploration on the North Slope.

Senator Bishop requested an example of capital investments that could improve production on the North Slope in an amenable investment climate. Mr. Bilbao replied that BP had more resources in Alaska than it did anywhere else other than the Lower 48. He emphasized that the company was not lacking in opportunity; BP did not have a policy that made the opportunities competitive globally.

[10:31:31 AM](#)

Senator Dunleavy asked when the uptick in investment would occur following the implementation of new legislation. He wondered if durability and flexibility factored into the decision to increase investment.

Mr. Bilbao responded that the right policy should be applicable at any oil price. For example, if the policy returned 65 percent to the government the percentage would remain the same regardless of the cost of oil. He reminded the committee that the price of oil had never averaged greater than \$110 dollars per barrel. He pointed to slide 4 related to spending and noted that the price of oil had increased from 2008 to 2010. He stated that given the right policy BP could respond relatively quickly, particularly around drilling opportunities. He elaborated that some of the larger scale infrastructure expansion would take a couple more years, but activity should be expected in the near-term.

[10:34:05 AM](#)

Senator Hoffman wondered whether BP (as a member of AOGA) was concerned about what would happen in 5 to 7 years if the tax policy was not successful and Alaskans felt that oil revenues had been given away. He noted that BP did not

explore in the North Slope. He stated that given data provided to the committee by DOR it was contemplating the removal of the current progressivity clause. He stated that from FY 11 to FY 15 there were estimates that progressivity would bring in \$11.3 billion to the state, which averaged to \$2.25 billion per year. He noted that he did not vote for ACES, but believed that eliminating progressivity would lead to great expectations for Alaskans to level off oil production to 600,000 barrels per day (or to the governor's expectation of 1,000,000 barrels per day).

[10:36:27 AM](#)

Mr. Bilbao directed attention to slide 3. He stated that BP's greatest concern was that production would continue to decline. He pointed to slide 4 and stated that Alaska was competing for the great opportunity on the North Slope. He stated that the status quo was not attracting investment and that a new policy was necessary to deliver a different future for the state.

Senator Hoffman repeated his question. He believed that giving up \$2.25 billion per year for 5 years created the expectation that more oil would be added to the pipeline. He stated that many Alaskans felt that there should be no reduction without new production. He wondered whether BP was concerned about what would happen if new production did not occur. He reiterated that giving up over \$11 billion in a 5-year period raised expectations by Alaskans.

Mr. Bilbao understood the challenge facing the committee. The company's concern was that the production decline would continue. He detailed that declining production raised the costs of operations and made opportunities such as heavy oil difficult to impossible. He stressed the importance of creating a policy that would attract investment. He noted that the current future under ACES was continued decline.

[10:40:29 AM](#)

Senator Bishop requested commitment from the industry to provide information on projects that would increase production.

Co-Chair Kelly remarked on the production decline occurring under ACES. He stated that the current system was too complicated and took too much. He surmised that the goal of

the former policy makers had been to extract more from the producers. He believed it was important to look at what would be best for Alaska and how to fill the pipeline. He was comfortable reducing the government take in order to achieve increased production. He stressed his interest in increasing productivity.

Co-Chair Meyer discussed slide 3 and testimony that BP was not exploring on the North Slope. He surmised that any increased investment by BP would involve extracting more oil out of the existing Prudhoe Bay reservoir. He looked at slide 2, which indicated that cumulative Prudhoe Bay production had exceeded 12 billion barrels. He wondered how much oil BP believed was still remaining. He wondered what incentive would allow for more oil extraction from the field.

[10:44:29 AM](#)

Mr. Bilbao responded that recent assessments showed \$2 billion barrels of recoverable oil remaining in Prudhoe Bay. He shared that the remaining oil was more difficult to extract. He stated that the legislature's consultants had shared information about the impact of higher cost developments relative to the different tax considerations. He expounded that investment would flow to Alaska in a more competitive nature if a policy was in place that made Alaska competitive. He communicated that the CS structure could work; however, BP believed the base rate was too high. He suggested that the committee consider the decline that was occurring with the 25 percent base rate under ACES and credits that would be necessary to offset the high tax rate. He relayed that the company would provide a model once a policy had been decided upon.

[10:46:12 AM](#)

Senator Dunleavy discussed the history of production in Prudhoe Bay. He pointed to a peak in production in the late 1990s followed by a natural decline that had not been stopped by an increase in investment. He wondered whether there had been any investment at the time to produce more oil. He referred to Mr. Bilbao's testimony that the environment was a function of price. He pointed to ACES and the current price and tax policy increases. He surmised that it was necessary to examine what had occurred in the past 5 years under ACES. He asked for verification that BP

believed the decline could be stemmed or increased for an undetermined period with investment and current technologies.

Mr. Bilbao replied that investment flowed to the best opportunities. He stated that more production would result if Alaska was competitive on a global level. He emphasized that the tax policy needed to incentivize all potential investors.

Senator Dunleavy pointed out that decline had existed under prior tax structures. He surmised that the prices at the time had not warranted investment. He asked for verification that the current price environment made investment worthy to BP.

Mr. Bilbao responded that there had been opportunities taken at lower prices because costs had also been lower (e.g. North Star and Prudhoe Bay satellite developments, which had been competitive globally). He stressed that investment would flow towards opportunities when they were competitive and the economics worked. He pointed to slide 5 that showed spending compared to other jurisdictions. He emphasized that Alaska was not competing globally for investment; therefore, production continued to decline.

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DAN SECKERS, TAX COUNSEL, EXXONMOBIL, provided testimony regarding SB 21. Exxon supported the prior AOGA and BP testimony. He stated that Alaska's fiscal regime was not competitive. The company believed it was up to the legislature to decide whether ACES or a revised tax system was the right course for Alaska in the near-term and into the future. He stated that a revised tax structure could enable Alaska to compete globally for capital investments; Exxon hoped the legislature would chose to revise the system. He relayed that Exxon believed the legislation, including the elimination of progressivity, made significant progress towards increasing Alaska's competitiveness. He stated that the high marginal rates resulting from progressivity adversely affected the investment climate, capital intensive investments needed in

the state, and the optimization of operations on the North Slope.

Mr. Seckers stated that eliminating progressivity would fix one of the most penalizing aspects of Alaska's fiscal policy. He mentioned the GRE and shared that Exxon supported tying incentives to increasing production. He communicated that most of the near-term investment in the legacy fields would not be in new exploration or benefit from the GRE. He emphasized that the legacy fields were the cornerstone of Alaska's future. Exxon believed that increasing investment to maintain the health and strength of the legacy fields was as important as encouraging development and exploration in any new field.

Mr. Seckers addressed the \$5 per barrel credit included in the legislation. He relayed that Exxon supported tying incentives to increasing production and supported AOGA's concerns that the \$5 per barrel credit may not sufficiently offset the significant increase caused by the increase to the base tax rate. He stressed that the policy should provide balance across a wide spectrum of prices. He reiterated the company's support for the legislation, but noted that it also had concerns. He underscored that Exxon believed the base tax rate was much too high; the increase from the current 25 percent up to 35 percent under the bill was "going in the wrong direction." He stated that Alaska faced obstacles that other markets did not, including high cost, Arctic environment, distance to market, and other. The company believed that global attractiveness was crucial to increasing investment.

Mr. Seckers spoke to the company's support for tax credits. He stated that credits provided a useful tool to offset costs for expensive investments needed in Alaska and helped to balance a fiscal regime over a broad range of prices. The company supported efforts by the Parnell administration and the legislature to increase Alaska's global competitiveness. Exxon recognized the difficult challenge facing the legislature to balance long-term revenue needs, budget concerns, and to increase production. He stressed that the need for Alaska to develop a competitive and stable fiscal system was one of the most critical issues facing the state. Exxon believed that the CS represented a crucial step in the right direction; however, it believed more needed to be done. He communicated that Alaska remained an essential component in Exxon's global

portfolio; it had done business in the state for over 50 years and looked forward to many more years. He concluded that it was up to the legislature to decide whether ACES or a new tax system was the right answer to bring critical investments to the state; Exxon hoped a new system would be implemented.

11:09:29 AM

Co-Chair Meyer agreed that ACES required changes, but Alaskans needed assurance that increased production would occur. He stated that no one had provided a guarantee that the changes would result in increased production. He pointed out that some individuals believed making changes was unnecessary if production did not increase. He asked about Exxon's current activities in Alaska; he understood that the company was not undertaking exploration. He asked about potential prospects Exxon had in Alaska that would promote more production.

Mr. Seckers replied that Exxon remained bullish in Alaska and was moving ahead with development at Point Thompson. The company was also the largest lease holder in Prudhoe Bay and the largest owner of known commercial gas on the North Slope. He stated that Exxon was exploring in and around the legacy fields to increase overall recovery in the area. The company believed that a small increase in the total recovery from Prudhoe Bay would dwarf any new field found on the North Slope. Exxon supported efforts by operators going forward and would work to do everything it could under the policies implemented by the legislature. He did not have specifics to provide, but the company believed that the more competitive the tax policy was the more investment would increase from existing and new companies.

11:12:16 AM

Vice-Chair Fairclough stated that Alaska's tax policy changed multiple times in the past decade. She asked why a change to the current policy would incentivize Exxon to increase investment. Mr. Seckers responded that company valued stability and agreed that the state's history of reexamining its tax structure was troubling from a statutory and regulatory point of view. The company hoped that the legislature would determine that Alaska was not currently competitive going forward and that a durable policy would be implemented that was balanced over a wide

range of prices. Exxon appreciated the deliberate examination the legislature had undertaken.

Vice-Chair Fairclough remarked that Alaska's unstable tax structure would be a ding against its global competitiveness; however, she had been convinced that Alaska was not competitive in attracting investment capital under the current tax structure. She noted that she had not supported ACES because of her belief that it took too much. She recalled that when ACES had passed, the legislature had not known that the system would take close to \$1.5 billion per year over what was expected. She asked about the difference between the GRE and cost recovery. She pointed to testimony that the company valued the qualified capital credits.

[11:15:39 AM](#)

Mr. Seckers replied that tax policy was just math; it was a way to get to a bottom line. He stated that a GRE could work and is based on production. The exclusion included a timing value; making an investment and recovering the money later through the GRE. Alternatively, a tax credit is more immediate; therefore, the impacts are more pronounced on a present value basis. He opined that the goal for policy makers was to create a policy that was balanced over a wide range of prices. He believed there were a variety of different options that could work, but it came down to how competitive the state wanted to be.

[11:17:03 AM](#)

Co-Chair Meyer stated that the goal was for the new policy to last 10 to 15 years. He understood there was the potential for a world crisis to dramatically increase the price of oil. He wondered if Exxon would feel comfort knowing that a new tax policy addressed the possibility with a type of bracketing progressivity. He discussed that without addressing the potential for much higher oil prices the policy may need to be revisited again in the future.

Mr. Seckers replied that the policy considered by the state should balance over a wide range of prices. He understood that many other jurisdictions faced the same question and had remained relatively stable for many years. He was not convinced that an immediate adjustment would be necessary if a good policy was put in place at present; it was

difficult to project for an unknown global catastrophe in the distant future, which could also decrease the price of oil. The company hoped the legislature would create the best policy for the present time that was as balanced as possible to withstand price fluctuations.

Co-Chair Meyer surmised that Exxon was not opposed to a bracketed progressivity at high oil prices as long as the total package made Alaska's investment climate stable and competitive. Mr. Seckers replied that Exxon was responding to the CS that had eliminated progressivity, which it supported. He communicated that the company had supported legislation the prior year (HB 110), which had included a bracketed progressivity. Exxon believed the elimination of progressivity in the CS was a positive and critical step forward. He reiterated his prior comments that Exxon's primary concern was that the structure was balanced and competitive.

[11:20:52 AM](#)

Vice-Chair Fairclough wondered whether Exxon was involved with any global tax system that was not regressive. She mentioned the regressive nature of past taxes. She discussed that progressivity had been one answer, but she did not believe it had worked well. She pointed to other previous tax legislation; HB 110 would have placed a cap on progressivity. She addressed the Senate Resources Committee version of SB 21, which had proposed a 35 percent base tax and a \$5 per barrel credit. She noted that the committee had heard skepticism at best regarding the structure. She wanted to find a non-regressive taxing structure. She stressed that committee members were working to find a solution supported by constituents, which included a fair share for Alaska. She did not believe the state's current share was helping it compete for investment. She believed the 35 percent base tax/\$5 per barrel credit had looked like an attractive solution.

Mr. Seckers appreciated the struggle facing committee members. He imagined that Exxon was actively engaged in some locations with progressive elements. He would follow up with detail on the question.

[11:23:25 AM](#)

Vice-Chair Fairclough wondered whether Exxon would be supportive if the legislation allowed the administration to negotiate participating areas for a term of 5 to 15 years.

Mr. Seckers asked for clarification on the question.

Vice-chair Fairclough asked if the company would support the contracting of a specific price for a period of 5 to 15 years to create increased certainty. Mr. Seckers replied that Exxon valued long-term stability; many jurisdictions where the company worked had the stability. He believed the goal could be accomplished in Alaska without radical changes. He furthered that the legislature had the ability to make any proposed change prospective only; it could grandfather-in certain tax treatments on existing investments or fields. He stressed that the legislature did not have to change anything with respect to existing investments. He noted that many options existed that would achieve certainty. He stated that the company valued certainty and durability in any fiscal regime.

[11:25:43 AM](#)

Senator Hoffman recalled that when ACES had been considered it had initially not been regressive at the lower end. He pointed out that there were ways to implement something similar; however, he believed progressivity would still need to be looked at. He asked if Exxon was less concerned with the regressive nature at the low-end than it was with high progressivity.

Mr. Seckers answered that progressivity was the most crippling part of ACES.

Senator Hoffman asked whether Exxon would continue to have major concerns about the legislation if it was non-regressive and minor tweaks were made. Mr. Seckers replied that the company would look at any proposal advanced by the legislature. He stated the company shared the legislature's goal for a globally competitive and attractive system.

[11:27:17 AM](#)

Co-Chair Meyer asked whether the current CS [(CSSB 21(RES))] made Alaska competitive on a global basis. Mr. Seckers responded that the CS represented a strong step forward in improving the state's competitiveness; however, there were

continued concerns about the legislation including a high base rate. He opined that the bill was a significant improvement over ACES. Whether the bill made Alaska as competitive as it desired was a question the legislature would need to decide. The company sensed that given Alaska's obstacles the state should be as attractive and competitive as possible.

Co-Chair Meyer noted that the committee would examine the 35 percent base rate. He reminded Mr. Seckers that the base rate had been offset by the \$5 per barrel credit; the credit was only available if oil was produced. He surmised that in Exxon's opinion, the \$5 credit did not sufficiently offset the higher base rate.

Mr. Seckers replied that Exxon believed the current 25 percent base rate was too high. He emphasized that increasing the rate to 35 percent was a step in the wrong direction. He stated that the \$5 credit was simple and creative; however, Exxon shared AOGA's concerns that the policy may not be as competitive as it should be.

Co-Chair Meyer discussed the afternoon's schedule.

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ADJOURNMENT

[11:29:43 AM](#)

The meeting was adjourned at 11:30 a.m.