

HOUSE FINANCE COMMITTEE

April 1, 2016

2:00 p.m.

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CALL TO ORDER

Co-Chair Thompson called the House Finance Committee meeting to order at 2:00 p.m.

MEMBERS PRESENT

Representative Mark Neuman, Co-Chair
Representative Steve Thompson, Co-Chair
Representative Dan Saddler, Vice-Chair
Representative Bryce Edgmon
Representative Les Gara
Representative Lynn Gattis
Representative David Guttenberg
Representative Scott Kawasaki
Representative Cathy Munoz
Representative Lance Pruitt
Representative Tammie Wilson

MEMBERS ABSENT

None

ALSO PRESENT

Kara Moriarty, President and Chief Executive Officer, Alaska Oil and Gas Association; Scott Jepsen, Vice President, External Affairs, ConocoPhillips; Paul Rusch, Vice President, Finance, ConocoPhillips; Dan Seckers, Tax Counsel, ExxonMobil; Joe Reese, Senior Tax Manager, BP; Dave Wilkins, Senior Vice President of Alaska, Hilcorp; J. Patrick Foley, Senior Vice President of Alaska Operations, Caelus; Representative Lora Reinbold, Representative Dan Ortiz.

SUMMARY

HB 247 TAX;CREDITS;INTEREST;REFUNDS;O & G

HB 247 was HEARD and HELD in committee for further consideration.

Industry Testimony: Alaska Oil & Gas Association (AOGA), ConocoPhillips, Exxon, BP, Hilcorp, Caelus Energy Alaska

Co-Chair Thompson relayed the agenda for the day. He asked Ms. Moriarty to approach the table.

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#hb247

HOUSE BILL NO. 247

"An Act relating to confidential information status and public record status of information in the possession of the Department of Revenue; relating to interest applicable to delinquent tax; relating to disclosure of oil and gas production tax credit information; relating to refunds for the gas storage facility tax credit, the liquefied natural gas storage facility tax credit, and the qualified in-state oil refinery infrastructure expenditures tax credit; relating to the minimum tax for certain oil and gas production; relating to the minimum tax calculation for monthly installment payments of estimated tax; relating to interest on monthly installment payments of estimated tax; relating to limitations for the application of tax credits; relating to oil and gas production tax credits for certain losses and expenditures; relating to limitations for nontransferable oil and gas production tax credits based on oil production and the alternative tax credit for oil and gas exploration; relating to purchase of tax credit certificates from the oil and gas tax credit fund; relating to a minimum for gross value at the point of production; relating to lease expenditures and tax credits for municipal entities; adding a definition for "qualified capital expenditure"; adding a definition for "outstanding liability to the state"; repealing oil and gas exploration incentive credits; repealing the limitation on the application of credits against tax liability for lease expenditures incurred before January 1, 2011; repealing provisions related to the monthly installment payments for estimated tax for oil and gas produced before January 1, 2014; repealing the

oil and gas production tax credit for qualified capital expenditures and certain well expenditures; repealing the calculation for certain lease expenditures applicable before January 1, 2011; making conforming amendments; and providing for an effective date."

^Industry Testimony: Alaska Oil & Gas Association (AOGA), ConocoPhillips, Exxon, BP, Hilcorp, Caelus Energy Alaska

Representative Wilson asked if testimony would be based on the House Resources version of the bill or the governor's bill.

Co-Chair Thompson thought there might be a combination of both. He directed industry to provide clarification in their testimony.

KARA MORIARTY, PRESIDENT AND CHIEF EXECUTIVE OFFICER, ALASKA OIL AND GAS ASSOCIATION, indicated that the majority of her comments were based on the committee substitute from the House Resources committee. She relayed that she would be referencing the governor's bill version in certain places in her testimony. She read from a prepared statement:

"Good Afternoon, Co-Chairs Thompson and Neuman, and members of the Committee. For the record, my name is Kara Moriarty and I'm the President/CEO of the Alaska Oil and Gas Association, commonly referred to as "AOGA".

AOGA is a professional trade association whose mission is to foster the long-term viability of the oil and gas industry in Alaska for the benefit of all Alaskans. Thank you for the opportunity to testify today on Committee Substitute (CS) for House Bill 247, Governor Walker's oil and gas tax proposal.

Although I am here on behalf of a varied and diverse group of companies, my testimony today represents the thoughts and sentiments of each and every member. On matters related to tax, AOGA requires unanimous consent on testimony.

There is no denying it - as legislators you have a tremendous challenge in these economic times. And

whether you want to believe it or not, the reality is, the oil and gas industry is facing similar challenges. Loss of revenue. Cutting budgets. Laying people off.

Even in the face of these low prices, industry recognizes the value of investment and jobs to Alaska and we are doing our part to sustain what we can in this tough environment - weather the storms and continue operating at a loss in the interest of longer term sustainability. Do not make it harder for us to sustain Alaska's economy and jobs by adding additional costs and more economic hardship."

Ms. Moriarty turned to slide 2: "Oil & Gas Drives Alaska's Economy." She read from her prepared statement:

"Alaska's oil and gas industry fuels our state's economy. No other industry comes even close.

- 1/3 of all jobs in Alaska are attributed to the oil and gas industry. Over 110,000 jobs.
- For every direct job created by the companies exploring, producing, transporting, and refining oil and gas in Alaska - 20 more private and public sector jobs are created.
- For every dollar in wage created by industry, \$8 additional dollars in wages are created.
- And, even though oil and gas revenue constitute 66% of the state's unrestricted revenue due to low prices, for FY2017, 2/3 of the state's revenue will be from one industry.
- In addition to state revenue, last year, the industry paid \$447 million in property taxes to local governments.
- What other industry or individual Alaskans are currently contributing 2/3 or have contributed so much to the state's budget and local governments? None. No one comes close. Our detractors may not like it, but the fact is, the oil and gas industry has been part of the solution and is currently contributing a significant share to the state's budget."

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Ms. Moriarty advanced to slide 3: "Questions to ask when considering policy change." She continued to read from a prepared statement:

"The industry and the state have a long standing, mutually beneficial partnership, but we are businesses who respond to the policies you make. So, as you deliberate changing oil taxes, again, please ask yourself these four questions:

- 1) Will this policy change create more production in Alaska?
- 2) Will this policy change make Alaska more or less competitive on a global scale?
- 3) Will this policy provide stability to the state of Alaska and to the industry?
- 4) Will this policy provide predictability?"

Ms. Moriarty continued her statement on slide 4: "Alaska Oil and Gas Tax Policy Changed 5 times in a decade":

"The House Resources Committee spent over 40 hours hearing testimony from the Administration, legislative expert consultants, and industry on the Governor's proposal. As a result, the Resources Committee realized the detrimental effects of many of the original provisions of HB 247, including the \$25 million cap on refundable credits, the zeroing out of tax credits in the Cook Inlet and middle earth, and the increase and hardening of the floor for minimum tax. While this improved the CS, the CS nevertheless is concerning to industry, in part, as it would represent the 6th major change in tax policy in 11 years.

Two weeks ago, I was on the phone with Jamy Rosenfield, the Senior Vice President of IHS - a global consulting firm and co-founder of CERA with world renowned and best-selling author, Dr. Daniel Yergin. We were discussing the global downturn and the economic challenges facing the oil and gas industry across the globe. When I told him that the state of Alaska was considering a tax increase and elimination of key incentives, his response was shock and disbelief. He was shocked that a state so dependent on the industry would actually consider increasing taxes in this price environment.

As your legislative consultant has said, and will likely testify to later today, he is not aware of any other region that has considered so many tax changes in the past decade."

Ms. Moriarty discussed slide 5: "If DOR forecasts hold for FY 2016, production will increase for the first time since 2002." She provided her statement:

"Objectives like stability and predictability can be subjective, I understand that. However, production is production. We either have it or we don't. It won't matter if prices go back up to \$60 or \$80 or \$100 per barrel if production goes back to the decline rates of the past.

So - what has happened to production in the current fiscal system? If the state's forecast holds for the next three months, FY16 will see the first increase in production since 2002. But - you cannot just look at production today. It's also important to look forward and consider what the impact of today's investments will have on future production. The black line is historical production in Alaska for the last decade, the red line is the forecast from December 2013, after we started the current fiscal regime, and the blue line is the forecast from just last week.

If you look at the chart to the right, to the year 2020, and compare this year's forecast to the forecast released in the fall of 2013 you will notice that after just over two years in our current system, the Department of Revenue is forecasting over 50,000 barrels per day more than what they were forecasting in 2013. To provide further context, the spring price forecast is \$50/barrel less for 2020 than it was in the 2013 forecast. Think about that: Even with the much lower price forecast, the production forecast is still over 50,000 barrels per day more four years from now.

There has been a lot of conversation about "new oil" or oil that qualifies for the gross value reduction or "GVR". The very purpose of the GVR was to lower the effective tax rate on new oil as a way to incentivize more production. It was designed for the new oil to pay a bit less in tax as an incentive, and it's

working, but it's important to point out that according to DOR's own estimates, the lion's share of our future production will continue to come from the legacy fields that do not qualify for this additional incentive. Industry will be paying current tax rates on 91-92% of the future production for at least the next 15 years."

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Ms. Moriarty scrolled to slide 6: "Unprecedented Low Oil Price":

"The industry, just like the State of Alaska, is experiencing the repercussions of an unprecedented drop in oil prices. Prices today are the lowest we've seen in more than a decade. In less than two years, the industry has experienced a 70% drop in oil prices. You are well aware of the impact this has had on the State of Alaska's revenues. The State has historically received 85-90% of its revenue from oil. As significant as that is, it's important to recognize that the industry receives 100% of its revenue based on the market prices for what it produces. As my friends in other industries will tell you, we are price takers, we are not price makers."

Ms. Moriarty continued to slide 7: "Companies Have Negative Cash Flow." She continued with her prepared presentation:

"Invariably, companies are forced to operate despite the current oil price environment, and in doing so, the oil and gas industry is currently cash flow negative, meaning, we are not collecting enough revenue each day (represented by the green line which represents oil price) to pay our bills (represented by the blue line).

When businesses do not have enough cash flow to pay their expenses, it results in cut backs. The oil and gas industry is no different. We have seen a dramatic increase in project delays, deferrals, and rigs going idle. Most painfully, Alaskans have lost jobs, and not just 40 or 50 of them. Individual companies can give you their specific job loss numbers, but from June 2015 to June 2016, there will be over 1,000 fewer

direct employees of the oil and gas industry. This number does not include the multiplier effect."

Ms. Moriarty turned to slide 8: "At current prices, industry has negative cash flow before tax":

"To add insult to injury, Alaska has been and continues to be, a high cost environment. High costs make it even more difficult to navigate during this unprecedented low price environment. According to the Department of Revenue's Spring Sources Book, (page 10 specifically), the estimated average cost of producing a barrel of oil on the North Slope and getting it to market - before a company pays even one penny of tax - is \$50/barrel.

Yet despite this, here we are, testifying about legislation to add costs for industry.

Let me be very clear: if additional taxes are levied on the industry, either in the form of increasing the minimum tax, hardening the minimum tax floor or eliminating tax credits, there will be less oil production and fewer jobs.

It is really quite simple. Industry is cash negative. They don't have any more money to give for increased costs from government. Some companies may already be burning through savings to pay for operations, and the reserves are not unlimited."

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Ms. Moriarty explained slide 9: "Administration Goal is to Raise Money." She continued with her statement:

"As I mentioned earlier, the Administration's proposal represents the sixth major tax change in the last 11 years. Prior changes came from unprecedented high oil prices, or aimed to incentivize development in the state and make Alaska more competitive.

However, the motivation behind this current proposal is not to increase production, make Alaska more competitive or create stability or predictability. Rather, it is purely driven by the state's desire for more money, now.

Raising taxes when prices go up, and then raising them again when prices go down, undercuts stability and predictability. The Administration acknowledges the industry is suffering tough economic times; in fact, according to their testimony, if prices average around \$40/barrel for 2016, the industry will suffer just over an \$800 million "loss" in the state of Alaska. That is a staggering number. It's remarkable that serious considerations are being made to increase taxes on the state's largest private sector economic driver when that industry is facing a staggering downturn."

Ms. Moriarty discussed slide 10: "Specific Concerns with CSHB 247." She relayed her statement:

As I also mentioned earlier, the House Resources Committee Substitute does not have the same level of impact as the Governor's original proposal. But it still causes industry concern.

AOGA supports the current law with simple interest for overpaid and/or underpaid taxes. It is appropriate in light of the lengthy statute of limitations which gives the Department of Revenue six years to audit a company's production tax. Compounding the interest over a 6 year period, even at the current rate, would add more than 25% of the bill before the audit is done.

Today is April 1, 15 days to tax day. Can you imagine filing your taxes, utilizing your best interpretation of the tax code, and 1 - 2 - 3 - 4 - 5 - 6 years later, the IRS comes back and says, I'm sorry, we have finally finished auditing your taxes, and not only do you have to pay the tax bill, you have to pay compounded interest on top it. This is the situation industry currently faces with this proposal. There could be likely scenarios where the interest payment is more than the actual tax bill.

Another major concern relates to a so-called "loophole" in calculating a net operating loss (NOL) tax credit.

NOL tax credits are utilized both on the North Slope and Cook Inlet and were established in part to help

level the playing field for new companies trying to get a foothold in Alaska. The NOLs arise before these companies have enough production to cover their costs, and the credit allows them to realize a benefit from their lease expenditures by getting tax-credit certificates for them.

For companies who qualify for the gross value reduction, being able to use that reduction in determining their NOL is a significant factor in their project economics. Losing the ability to use it will result in a tax increase for the very companies that policy makers wanted to attract to Alaska.

Yet another disincentive for future investment is the setting of arbitrary limits on credits of any dollar amount per company, especially when even the "smallest" of projects range in the \$500 million - \$1 billion range. Eliminating or discouraging cash rebates for companies that may not yet have production or profits, would disadvantage new companies that have invested here in good faith based on the tax policy in place when the investments were committed.

Phasing out and eliminating two important credits for Cook Inlet and "middle earth" is also dangerous. Some argue those credits are no longer necessary, but they have attracted new companies here, and production has increased. Some companies have already entered into contracts and made large financial commitments for spending over at least the next year. Abruptly terminating or changing those credits after the fact will not attract these types of investments in the future.

The House Resources CS also creates a working group to specifically focus on Cook Inlet. This group, in addition to the Oil and Gas Competitive Review Board, signals to industry that even if changes are made this session, that additional changes are coming. Once again, the State will be looking at making a change to the fiscal system signaling to investors that the state fiscal regime is not be stable or predictable.

The proposed revisions in Section 17 of CSHB 247 define "outstanding liability to the state" broadly as "an amount of tax, interest, penalty, fee, rental,

royalty, or other charge for which the state has issued a demand for payment that has not been paid when due and, if contested, has not been finally resolved against the state." Even though the House Resources CS does try to minimize the impact of this "outstanding liability" section, it still creates uncertainty for companies when trying to determine economics of a project.

Finally, retroactively applying regulations is concerning and will again, cause additional instability."

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Ms. Moriarty moved to slide 11: "Any change will have a negative impact on industry." She finished reading her prepared statement:

"Whether or not the production tax is raised, the oil and gas industry will still be the largest annual contributor to state government by far.

The oil and gas industry will contribute 7.5 times more than the Governor's proposed income tax, 50 times more than the proposed revenue from mining, and 37 times more than from commercial fishing.

In this environment some companies may find themselves in the position of borrowing money just to keep the doors open for business. We cannot emphasize enough any increase in cost will have a serious negative impact on industry and Alaska.

The industry is not before you today asking for tax relief while we struggle though extraordinarily low prices. We do ask, however, at this trying time, you do no harm."

Ms. Moriarty concluded her presentation and made herself available for questions.

Representative Wilson asked why other states did not offer refundable tax credits. It was her understanding that Alaska was the only state to offer cash.

Ms. Moriarty recommended that Representative Wilson direct her question to the legislature's consultant. She thought he had better knowledge of different systems than she did. She believed Alaska was one of the few states that had a net tax system - credits were inherent of a net tax system.

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Representative Gara mentioned that when he heard from his constituents they recognized the fiscal gap and most thought that everyone needed to step and contribute what they could. He mentioned two sets of fields on the North Slope: those that paid a lower tax (Gross value reduction fields - fields after 2002 and all future fields), and those fields before 2002. He stated that according to the Department of Revenue over the long term the gross value reduction fields (GVR) fields paid no production tax at all - a net zero production tax until the prices reached over \$73 per barrel of oil. They were not subject to the minimum tax floor and paid no production taxes. However, the state was providing credits and the industry was asking that the credits be maintained. He wondered if, from the state's perspective of wanting more revenue at higher prices, the industry should step up to the plate reconsidering the net zero production tax rate.

Ms. Moriarty relayed that the state set the policy and the industry responded. The policy was set for the GVR because the state wanted additional new oil production. The industry responded and more production could be seen in smaller fields. She believed that in looking at the forecast, 91 percent of the state's production in the following 15 years would come from the legacy fields (the fields that did not receive the GVR). For Alaska Oil and Gas Association (AOGA) it was a matter of policy. If the state wanted incentives to get new oil, the association would respond to the state's policy. If the state decided to roll it back, the companies would respond. She added that in looking at the entire system, rather than focusing in on one component, the state was collecting revenues from 8 to 9 percent of production from the GVR fields. Royalty went up as prices went up. Income tax would theoretically go up because of a higher income tax as prices went up. Property taxes would also climb. The association would respond to policy if the legislature decided to change it.

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Representative Gara understood the current policy. He asked if she thought it was fair for the state to have a net zero production tax up to \$73 per barrel of oil for the post 2002 and new fields.

Ms. Moriarty asserted that the state determined its policy and AOGA only responded to it. If the legislature thought the policy was unfair then the legislature would need to change it. She added that if the state wanted to have GVR oil to account for the 8 to 9 percent, there would be companies testifying in the current meeting that were part of the GVR oil that could talk more directly about fairness. Speaking for the industry collectively, she responded that if the legislature did not think the policy was fair it should change it. She reiterated that AOGA would just respond to the policy rather than commenting on whether it was equitable.

Representative Gara understood that raising taxes on oil field companies was not very sensible at a time when companies were losing money with the price of oil at \$20 per barrel. The minimum tax of 4 percent (an emergency tax of sorts) for the larger fields applied up to \$76 per barrel. At the Prudhoe Bay, Kuparuk, and Alpine fields companies would only be paying a minimum oil production tax of 4 percent. He wondered if Ms. Moriarty thought it was fair for the legislature to revisit the taxes for the larger fields.

Ms. Moriarty answered that the State of Alaska decided to adopt a net tax system. The state was taxing on the economics of the applicable fields. She explained that costs were very high in those fields. Producers were cash negative with the current price of oil and would continue to be so for a while. She furthered that the floor was put in place to protect the state when oil prices went down. Without the floor in place today the state would actually be collecting even less revenue. She emphasized that the companies that AOGA represented were cash negative. The net tax was designed to tax on the economics and, the fact remained that presently the producers were losing money.

Representative Gara did not mean the current day. He meant when prices adjusted to the \$50 or \$60 per barrel level and above when companies were making money. He asked if she

thought it was fair for the state to keep the 4 percent tax in place up to \$76 per barrel for the larger fields.

Ms. Moriarty responded that she was not going to comment on whether the state's policies were fair. Alaska Oil and Gas Association was responding to the state's policies. The state had a net tax in place. It took the specified price to make a profit (if that was Representative Gara's assumption at \$70 or \$76 price per barrel). The law stated that producers had to pay "the greater of" amount versus the price of oil minus the cost of transportation, minus deductible expenses (producers had additional expenses that were not deductible). Once a calculation was done the producers were required to pay the higher number.

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Representative Gara mentioned that she had gone through her predictions of production anticipating it to be down below 400,000 barrels in a few years under the existing system and the forecast. He was aware that fields were coming online since the law was changed. He noted the CD5 field, but the announcement of the field coming online came before the law was changed. Point Thompson was coming online but was based on a settlement achieved in 2012 prior to the law changing. There were other fields, Moose's Tooth and Bear's Tooth, which were being invested in before 2013. He wondered if there were any fields where investment had not started prior to the tax law changing.

Ms. Moriarty relayed that about 91 to 92 percent of production was coming from the legacy fields. All of the fields were in place and investments were made in previous tax fiscal systems such as Alaska's Clear and Equitable Share (ACES), Alaska Petroleum Profits Tax (PPT), or More Alaska Production Act (MAPA) - the current tax structure. Prior investments were impacting production, which without them the state would be currently in a more serious financial strait than if the state was at the historic 6 to 8 percent decline. She explained that in terms of production it was necessary to look at investments being made currently and how they might impact production in the future. Since the passage of SB 21 [legislation passed in 2013 relating to oil and gas production tax] the industry had invested almost \$5 billion above and beyond what had been invested in prior years. The impact of investment might not be realized yet. However, if the state wanted to

raise taxes on an industry that was losing money she guaranteed that the investments would decrease and production and jobs would be negatively impacted.

Representative Gara clarified that he was asking questions about taxes when companies were making profits.

Vice-Chair Saddler asked if the state was paying the oil industry to take oil out of the state.

Ms. Moriarty responded in the negative. She added that the producers had to make investments before they could apply for any credits. She provided an analogous situation. The state was not paying producers. Producers were leasing the property from the state, producing oil and gas from those properties, and after they made investments they were able to apply for some level of credit based on the system the state had in place.

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Vice-Chair Saddler asked if the state was paying the oil industry to give away Alaska's oil.

Ms. Moriarty responded in the negative. The state was paying the industry credit that producers earned by investing money, then applying for credits according to statute.

Vice-Chair Saddler asked Ms. Moriarty about other sources of income to the state that accrue from oil production in addition to production tax.

Ms. Moriarty relayed that the oil and gas industry paid the state four different revenue streams including royalties (the state's share as the land owner), production taxes (a net tax based on the economics), corporate income taxes, and property taxes.

Vice-Chair Saddler asked Ms. Moriarty to provide Alaskan's with assurances that leaving the current tax system in place was to their benefit.

Ms. Moriarty recognized that it could be a challenging argument to make when the state was faced with a severe budget crisis. She posed the question as to how the state could afford to pay oil tax credits. Her response was that

she was not sure if the state could afford not to pay the credits. The credits were assuring that the industry was investing in the future of Alaska. She wondered about a growth plan for the state, about how Alaska's economy was going to grow. She mentioned the mining bill and opined that the miners would tell legislators that one new mine could produce more revenue than the proposed increase in the mining tax. She supposed the oil and gas industry was really no different. The oil tax credits were a way to incentivize behavior to make additional investments and produce more oil. If production were to continue to hold steady and slightly increase over the following couple of years and prices went up it would be a positive thing for the state. However, if prices went up but production went down, there may not be a net benefit for the state. Even though there might be an increase in price there might not be a net benefit if production decreased. It was key for producers but production went down a net benefit might not occur. For producers keeping the current fiscal system in place was key to keeping production steady.

Vice-Chair Saddler asked if losses by the industry in Alaska were being balanced out by business operations elsewhere in the world.

Ms. Moriarty responded that his questions should be addressed to specific individual companies. She commented that the price of oil was low everywhere. It was not just low in Alaska. Companies were cash negative in Alaska and were generating less revenue in other regions. It was also forcing regions to be more competitive because there was less investment dollars available to invest in current development as well as future development.

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Vice-Chair Saddler commented on the DOR revised Spring Revenue Forecast. The forecast indicated that by 2026 the state would have 217,000 or 277,000 barrels a day in the pipeline. He wondered if it was a fair decline prediction assuming there were no other capital investments made. He asked if the industry would continue to produce oil in a declining production environment without significant additional capital expense.

Ms. Moriarty responded that it obviously became more expensive to produce as production declined. She believed

all Alaskans should be concerned that producers were currently operating the pipeline at less production than the original start-up in June 1977. She explained that when Alyeska Pipeline started production it was producing about 700,000 barrels per day. Admiral Barrett could confirm that there were operational challenges and costs at present at 500,000 barrels per day. For engineers it was an exciting project. As modifications arise they came at a cost.

Vice-Chair Saddler noted that the models seemed to predict the effect of the tax credits infinitely without accommodating practical considerations.

Representative Pruitt asked if she had any knowledge of any other existing tax regime for which one of AOGA's member companies operated that was looking at increasing taxes in the current environment.

Ms. Moriarty thought his questions would be better answered by the legislature's consultant. She also mentioned a recent article in the "Economist" on the same issue. There were a few regions looking at increasing their tax rates whether having to do with production or royalties. She was aware that some of her member companies were operating in those areas such as in Russia and Nigeria. However, she was not aware of any state in the United States or province in Canada planning to increase their tax rates.

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Representative Pruitt asked Ms. Moriarty if companies would be able to maintain the same level of investment and production with increasing taxes.

Ms. Moriarty did not believe AOGA's member companies would be able to maintain the same level of investment if taxes were increased or credits were eliminated.

Representative Pruitt asked if Ms. Moriarty thought that the current tax policy was focused more on production or general fund monies. Based on her answer to his first question he wondered if the change the legislature was contemplating adjusted the focus of the policy of the state.

Ms. Moriarty stated that the current policy was focused on getting more oil in the pipeline. It was focused on making

Alaska a competitive environment while allowing a return to the state and its citizens. If prices were to return to the same levels as when SB 21 was passed the government take would be around 62-63 percent. She referred to Governor Jay Hammond's philosophy of one-third, one-third, and one-third: one third to the federal government, one-third to state government, and one-third to industry. At those prices, SB 21 achieved that ratio. At current prices the government take was almost 100 percent and for some fields it was 100 percent. The Alaska Oil and Gas Association noticed the state looking at tax policy from the perspective of how to achieve more production, maintain competitiveness, make the policy simpler, and one other component. The administration stated that if prices returned to the \$80-\$100 range it might not be having a conversation about changing the current tax policy. The administration's focus has been on how to get more money in the current low price environment recognizing that the industry was losing money. She opined that a change in tax policy was more about state finances rather than getting more oil in the pipeline.

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Representative Pruitt asked whether investments and production would increase if prices were to go up again, based on her answers regarding the potential decrease in investments.

She could not guarantee what companies would do when prices increased. However, it would be extremely difficult to attract capital back to Alaska if the state raised taxes when prices went up and raised taxes when prices went down. Most companies would have to plead their case to a board of directors although for some only one person would need convincing. The first question from board members would be whether a company made money in Alaska in the previous year. The response might be that at \$40 oil the company did not make money, but if prices were to go up it might be possible to make money. Questions about taxes might ensue making it more difficult to argue in favor of further investment in Alaska. She noted that the legislature would be hearing from Cook Inlet producers in the following week. She relayed that it would be very difficult to get the jack-up rig back to Alaska in the following 5 years or at all if it were to leave the inlet.

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Representative Guttenberg emphasized that Alaska owned the resources although he thought that some people attributed revenue to the oil industry. He pointed out that the industry obtained leases for the state's resources. The state and industry prospered together, rising and falling together. Alaska had always been a resource extraction state. Alaska had several different resources including, furs, fish, timber, coal, gold, and copper. He thought that Ms. Moriarty viewed the framework based on taxes. He saw credits as the means of driving behavior. He asked her to speak to direct production resulting from tax credits. He commented that he wanted to see production continue in Prudhoe Bay. He wondered if she could identify credits that produced more oil. He mentioned consistently hearing producers talk about being in Alaska for the long-term. The credits were designed to change behavior. He wondered if she could expound on when production would stop as a result of tax credits halting.

Ms. Moriarty responded that the committee would be hearing from industry participants who would report that their production was a direct result of the credits. She used Cook Inlet as an example. The production was down to about 8,000 barrels per day. Some of the legacy rigs were only producing 600 barrels per day. Legislation that was passed, often referred to as the Cook Inlet Recovery Act, enticed companies to Alaska. Some Cook Inlet producers would claim that the credits were the reason for coming to Alaska. There had been a 100 percent production increase in Cook Inlet. There were companies like Hilcorp, BlueCrest Energy, and Furie Operating Alaska who were either producing or close to production. In the past there have been other North Slope producers that have invested and have experienced an increase in production due to the tax credits. She could not provide each company's percentage of production because of confidentiality issues. However, she suggested looking at the fields and the names of the companies on the Department of Natural Resources (DNR) area wide leasing map and those companies had testified in the past that there had been a direct correlation between the credits and production.

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Representative Guttenberg commented that Cook Inlet was very different from the North Slope and both were different from Middle Earth. He thought that how the credits applied to Middle Earth were very important because not only were they important for companies doing exploration but thought it was a game changer for the state in terms of the diversification of supply. He thought it was key to driving the cost of energy down throughout the state. He believed there were many benefits in Cook Inlet and in Middle Earth. He opined that what Doyon Ltd. and Ahtna Inc. were doing was very important as well. He had a very tough time hearing that the administration could only provide aggregated numbers. Legislators had been told that the state was paying 85 percent of operating costs. He commented that anyone would be investing in Alaska if 85 percent of their costs were being paid. He wanted to understand the economics of each of the industry companies but he was not able to without more information.

Representative Guttenberg told of receiving an email from Alyeska Pipeline that reported daily production to be 547,000 barrels per day. He understood that the number was not a yearly average but a daily high.

Co-Chair Thompson thanked Ms. Moriarty and invited Conoco Phillips to the table.

[2:52:02 PM](#)

SCOTT JEPSEN, VICE PRESIDENT, EXTERNAL AFFAIRS, CONOCOPHILLIPS, appreciated the opportunity to provide its perspective on the various tax changes being considered. He addressed a PowerPoint presentation titled "House Finance Committee: CSBH247" dated April 1, 2016 (copy on file). He began with his agenda on Slide 2. He relayed that he would be presenting some of the company's key concerns with the original bill, in part, because there had been a great deal of testimony on the original bill in front of the House Finance Committee.

Mr. Jepsen turned to slide 3: "Activities Since Tax reform (MAPA) Passed." Since More Alaska Production Act (MAPA) was passed in 2013 ConocoPhillips had added 2 rigs to its drill fleet. There was another order in place for 2 additional rigs of which one had already been delivered. The second rig would be delivered later in the current year. Conoco had already proved and constructed a new drill sight at

Kuparuk, Drill Site 2S (DS 2S), the first new drill site at Kuparuk in about 13 years. Once it was fully on stream it would add about 8,000 barrels per day to production from the field. The cost was about \$500 million to construct it and it added about 250 construction jobs while it was being built.

Mr. Jepsen continued to explain slide 3. He reported that ConocoPhillips was currently also involved in expanding its viscous oil operation. It had approved a project called 1H News - 1H stood for the drill site being developed and News stood for Northeast West Sack. Once the site was on stream it would add about 8,000 barrels per day, similar in magnitude of DS 2S. However, due to the downturn in oil price CP differed its drilling on the new well. The modules were built and transported to the North Slope. Currently, the company had had to respond to what it saw in the world economic environment. Conoco Phillips decided to defer the drilling until the following year and estimated having oil at the site in 2017.

Mr. Jepsen reported pursuing new developments in the National Petroleum Reserve Alaska (NPRA). The company was pursuing a development of Greater Moose's Tooth 1 (GMT1), a project in which the investment decision was made late in the prior year. The project would cost about \$900 million to construct and would add approximately 600-700 construction jobs and would add about 30,000 barrels of oil per day once it was on stream. The first oil was anticipated in 2018.

Mr. Jepsen furthered that with GMT1 underway the company was doing the engineering and ordering long lead materials. It was also permitting another new development referred to as GMT 2. Greater Moose's Tooth 2 (GMT2) was about 9 miles Southwest of GMT1. It was not as far along as GMT 1 in terms of engineering and cost estimating. However, the cost would be in excess of \$1 billion and slightly larger than GMT1. There would likely be 600-700 jobs during the construction phase.

Mr. Jepsen reported that ConocoPhillips had also been active in exploration. The company drilled 2 exploration wells in NPRA in 2014, acquired seismic data for GMT1 in 2015, and 3 exploration wells would be drill in 2016 in NPRA. Two of the three wells were about 9 miles West of GMT2 and the third was being drilled off of the CD5 drill

site. He noted that one major project underway that was coming on stream at present was CD5. The company had decided to pursue CD5 before SB 21 was passed in large part because it had spent about 10 years trying to obtain the permits. Everything was in place and a decision had to be made whether to pursue it. ConocoPhillips elected to go ahead with the project because of all of the other investments that had been made in trying to get the permits in place. Also the company had hoped there would be a change in oil taxes away from Alaska's Clear and Equitable Share (ACES) to something more reasonable based on the recent discussions that had been in play.

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Mr. Jepsen continued to address slide 3. He pointed to the activities ConocoPhillips currently had going on in Kuparuk - it had 5 rigs running. Before the passage of SB 21 the company only had 3 rigs running. Under the current low price environment in ConocoPhillips' entire Lower-48 operation it had 4 rigs running and anticipated going to 3 rigs in the following month compared to 5 rigs in Alaska. Alaska had been differential in terms of its investment philosophy. He also mentioned that there had been several comments made about all the new fields coming on stream since 2002 or 2003 and qualifying for the GVR. ConocoPhillips added new production at drill sites 2S, 1H News, and CD5 and had not filed for the GVR on any of the related production. At drill site 2S and CD5 there was some production that could potentially qualify for the GVR but when it took a look at the requirements for measurement, the cost, and compounding it out with the difficulty in trying to determine how much oil came from an existing pa and a new pa, the company decided not to pursue the GVR for CD5 or DS 2S.

Mr. Jepsen continued that regarding 1H News, there was testimony on behalf of the state that it thought that the site would qualify for the GVR but the way the regulations were written the site did not qualify. He emphasized that there was no GVR production coming from any of ConocoPhillips' existing fields and there was no GVR production in NPRA. However, GMT1 would qualify, and it would be much easier to isolate the production and prove to the state where it came from and that it came from a new participating area.

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Mr. Jepsen addressed slide 4: "Capital Spending Trends." He wanted to discuss the present economic environment that ConocoPhillips was in and compare it to what it had been in the past. He pointed to the plot on the bottom left hand side of the graph representing the steep decline in oil prices. He suggested comparing the graph to the bar chart right above it which tracked the corporation's capital spending during the same period. He noted that in 2014 ConocoPhillips peaked at about \$17 billion of capital spend and as oil prices dropped the capital spend declined to a current estimate of about \$6.4 billion for 2016 - a drop of about 63 percent since 2014.

Mr. Jepsen moved to the right portion of the slide. Statistics were provided describing what the company has been doing in Alaska. He pointed to the top bar chart depicting what the company has been spending on capital since 2012. The last year of ACES was 2012. During the entire time of ACES, from 2007 to 2012, the company was spending about \$800 million per year in Alaska. In testimony over that period of time the company indicated that if there was a better investment climate ConocoPhillips would make more of an investment. The company stepped up its investment in 2013, 2014, and 2015. Some of the spending in 2014 was from CD5 but much of it was from the drill rigs in place and from new investments such as DS 2S and 1H News. Originally, the company had announced the capital budget for Alaska in 2016 of about \$1.3 billion. However, due to a steep price drop and in recognition of being in a negative cash flow position, the company reduced its costs. The company reduced its Capex (capital expenditures) in Alaska to about \$1 billion for 2016. He remarked that the investment remained healthy and more than what the company was spending during the years of ACES and more rigs were running. In terms of discussing capital, a measure of how many jobs were being created and how much was being invested in new resources, adding oil to the field really had to do with how many rigs were running. ConocoPhillips had managed to keep its rig count high.

Mr. Jepsen moved to the bottom right hand plot which showed the percentage of ConocoPhillips capital spent in Alaska. Spending had steadily ramped up to the point of where in 2016 the company was at about 16 percentage of the corporation's total Capex. He commented that the trend was

significantly different in other regions. The change in capital seen in Alaska was down about 23 percent from where the company had anticipated being at the start of the year. In many other regions of the corporation it was down much more than that. He reemphasized that ConocoPhillips was still investing differentially in Alaska and in Alaska the corporation was in excess of \$100 million negative cash flow in the previous year. He remarked that it was not a long-term business plan for the company but it hoped to manage through it and hopefully see a return in oil prices.

Mr. Jepsen advanced to slide 5: "North Slope Investors Negative at Current Pricing." He thought the slide summarized what the industry was currently facing and what the state was facing. In the range of prices currently at hand industry was in a negative cash flow position. He noted that the left hand side of the plot represented cash flow and that the "X" axis showed ANS West Coast price. The data used to construct the plot came from the Spring 2016 Revenue Sources Book. The orange blocks estimated state cash flow, the green represented federal taxes, and the blue showed the producers cash flow. The plot did not include any reimbursable tax credits the state might pay back to other producers who were in a non-tax paying position. The plot represented the free cash flow the state received and also represented the cash flow position the industry was in. He reemphasized what Ms. Moriarty stated. The conversation currently was about potentially increasing taxes on the oil and gas industry, an industry in a negative tax flow position. If the state taxed the industry it meant that there would be less money for investment. Companies would respond rationally like any company would.

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Mr. Jepsen turned the presentation over to his colleague who would discuss ConocoPhillips' key concerns about the original bill. He mentioned that they were going to go through the issues because there had been a fair amount of testimony in front of the committee on provisions that were not included in the committee substitute that were included in the original bill. They wanted to provide ConocoPhillips' perspective as to why some of the provisions would not have been very helpful.

PAUL RUSCH, VICE PRESIDENT, FINANCE, CONOCOPHILLIPS, addressed slide 6 "Key Concerns with Original HB 247". He

relayed that there were several points the company had raised in the previous testimony to the House Resources Committee identifying the major concerns that the company had with the original bill. He wanted to walk through those concerns. He stated that the first item was increasing the minimum tax from 4 percent to 5 percent. The industry was clearly in a position where it was losing money. If taxes were increased it would come out of somewhere else within the industry. The second item was the hard minimum tax floor. He explained that within HB 247 there was a proposal that was particularly concerning that impacted the use of net operating losses to go below the floor. In the company's view the net operating losses were very customary in federal income taxes and in a number of other fiscal regimes. By removing the ability to utilize those losses to go below the floor during periods where the industry was losing money was a true increase in taxes.

Mr. Rusch pointed to the third bullet point on the slide surrounding the increase in interest rates that applied to taxes that were either due to or from the state depending on the audit position. There was a 6-year statute of limitations that applied. He relayed that ConocoPhillips just recently closed out its 2006 production tax audit, over 9 years from the end of that tax year. Interest would apply to that entire period. It would be more than 6 years. He also mentioned that the company had just received its 2009 production tax audit, within the statute of limitations, but to the date. The system had a built-in delay on when the audits would be settled.

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Representative Gattis referred to the audits. She wondered about the interest charges that accrued and whether they were due to the company falling behind. She also asked who performed the audits.

Mr. Rusch explained that the 6-year period was a statute of limitations within the current tax law and governed by the state.

Mr. Jepsen added that the company received its first audit under the state's control at the time Mr. Rusch mentioned.

Co-Chair Thompson clarified that it was the Department of Natural Resources' audit.

Mr. Rusch confirmed that it was a DNR audit.

Representative Gattis understood that the state was looking for money and it was taking the state 6 years to perform audits. It seemed that if the audit was performed in a quicker timeframe, especially in the state's current budget crunch, the state would receive its money in a timelier manner. She would call on the administration to find out why audits took so long. She wanted to clarify whether it was the company's problem or the state's problem.

Representative Gara remarked that in past years the administration has asked for more auditors in order to avoid missing the statute of limitations. He reported that the legislature had not always responded to the requests.

Mr. Jepsen commented that ConocoPhillips tried to pay its taxes as accurately as possible. However, the system in place was highly subjective and not crystal clear. There would always be differences of opinion. In some instances the state could owe ConocoPhillips money. He thought it worked better for all parties if the time period for audits was shortened considerably.

Mr. Rusch continued with slide 6. He pointed to the bullet point concerning per barrel credits. He explained that, in the original bill version, there was a restriction on the use of per barrel credits in the month earned. In the company's view it meant the state was moving more towards a minimum tax. The production tax was clearly a yearly tax. In the current process the company made monthly installment tax payments. It was based on an estimated tax for the full year. He added that as part of that estimate the company took the per barrel credits that it was entitled to, divided the number by 12, and applied it to the monthly tax installments. It was a fairly complicated process. At the end of the year the full allotment of credits would be applied to the final tax calculation. The way in which the company was addressing installment payments and the yearly true up was based on statute and the state's tax regulations.

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Vice-Chair Saddler asked about the impact of the monthly tax limitation combined with the impact of not allowing the

gross value at the point of production to go below zero. He understood that there was a combined effect.

Mr. Rusch answered that the restriction on the per barrel credits was strictly an issue around monthly fluctuations in price. He noted that at the end of the 2014 or 2015 tax year there was significant volatility in the oil price which impacted the number of per barrel credits that could have been used if the monthly restriction had been applied as opposed to the full year entitlement.

Representative Munoz asked Mr. Rusch to explain how the loss credit functioned and whether the losses were specific to ConocoPhillips' investments in Alaska.

Mr. Rusch asked if Representative Munoz was referring to the NOL's.

Representative Munoz responded that she was referring to the 35 percent loss credit, how it worked in conjunction with the 4 percent minimum, and whether the losses were specific to Alaska.

Mr. Rusch answered that the 35 percent net operating loss was specific to Alaska based on the Alaska's production tax regime. It was completely separate from any state income tax. He explained that in a year where a company was in a net operating position from a production tax standpoint, the company would be paying minimum tax. However, there would also be a calculated net operating loss. Within the current tax law a company was allowed to apply the 35 percent net operating loss to its taxes in the following year or years.

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Representative Munoz asked if there was a limit on the number of years which the credits could be applied.

Mr. Rusch did not believe there was a limit but within the proposed bill there was a 10 year limit.

Mr. Jepsen thought the provision was in the original version of the bill.

Mr. Rusch concurred.

Mr. Rusch drew attention to the last bullet on slide 6. There was a question about confidentiality. He was aware through various discussions a concern was raised about the lack of transparency mostly around the reimbursable tax credits. He understood the challenges the legislature had around confidentiality. In the original version of HB 247 the confidentiality issue was addressed very broadly potentially opening up the tax payer's entire tax return to public disclosure or disclosure governed by confidentiality agreements. In ConocoPhillips' view it would potentially open up a number of issues. The company's major concern was in making sure that, if the legislature had an issue, the wording was very specific to the particular issue rather than including broad language.

Mr. Jepsen moved to the final slide, slide 7: "Observations." He relayed that when ConocoPhillips saw significant changes in the tax law that occurred every other year or 18 months it caused the company great concern about the state's ability to implement a stable oil and gas fiscal policy. It had only been about 19 months since SB 21 was ratified by the voters and already significant changes in the state's oil tax were being discussed. Long-term investment required a durable, predictable, and reasonable fiscal framework. He relayed that the investment time horizon in Alaska was much longer than in other parts of the United States. He opined that with the proposed changes in the original bill ConocoPhillips thought it sent a very clear message to the company's corporate folks that Alaska was not a place that it could depend upon. He noted that the tax changes since the passage of SB 21 positively influenced the investments the corporation has made in Alaska.

Mr. Jepsen discussed the last point on slide 7. In terms of the committee substitute, the corporation thought it was a significant improvement over the original version of the bill. He mentioned that it did have some items that could potentially represent a cost increase. ConocoPhillips did not qualify for reimbursable tax credits. Many of the things that impact the small producers or the non-tax payers did not affect the corporation. The things that impacted ConocoPhillips were relatively minor. He concluded that although the company favored keeping the status quo, the committee substitute was an improvement. He asked if there were questions from members.

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Vice-Chair Saddler commented that ConocoPhillips was one of "The Majors" still aggressively exploring in Alaska. He wondered how the proposed oil tax credits changes affected the company versus its friendly competitors.

Mr. Jepsen ConocoPhillips did not explore based on exploration credits. The company was exploring prior to the credits existing, it was exploring currently, and it would be exploring after the credits expired. The credits were a help but not a deciding factor in whether the company was going to drill a well in NPRA. The ultimate investment the company was going to make was much larger than any sort of help it might get with the initial investment credit.

Vice-Chair Saddler mentioned hearing a discussion as to whether CD5 was influenced by the tax credit issues. He wanted to provide Mr. Jepsen with the opportunity to answer the following question. He wondered if the provisions of the bill have any potential to affect CD5's current or future economics.

Mr. Jepsen responded that in terms of the committee substitute he did not see any impacts.

Representative Pruitt asked if there was any other regime with which the corporation was operating under that was currently looking at increasing a tax on oil and gas production.

Mr. Jepsen responded in the negative.

Representative Pruitt asked that if the legislature were to move forward with the initial version of the bill would it have an influence on ConocoPhillips' investment in Alaska and, if so, he wondered what it would look like.

Mr. Jepsen answered that it would have an impact on the company's investment particularly at low oil prices. If the cost of doing business increased it would have to come out of somewhere. It would likely come out of the investments the company was currently making. The company would have to take a look at everything it was doing in Alaska and decide what it would do less of. In the long-term he thought it sent a chilling message to all investors that Alaska was a place that when oil prices declined it would increase taxes

and when oil prices rose the state would also increase taxes. He did not believe it was the message Alaska wanted to send to investors.

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Representative Pruitt wondered how difficult it would be to return to the current production level of 500,000 barrels per day if the state went forward with the legislation and the state witnessed decreased production.

Mr. Jepsen answered, "It depends really how far you let it go." He elaborated that it was difficult to predict the future. He reported that there were high tax frameworks particularly when there were increases in taxes at low prices. Activity would drop off and rigs would be put aside. It would be difficult to bring those rigs back. It would be a function of price, whether the state changed its fiscal framework again, and what the framework would look like if it was changed. Representative Pruitt's question was a very subjective question which he could not answer with confidence. He remarked that it would place Alaska in a hole and the state would be risking the loss of a significant amount of infrastructure.

Representative Guttenberg referred to slide 3. He asked who ConocoPhillips acquired GMT1 from.

Mr. Jepsen responded that when he stated acquired he meant that ConocoPhillips shot it - the company hired a contractor to go out and shoot it - referred to as data acquisition.

Representative Guttenberg mentioned that typically acquire meant getting something from someplace else.

Mr. Jepsen understood.

Representative Guttenberg relayed that the legislature had been complaining for years about audits. It had been a long-term problem for the legislature as well as for those being audited. He sympathized.

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Representative Gara conveyed that he had bristled when hearing that Alaska taxed high at low prices and high at

high prices. He did not agree. He remarked, "Certainly nobody in state government or in the oil industry is doing very well at current prices. Everybody is losing money at \$30 and \$35 per barrel and prices around there." He thought the state needed to be careful with whatever it did. However, in looking at ConocoPhillips annual reports and because of SEC [Securities and Exchange Commission] rules he believed it was the only oil company that produces in Alaska that reported its Alaska profits. In prior years the company's Alaska's profits were in the \$2 billion range while last year the company was down to zero to \$400 million in profits without writing off its Chukchi Sea leases. He asked if he was correct.

Mr. Jepsen responded that it reflected ConocoPhillips' net income but did not represent the company's cash flow.

Representative Gara asked him to explain his point.

Mr. Jepsen indicated that he brought a handout that might help in providing a response for Representative Gara's question.

Representative Gara asserted that no one was saying ConocoPhillips had earned much money the previous year. He went on to say that net income was either \$400 million or zero if it wrote off the Chukchi Sea leases. He asked if he was correct.

Mr. Jepsen responded affirmatively.

Representative Gara's mentioned that Alaska had been told to tax similar to North Dakota. He had read in the annual report that the company had lost \$1 billion in the Lower 48. He wondered if he was accurate.

Mr. Jepsen did not have the numbers in front of him but would agree with the report if the representative was looking at it correctly.

Representative Gara understood that in North Dakota the company paid a private royalty - private land owners owned the land unlike in Alaska - and a state tax. He added that the numbers were on the gross, a percentage of the value, rather than of profits. He asked if Mr. Jepsen knew the average private royalty that the company paid in North Dakota.

Mr. Jepsen responded that the information Representative Gara was asking about was confidential. He made it clear that ConocoPhillips was not drilling in North Dakota.

Representative Gara remarked that the call that Alaska would be more like North Dakota from a few years ago [Mr. Jepsen interrupted Representative Gara with a response].

Mr. Jepsen clarified that the previous conversation was held when ACES was being discussed. At the time ACES was considerably higher than North Dakota. The company was putting itself in a comparison perspective in terms of what the tax framework looked like around the United States and other places around the world. He furthered that currently in terms of comparative places to invest Alaska was a pretty good place. However, when prices go up the company would be paying more than in other places. The good thing about being in a good place from a competitive point of view was that the company was seeing more activity in Alaska than other regions around the world or the Lower 48. He thought it was due to the current tax policy and because of some other issues around doing business in Alaska. Things could change if the state changed its tax policy.

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Representative Gara wanted to clarify that at current prices the state received a 4 percent gross minimum tax on the older field and a 12.5 percent royalty on the percentage of the value of the oil. He wondered if the private royalty and tax the company paid in North Dakota was substantially higher.

Mr. Jepsen believed the current severance tax in North Dakota was 5 or 6 percent. Royalty payments were based on what had been negotiated. It could range anywhere from 12.5 percent to something higher. It was very company specific and lease specific. The drilling location was a function of what kind of royalty and taxes were being paid.

Representative Gara indicated he had another question about North Dakota.

Co-Chair Thompson reminded Representative Gara that ConocoPhillips was not in North Dakota.

Representative Gara remarked that North Dakota was very relevant when they wanted to lower their taxes. He asked if Mr. Jepsen would concede that the gross private royalty and the tax that the company paid in North Dakota was higher than in Alaska.

Mr. Jepsen responded that it probably was at preset. He reiterated that the company's activity in North Dakota was about nil. ConocoPhillips was drilling in Alaska. If the legislature wanted to see the kind of actives that Representative Gara was seeing in other places where there was a higher tax framework and a tax policy could be set that would drive those results.

Representative Gara asked if Mr. Jepsen would have any problem with the state moving the 4 percent minimum floor modestly higher when prices were in the profitability range again.

Mr. Jepsen referred back to slide 5 and emphasized that the state was always making more money than ConocoPhillips even under the current bill. The company was not there to talk about what was fair and unfair or whether it had a problem with the state increasing its taxes. He was there to tell legislators that if the state took certain actions the industry would take certain actions. If the state made it a more hostile environment, a difficult place, or increased taxes the company would reevaluate its investments in Alaska. It was a hypothetical question. The state would need to determine what kind of tax policy it wanted which would drive investments.

Mr. Jepsen tried to put things in perspective. At the time discussions ensued about changing ACES \$73 was considered a very low price. Currently it was being discussed as a high price. He reiterated that he thought the state was better off under SB 21. He encouraged members to go back and look at the data. As the price curve had gone down the tax policy had been beneficial. If the state wanted to discuss trying to increase taxes again as the prices went up it would have a direct impact on the company's short-term and long-term investments.

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Vice-Chair Saddler mentioned a provision that had not been discussed much which was the condition of some of the

credits on Alaska hire percentages. He asked for Mr. Jepsen's thoughts on the issue and wanted him to provide ConocoPhillips' Alaska hire percentage.

Mr. Jepsen answered that the provision regarding Alaska hire did not apply to the company because the company did not receive the reimbursable tax credits relating to Alaska Hire percentages. He told of ConocoPhillips of having an overall percentage of Alaska hire of 70 percent. In Anchorage the company was up to 85 to 90 percent. On the North Slope the percentage tended to be lower in part because people had the option to live outside of Alaska and in part because the company had to hire people with specialized skills that do not live in Alaska. He added that the company asked the question of all of its contractors and looked at it each time it issued a contract. The company tried to make a conscious decision that it had a bias towards Alaska hire and buying.

Representative Gattis asked what motivated the oil companies to do business and what motivated companies to do business in Alaska. She did not distinguish oil companies from any other business. She thought it was more about what motivated businesses. As a small business owner she looked at various aspects trying to plan ahead to avoid knee jerk reactions. She did not see oil companies being any different than any business that might be sitting in front of the committee being asked the same questions. She also did not think it mattered whether it was a business in North Dakota or Alaska: businesses react the same way.

Co-Chair Thompson thanked the presenters from ConocoPhillips. He invited the presenter from ExxonMobil to the table.

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DAN SECKERS, TAX COUNSEL, EXXONMOBIL, thanked the committee for the opportunity to come before the committee. He stated that the committee substitute before members was a very concerning piece of legislation. He reemphasized something he had stated many times in the past. He thought it was worth repeating in the current economic environment, which was that ExxonMobil was committed to Alaska and would continue to actively pursue attractive investment opportunities. The company has had a presence in Alaska for over 90 years and invested over \$20 billion to-date. Alaska

remained an important component of the company's worldwide investment portfolio and it looked forward to being in Alaska for many years.

Mr. Seckers continued that the company recognized the difficulty the legislature faced as policy makers in tackling the state's current budget issues while trying to protect the current revenue streams and trying to make certain that Alaska remained a competitive place to do business. ExxonMobil appreciated how difficult and how hard the legislature's task was. The tax policy decisions fundamentally impacted the economic health of the state in all the industries that did business in the state. From ExxonMobil's view tax policy decisions that would move Alaska either toward or away from its vision for the future - its vision of promoting oil and gas development - should not be taken lightly. The need for Alaska to maintain a competitive and fiscal regime, one that attracted and encouraged ongoing investments and future investments especially in the current low price environment, was one of the most important issues the state faced. While Exxon Mobil appreciated the need to close the state's fiscal gap, it believed that any tax policy change should be weighed against the potential negative impacts on the state's long-term investment climate. From the company's perspective, the question that was before the committee was whether raising taxes on the oil and gas industry at a time when the Department of Revenue had confirmed that companies were reporting significant losses was consistent with Alaska's future and the legislature's belief that such actions would help Alaskans weather the economic downturn or make matters worse.

Mr. Seckers pointed to the committee substitute before House Finance members. He started by confirming that ExxonMobil supported the testimony presented by the Alaska Oil and Gas Association (AOGA) and by ConocoPhillips. He relayed that while the committee substitute represented a substantial improvement over the original bill introduced by the administration it remained a very concerning piece of legislation. Despite the improvements made by the House Resources Committee, the committee substitute was troubling because it would represent another significant change in Alaska's oil and gas policy within the past 11 years. It would raise the interest rate on over and under payments of taxes while not addressing the core issue raised by AOGA and ConocoPhillips which was the length of time on audits.

It would not improve Alaska's overall investment climate. It would not lead to more industry jobs or more opportunities in the state. It would not lead to more production, or long-term sustainable oil and gas revenues. In fact, Exxon Mobil believed the committee substitute would do the exact opposite. For the reasons he has presented ExxonMobil opposed the committee substitute. While he mentioned that the company believed the committee substitute as a whole was troubling he wanted to highlight two provisions that gave him, as ExxonMobil's tax counsel, concern. The first was that for any tax policy to be successful and to meet the state's long-term goal of sustainable oil and gas production and revenues such tax policy needed to be stable, predictable, and provide confidence to tax payers and investors that the underlying rules of the game would not be changed repeatedly to adversely affect the economic investments already made and those being considered for the future. Like any business large or small ExxonMobil valued a very predictable environment in which to make long-term investments. The company's investments were very capital intensive and span many years. He relayed that any change in the regime that went forward would affect the viability of those investments and the company's view of investments going forward.

Mr. Secker highlighted another significant change being proposed: The raising of the interest rates. He reported that in the previous day, like ConocoPhillips reported, Exxon Mobil received its 2009 assessment 6 years after the company filed its return. He could not reveal the amount of interest because it was confidential but he confirmed that the amount was staggering. ExxonMobil thought it was wrong. The legislature was proposing to adjust the interest rate, but the underlying problem was not being addressed. The effect was lessening the incentive of the state to expedite audits. The company felt the state was going in the wrong direction. ExxonMobil thought the current rate worked.

Mr. Seckers reemphasized that the committee substitute represented a troubling bill. He highlighted a couple of the provisions that were in the original bill that were removed by the House Resources Committee because of its extensive examinations into those provisions and their damaging effects. He pointed out the hardening of the minimum tax floor. The committee substitute was a substantial improvement because it did not attempt to raise

taxes by hardening the minimum tax floor. Preventing companies from realizing the true economics of their investments by preventing critical tax credits from being realized to offset the minimum tax would have represented an immediate and significant tax increase. It would have penalized companies who had made prior year investments even when they were losing money, it would also have penalized those companies who wanted to continue to make potential current year investments despite the low economic environment. For those companies, large or small, that might have new oil tax credits, expiration drilling credits, and tax loss credits from prior year investments and that might be in a loss position today because of current prices and thus were depending on the credits to continue funding their current investments - that provision, alone, could have delayed or possibly denied that economic investment to those investments at the very time the companies needed it the most. In order to maximize investment opportunity in Alaska, he thought it was critical to provide investors the opportunity to capture the economic opportunity of those investments especially given the long-term outlook and the risks involved in the inherent high-cost environment that was Alaska. That provision, alone, would have significantly and negatively impacted Alaska's investment climate in the perception of the investment climate to any future investor by announcing to the world that Alaska was willing to adversely affect the economics of past and future investments solely for short-term revenue needs.

[3:37:47 PM](#)

Mr. Seckers spoke to the raising of the minimum tax. The change would have resulted in a very substantial tax increase and a regressive tax increase because it was based on gross revenues rather than net income. Raising taxes on companies who were reporting record losses, losses on the very activity the legislature was trying to tax under HB 247, was not a wise or feasible long-term solution or a wise long-term tax policy.

Mr. Seckers moved on to discuss another of the provisions that was removed from the committee substitute: the application in the termination of the gross revenue at the point of production. The provision would have also raised taxes on the industry. He understood that it did not seem intuitive for the gross revenue at the point of production

to go below negative. However, currently the price of oil fluctuated. There were costs such as marine transportation and pipeline costs which were the only deductions that could be taken to determine the gross value at the point of production which could cause the gross value to go negative. If the gross value could not go below zero, then the economic investments in marine transportation and pipeline costs would potentially be lost. Companies did not file a field-by-field tax return but rather a segment return. He used the North Slope as an example. For the North Slope it included all of the economics of the North Slope. Therefore, a loss in one area, would possibly be offset by income in another to represent the economics of that segment for a company. The bill provision would have prevented the gross value at the point of production from going below negative without an explanation of what would have happened to those investments costs [deductions]. It would have changed the substance of the law of how the tax was determined, how the gross value at the point of production was applied, and would have been nothing more than a tax increase.

Mr. Seckers brought up the issue of taxpayer confidential information. The problem with the original bill was that the provision would have allowed very confidential and taxpayer sensitive information to be released. Although ExxonMobil was partners with BP and ConocoPhillips at Prudhoe Bay and other fields but they were competitors domestically and internationally. The companies were bound by federal law of what they could or could not disclose or share. ExxonMobil could also not share proprietary sensitive business information. The provision in the original bill would have opened the door for the disclosure of very troubling and possibly unlimited information. He concluded that he discussed the original bill because he wanted to acknowledge the improvements made to the original bill by the House Resources Committee, but to discourage the legislature from reintroducing those provisions into any bill under consideration. He opined that reintroducing any of those provisions would dramatically reduce Alaska's overall global competitiveness by raising taxes when many companies were reporting record losses. The losses were on the very activity the legislature was trying to tax, which would be poor tax policy. Reintroducing those provisions would force companies to reexamine short and long-term investment behavior and was inconsistent with the state's long-term vision of promoting oil and gas development.

Previously, the state enacted a petroleum production tax in ACES when prices were rising to raise revenue. He communicated that enacting those same provisions would send a clear signal to the entire global investment community that Alaska's tax policy was to raise taxes when industry made money and again when it lost money just for short-term revenue needs. Alaska needed to remain globally competitive for critical capital investment. He furthered that increasing or imposing a tax on companies in a negative cash position would not lead to more jobs, to more investment, to more production, or to long-term sustainable state revenues. Alaska remained a very important component of ExxonMobil's worldwide portfolio. The company had been in Alaska a long time and wanted to remain in Alaska for a long time to come. However, as ConocoPhillips had indicated, when the state raised taxes it raised costs for companies to do business. Every opportunity that ExxonMobil looked at in the future would become less attractive and would diminish.

Mr. Seckers concluded his testimony. The need for Alaska to maintain a competitive and stable fiscal regime that attracted and encouraged ongoing critical future investments especially in the current low-price environment was one of the most important issues facing the state. Policy makers needed to decide whether increasing taxes on companies that were losing money would lead to more jobs, more investments, more production, and more long-term revenues was a wise state tax policy. ExxonMobil believe the answer was, "No." If the committee substitute reverted back to the original bill the answer would be emphatically, "No!" He was happy to answer any questions.

[3:43:03 PM](#)

Vice-Chair Saddler asked if the changes in the oil tax credit bill proposed in the committee substitute had any potential for affecting the likelihood of getting to a front end engineering decision (FEED) decision for the AKLNG project.

Mr. Seckers responded that the AKLNG project was obviously a very critical project and a very expensive project. He commented that fiscal stability undercutting the state oil and gas regime was important because a decision could not be based on an unstable oil and gas structure. Any change in the structure would have an effect. The company would

look at it very carefully. It was difficult for companies to want to invest \$60 billion when the risk of tax changes was constantly a possibility.

Vice-Chair Saddler asked about the role that any of the various credits might have played in the construction of the Point Thomson unit.

Mr. Seckers responded that Point Thomson was part of a settlement that was ongoing. It was also an underpinning of the gas project that ExxonMobil was looking at. In terms of the credits that Point Thomson enjoyed but prior to SB 21 there was the Capex tax credit that was no longer available. There were no other credits in play because the unit was not currently up and running. At the time that it was running a \$5 new oil per barrel credit would be available to the Point Thomson production.

Vice-Chair Saddler asked Mr. Secker for his assessment of the effect of not allowing the gross value at the point of production to fall below zero might have with the monthly tax regime proposed by the governor's original bill.

Mr. Seckers was uncertain of the context of Vice-Chair Saddler's question. He responded that he was unsure of the effect on a monthly basis of the gross value at the point of production. He suggested that if the gross value at the point of production went negative on one particular field the taxpayer, assuming that they had more activity on the Slope, would consolidate it when they made their monthly payment with their other filings. The amount of monthly tax would go up if the deductions were taken away resulting in a tax increase.

Representative Pruitt asked if there was any other regime that ExxonMobil was currently operating in that was proposing to increase taxes.

Mr. Seckers encouraged him to ask the state's consultant that would be testifying later in the same day. He would likely have more detail. He responded that to his knowledge the answer was "no."

[3:46:27 PM](#)

Representative Pruitt asked how ExxonMobil's investment in Alaska would be influenced if the state went forward with

the hardening of the floor and some of the other adjustments to the actual tax.

Mr. Seckers answered that the provisions in the bill were troubling and would result in significant tax increases. The company took into account anytime taxes went up or a regime became unstable and would affect the company's investments going forward. He reiterated that when the cost of doing business in the state increased because of increased taxes there had to be an offset. Generally, there were 4 levers that would be evaluated: efficiencies, scaling back of activity, discretionary spending, and layoffs. ExxonMobil had not had to lay off its employees yet. An increase in costs would negatively impact these 4 areas.

Representative Pruitt recognized that reducing investment would impact the percentage of decline. He wondered if the state would ever be able to recover once it started seeing less investment and a decline in production.

Mr. Seckers stated that when costs and taxes were raised investment behavior changed. It also changed people's outlook and increased concerns that investments made in the present would be adversely affected going forward. If production and investment declined each company would have to approach its board to determine whether to invest again in Alaska. He thought it would be a difficult argument to make to a board of directors if the state had already raised taxes when prices were down and companies were losing money. Board members would be looking for assurances. He concluded it would be difficult to get investment and production back.

[3:49:46 PM](#)

Vice-Chair Saddler wanted to understand how credits given in one year did not return benefits to the state by investment. He wondered about the time horizon that the state should expect to see returns from a state investment from foregoing some taxes.

Mr. Seckers thought it was a difficult to answer from one company alone because each company's development scenarios were different. Credits affected behavior and it depended on the type of credit and type of investment. The purpose of credits was to incentivize an activity especially given

Alaska's tax regime. Under SB 21 Alaska's fiscal regime was rather competitive, whereas, under ACES it was not. Anytime a tax regime was changed it would have an adverse impact. The credits were designed to increase activity. It was particularly important given the fact that Alaska's base tax rate was 35 percent, almost 3 times higher than any other state in the country. Alaska had a very complicated system due in part because it had a high base tax rate. If Alaska did not have such a high base tax rate or if did not have the credits and deductions he wondered what the tax rate would be. Credits had a tremendous impact on investment and leveled the field. The timeframe of recovery depended on the type of investment. He assured the committee that it was an incentive to motivate investment and increase production which he thought the state was looking for.

Vice-Chair Saddler wondered if he was accurate in saying that if the tax credits were designed to incentivize a decision to drill, a decision was made to drill, oil was found, and oil was produced the decision would pay dividends throughout the lifetime of the production through the well rather than for just one year.

Mr. Seckers responded in the affirmative. He added that the drilling of the well would give rise to additional property taxes, additional income taxes, and additional royalties. He suggested that the focus be more on local government take. At the current price of oil the local government take in some instances was over 100 percent. It was an unsustainable business model for anyone running a business. Increasing it further would not be sound policy.

Co-Chair Thompson thanked Mr. Seckers for his testimony.

[3:53:15 PM](#)

JOE REESE, SENIOR TAX MANAGER, BP, introduced himself and read from a prepared statement:

Co-Chairs, Members of the Committee: For the record my name is Joe Reese and I am Senior Managing Tax Counsel for BP Alaska. I am very pleased to be here today to provide BP's views on tax policy and, in particular, the bill before you. BP is a member of AOGA and supports the testimony provided by AOGA earlier today.

The success of Alaska's oil and gas tax policy is critical to BP, to the AKLNG Project, and to the many Alaskans who benefit, both directly and indirectly, from the successful exploration, development, and production of Alaska's oil and gas. A durable, predictable, and administrable oil and gas tax policy must be in place to unlock those benefits.

BP is committed to maintaining a safe and compliant business in Alaska that is sustainable. Over the past two years, there has been a 70 percent drop in oil price. Under the current market conditions, BP's business in Alaska is spending more cash than it brings in, and this is not sustainable. As a result, BP is evaluating the activity level at PBU [Prudhoe Bay Unit] in order to adjust expenditures in response to the lower price environment. Improving our cost base is essential to maintaining our activity level at Prudhoe Bay and the long-term viability of an AKLNG Project.

BP is committed to complying with tax laws in a responsible manner and to having open and constructive relationships with tax policy makers. One of the major costs to BP's business in Alaska is oil production tax.

At current prices, BP receives no oil production tax credits from the State of Alaska, nor does Prudhoe Bay production have any oil production tax credits under the minimum tax. While BP doesn't currently receive production tax credits, we don't support limiting the production tax credits provided in SB 21 because it would negatively impact the oil and gas industry as a whole, including the many other companies that have made investments, created jobs, and added production in Alaska.

Just as the industry is struggling to make ends meet, the State also faces severe budget shortfalls. While reasonable people may disagree about how to improve the current oil and gas tax policy, now is not the right time to make changes to increase taxes and further undercut our ability to maintain the activity level at Prudhoe Bay. Near-term changes to the State's oil and gas tax policies will have long-term consequences for all of us.

Now, I'd like to provide a few comments specifically about the bill before you:

1. The Minimum Tax: The Resource Committee's CS does no harm to the 4% minimum tax rate.
2. Change to the interest rate calculation for tax overpayments and underpayments: Currently, the interest is calculated at a rate that is 3 % points above the federal funds discount rate, using simple interest. The Resource Committee CS has interest compound at the end of each calendar quarter. Such a compound rate would reward the Department of Revenue for being slow in its audits. This would increase the uncertainty in Alaska's tax system.
3. Net Operating Loss Tax Credit: The Resource Committee's CS is an improvement to the Administration's proposal because it continues to allow the use of net operating loss tax credits to reduce the minimum tax. In other words, companies that made important investments in the prior year, even when they may have been spending more cash than they were bringing in, still would be allowed to recover part of that investment. NOL tax credits are utilized by a broad range of companies both on the North Slope and in Cook Inlet, and changing their value would be a disincentive for future investment decisions.
4. Confidentiality: Current law allows the Department of Revenue to publicly disclose information about tax credits on an "aggregated" basis for a group of three or more taxpayers, and the Resource Committee CS does no harm to taxpayer confidentiality.
5. Retroactivity: The Resource Committee CS allows for regulations to be applied retroactively to the effective date of the law. This is neither predictable nor administrable by the taxpayer and thus is not sound tax policy.

Again:

- BP is committed to maintaining a safe and compliant business in Alaska that is sustainable;
- BP is committed to complying with tax laws in a responsible manner and to having open and

constructive relationships with tax policy makers; and

- BP supports durable, predictable and administrable oil and gas tax policy.

Mr. Reese thanked the committee for hearing his testimony and offered to answer questions.

[3:58:38 PM](#)

Representative Pruitt asked if BP had experienced any tax increases in any other regime it operated under.

Mr. Reese was not aware of any.

Representative Pruitt asked if there were any regimes that BP operated under that were offering incentives or lowering their tax.

Mr. Reese was aware that the 2017 UK [United Kingdom] budget included provisions to reduce the tax in the North Sea.

Representative Pruitt stated that BP had been vocal in terms of what to expect in the current year regarding employment. He thought the company anticipated a 17 percent reduction in its workforce. If the bill passed he asked if BP would continue to decrease its workforce and respond accordingly if the state increased taxes.

Mr. Reese answered that the company was currently in the process of making a 17 percent reduction. BP was exploring all available options to reduce costs. The company had hoped to maintain the level of investments at all of the locations it participates in Alaska. He added that it was a very simple equation that if taxes went up increasing costs it would impact the company's investment decisions.

Representative Pruitt asked if Mr. Reese saw the Alaska market recovering its current level if investment was reduced.

Mr. Reese replied that from a tax policy perspective and from an investment governance perspective BP required a predictable, durable, and administrable tax policy. It was difficult for the individuals in the organization that make the company's investment decisions to continue to ramp back

up or increase expenditures when they were uncertain of the rules.

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Vice-Chair Saddler had seen BP's statistical outlook on the energy industry for the past couple of years. He had heard that the large major international oil companies looked out decades rather than a few years. He asked if the company saw the cash negative net losses in Alaska as a short-term blip or a fundamental change in the oil market that Alaska should take steps to accommodate in its tax policy.

Mr. Reese admitted he was not an economist but offered that the company did not foresee market conditions changing significantly in the near-term. Therefore, BP's situation, being in a negative cash flow position, would remain constant.

Representative Guttenberg asked about conversations regarding the minimal level of yearly production increases needed in order to maintain the facilities and the Trans-Alaska Pipeline System (TAPS). He asked Mr. Reese to provide his comments.

Mr. Reese was unaware of such conversations as he dealt mainly with taxes at BP. He would relay the representative's question and follow up with a response.

Representative Guttenberg wondered about the liabilities if production did not increase and something happened to facilities in the line causing it to shut down.

Mr. Reese replied that he would follow up.

4:03:39 PM

DAVE WILKINS, SENIOR VICE PRESIDENT OF ALASKA, HILCORP, read from a prepared statement:

For the record my name is Dave Wilkins, I am the Senior Vice President for Hilcorp Alaska. Mr. Chairman and members of the committee thank you for the opportunity to address you today about the committee substitute for HB 247. I have previously testified on HB247 in the House Resources Committee on March 1st of this year.

For those of you who are not familiar with our company, Hilcorp is the largest privately-held oil and gas company in the United States. Headquartered in Houston, TX, Hilcorp has operations in the Gulf Coast of Texas and Louisiana, the Northeast United States, and Alaska's Cook Inlet and North Slope. Hilcorp was founded 1989 and has more than 1,400 full-time employees. Just over 500 of those employees support our operations here in Alaska and I am proud to say that nearly 90 percent are Alaskan residents.

Here in Alaska we operate approximately 53,000 gross barrels of oil per day and 150 million cubic feet of gross gas per day from approximately 500 producing wells, for a total net production to Hilcorp of approximately 57,000 barrels of oil equivalent per day.

Hilcorp's assets are primarily (although not exclusively) older fields with extensive production histories, steady and predictable performance that carry incredible opportunity for getting more oil and gas out of the ground safely and responsibly while extending production life through efficiency and thousands of smaller scale projects. We think the State needs to attract more companies like Hilcorp as fields and infrastructure continue to age.

That brings me to why Visit before you here today. Hilcorp's production in Alaska represents approximately 40 percent of what we produce company-wide, so our success here in Alaska is critical to Hilcorp's overall success.

I can say from Hilcorp's perspective, the credits in question have resulted in more investments here in Alaska, both on the North Slope and the Cook Inlet basins. Starting with the Cook Inlet area, it's no secret that Hilcorp has been a big part in reviving energy security in Southcentral Alaska.

During the past 4 years, we have invested over \$1 billion in projects and have drilled over 50 wells in the Cook Inlet Area. As a result of this investment and the increased production, we are sending more oil to be refined and used in Alaska. On the natural gas

side, due to our significant investment over the past four years, we are now making gas supply commitments with local utilities into the year 2023. We stand by our commitment to serve Alaskan's energy needs first and are working to ensure a reliable and affordable energy source for Alaska's largest population hub.

As you are well aware, prior to Hilcorp's entry into Alaska, there was widespread concern of "brownouts" and that utilities would need to import natural gas to meet demand. I have spoken to many who made electric generator purchases during this time expecting service interruptions.

Hilcorp's success certainly did not come without challenges. Developing oil and natural gas in the Cook Inlet basin carries a very high cost of production coupled with decline rates that vary from 15-50 percent annually depending on the field. The simple fact is that if we are not spending money on projects that bring on new production we cannot curb these declines. So we believe it is in both our best interest and the state's best interest that we continue to spend dollars on trying to produce more oil and gas.

It's also no secret that Alaska's tax credit system and the Cook Inlet Recovery act were key drivers in bringing Hilcorp to Alaska and in our investments to date. Since 2012," Hilcorp has spent approximately \$3.2 Billion dollars in capital and acquisition costs here in the State of Alaska. Those investments were aimed at one primary goal - increasing oil & gas production. Since 2012, we have increased overall production by approximately 40 percent. A lot of people like to ask us how we do it, and the answer is simple. We have and continue to make significant investments; investments that were encouraged by the State's tax credit program and investment that did just what the credits were meant to do, increase energy supply for Alaskans.

I would argue that our success has been meaningful to many, including the State. Increased production levels of oil and natural gas in the Cook Inlet basin has resulted in increased royalty rates, property taxes, jobs and more. One example of this is looking at our

Monopod offshore platform. In January 2012, right after Hilcorp took over operations, the realized oil price was approximately \$95 per barrel. Production was approximately 600 barrels of oil per day; a marginal rate for an offshore platform that has a high operating cost. Because of this marginal rate and low profitability, the Monopod qualified for royalty relief under HB 185 passed in 2003.

The royalty rate was reduced to help maintain profitability for the platform so it would not be shut-in and/or permanently abandoned. As the royalty owner, the state's take from the Monopod at that time was approximately \$90,000 per month again, when oil was about \$95 per barrel. Over the past 4 years, Hilcorp has done over 150 projects on the Monopod, most of which were smaller in scope, and has increased production to a current rate of approximately 3,000 barrels of oil per day.

Because of the increase in production, the state's royalty share is back up to the standard 12.5 percent and even with oil prices at \$35 per barrel, the state's royalty take from the Monopod has increased to approximately a half a million dollars per month. That's over a 5 times more in royalty dollars going to the state, despite oil prices declining more than 60 percent. Furthermore, and probably more important, our success at the Monopod has added 20+ years of production life and 8 million barrels of future oil production.

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The Monopod is not an isolated anomaly. Since Hilcorp's entry into the Cook Inlet area in 2012, oil production has doubled, which has increased oil royalty to the state of over \$70 million. Furthermore, even though oil prices are lower this year, estimated oil royalties will be approximately \$10 million more this year than what they were right before Hilcorp's entry when oil prices were high. Hilcorp's success in increasing oil production over the last 4 years also has increased future estimated oil production by 20-30 million barrels, meaning increased future royalties for the state.

I would offer, we need more results like this: more production. I will also offer that the state needs a system in place that is stable, predictable and incentivizes, not jeopardizes, continued investments. Hilcorp's Cook Inlet success is a really good example of the State putting good policy in place aimed at achieving a positive result and getting one.

I can tell you today that the credits Hilcorp earned were absolutely reinvested in the resource. Our current production rates prove it. We have managed to work our way above the 50K Barrel threshold both through acquisition and a lot of hard work. Breaking the 50K per day mark means we can no longer cash in the very credits that this legislation proposes to take away. But other budding companies can, and Hilcorp is a company that always welcomes competition in the market. We want to help promote a healthy industry throughout the state. An active industry means additional service companies will be attracted to Alaska which creates competition and will help drive down costs.

A lot of the discussion regarding credits has involved the Cook Inlet basin, primarily because of the notable increase in production and activity that the existing tax structure intended to generate was wildly successful. Our success in Cook Inlet is what fueled Hilcorp's interest in expanding to the North, and we did just that in November of 2014 when we purchased three of BP's assets on the North Slope: Milne Point, Endicott and Northstar fields. When we took over operations, we were producing approximately 36,000 gross barrels of oil per day from these three fields and now we produce approximately 37,000 gross barrels of oil per day.

After a year of working with these assets, I am so excited about the amount of opportunity up there. We have a comprehensive list of projects we can invest in projects that will put more oil in the pipeline and support literally hundreds, if not thousands, of jobs for Alaskans. We currently have one drilling rig running on the slope and would like to pick up a second rig by the end of the year

But, in today's price environment and in the face of an uncertain state fiscal structure, it is to be determined what projects move forward and when. We have to be very thoughtful with every penny we spend. Investment budgets are shrinking and compete with other oil and gas producing areas throughout the world. I want Hilcorp's investment dollars to come to Alaska. We have to continue to work hard to build efficiencies and cut costs, while ensuring we do it safely and without causing harm to the environment. Cutting costs, not corners, is the only way we will survive the current downturn.

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I know that we are not the only ones faced with difficult decisions and realities during this challenging time. I also recognize the members of this committee and the legislature have much to consider about what is best for the state and our future. I ask you today to recognize that change creates uncertainty, and uncertainty deters investment and affects jobs. Investment, whether for exploration or development, is the only way to increase production and increased production is the only way we can help get out of this situation.

Over the past 30 years, I have worked in several other basins throughout the United States, and I can say with confidence Alaska has changed its tax policy more in the last few years than other areas have in decades. I want to keep Alaskans working, I want to increase production but the company simply is not going to continue to invest hundreds of millions of dollars in Alaska, especially in this price environment, when the fiscal structure continually changes.

So, in closing I would just like to say again that the uncertainty we are currently facing threatens our ability to plan our investments and that the decisions you make today will impact the economics of the opportunities to increase tomorrow's production both in Cook Inlet and on the North Slope.

Mr. Wilkins thanked the committee.

Vice-Chair Saddler stated that the other co-chairs had to leave the current meeting and that he was given the gavel to continue with the meeting.

Representative Pruitt understood from Mr. Wilkins' testimony that approximately 40 percent of Hilcorp's investment was in Alaska. He wondered if there was another tax regime in which the company operated that was imposing additional tax increases at the current time and in the current price environment.

Mr. Wilkins responded in the negative.

Representative Pruitt felt that Hilcorp was slightly different than the three major oil companies and would be adjusting his questions. Yesterday the legislature had heard from the administration that Hilcorp was heralded for turning around investment which Mr. Wilkins had highlighted in his testimony in the Cook Inlet and on the North Slope. He first asked about how Hilcorp was able to increase production. He also asked about the impact the bill might have in Hilcorp's ability to maintain similar increases.

Mr. Wilkins responded to his first question about "how." He stressed that it was a lot of hard work by some very dedicated employees. Many of the employees were acquired, through Hilcorp's acquisition of Chevron, Marathon, and BP. They were very highly trained, highly dedicated, and highly motivated employees. He emphasized that all of the credit went to the employees who paid attention to the small details. He spoke again about the monopod and the fact that 150 projects were completed. The key with the older assets was to work them hard and to understand them.

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Representative Pruitt asked how the legislation would impact increasing production. He reiterated that Hilcorp was different than other companies that had been discussed. Mr. Wilkins had been talking about increases while the discussion had been about stemming decline. He wanted to better understand how he saw the legislation potentially impacting Mr. Wilkins' ability to increase.

Mr. Wilkins relayed that Hilcorp would live within its cash flow. His boss would not let him take a loan out to pay the company light bill or tax bill. Currently the company had

two drill rigs operating, one in Cook Inlet and one on the North Slope. The company would like to operate more. However, if the state's policy decision was to increase taxes it would place pressure on the operation of the second rig. He would have to decide whether the company could afford the second rig. He would rather take the money and drill additional wells in Alaska. It not only made sense for Hilcorp, it also made future sense for Alaskans. He saw nothing in HB 247 that encouraged the company to spend more money in Alaska over the current law. Both versions would discourage further investment in Alaska.

[4:24:25 PM](#)

Representative Munoz thanked Mr. Wilkins for his presentation and for Hilcorp's success in Alaska. The legislature appreciated the company's efforts. She mentioned that Mr. Wilkins had spoken about investing in Prudhoe Bay and Cook Inlet. In Prudhoe Bay the base rate was 35 percent and in Cook Inlet there was no production tax. She asked if he thought it was appropriate for the State of Alaska to consider a rate similar to the Prudhoe Bay and the Cook Inlet when the tax cap went away.

Mr. Wilkins responded that whether it was royalty taxes, property taxes, or income taxes he looked at what the costs were to Hilcorp. He looked at the total cost of doing business then decided whether he could afford to do business. He concurred with what Ms. Moriarty had stated that the state made policy and industry responded to that policy. If his costs went up it would likely drive down activity, capital costs would be reduced, and there would be a reduction in jobs and production. He also agreed with ConocoPhillips that any one decision made by the state would not necessarily cause a corresponding response but would impact Hilcorp's decisions. He would not be making a sheer investment decision based on the tax structure but it would certainly be a consideration.

Representative Munoz reported hearing testimony that Cook Inlet was sufficiently incentivized because of the lack of a production tax. She asked for his comments.

Mr. Wilkins responded that the tax incentives in the Cook Inlet did exactly what they were intended to do: increase production of oil, giving the state additional royalties, and gas, giving a stable price to the gas supply for homes

and utilities thus, avoiding brown outs. Gas prices could have double had the state had to bring gas in from somewhere else. He thought the tax credit system encouraged many projects and investment money to Alaska resulting in increased production.

4:27:24 PM

Representative Munoz talked about the minimum tax on the North Slope. She asked if he thought it would be appropriate for the state to consider a time certain for the net operating loss to be carried forward.

Mr. Wilkins replied that the state could make any policy it wanted and he would react to it. He was new to Alaska having only been in the state for a year. The idea that oil companies had a lucrative deal in Alaska lead him to pose the question as to why more oil companies were not pounding down the door to do business in the state. He noticed that more companies have left Alaska than come to Alaska in the previous 4 to 5 years. He added that Alaska was a difficult environment to operate in.

Representative Gattis asked if Hilcorp had operations elsewhere in the world.

Mr. Wilkins answered in the affirmative. He relayed that the company did business in the Gulf Coast and the Northeast - primarily in the United States.

Representative Gattis suggested that Hilcorp had other options. If Alaska took advantage of tax policies that allowed the company to take fuller and better advantage of other options (code-speak for the company could pick up and go somewhere else). Alaska would have no advantage at that point. The state could tax Hilcorp "until the cows come home", but if the company was not in Alaska to be taxed it would not matter. She thought the bigger challenge for Alaskans to look at was that many industry companies had other places to do business. She wondered whether Alaska was open for business. She conveyed that she would appreciate having Hilcorp's business so the state could pay for all of the things Alaskans have become accustomed to.

Vice-Chair Saddler thanked Mr. Wilkins for his testimony and asked him to provide a copy of his written comments to staff. He invited Mr. Jepsen from ConocoPhillips back up to

the table. There was a correction he would like to make on the record.

4:30:40 PM

Mr. Jepsen commented that Vice-Chair Saddler had previously asked about the percentage of Alaska residents employed by ConocoPhillips. He might have provided some information that could have been misleading. He relayed that there were about 1200 employees hired directly by ConocoPhillips and about 85 to 90 percent of those employees were Alaska residents.

Vice-Chair Saddler commented that the number had seemed a little low.

4:31:23 PM

J. PATRICK FOLEY, SENIOR VICE PRESIDENT OF ALASKA OPERATIONS, CAELUS, would try to respond to the questions asked earlier in the meeting. He asked members to listen for and to make their own determinations about whether a company like Caelus was part of the solution or genuinely part of the problem. He suspected Caelus was not the problem. He provided some background information. He came to Alaska in 1983 and had spent more than half of his adult life in the state. He had worked in every oil and gas jurisdiction in the Lower 48 and spent about 4 years working internationally. He had some experience in the related issues. He wanted to remind members of who Caelus was, what the company had accomplished, and to provide some insight into what the company's future would hopefully look like. He also wanted to share with members what the proposed changes to tax policy would have on his company. Sadly, he thought he might be the expert in net operating loss transferable credits. He wished he was not in a loss position. Caelus bought the Pioneer Natural Resources Co. (Pioneer) assets. Therefore, when he discussed Caelus' history Pioneer's history was included. He conveyed that he had personally opened the office for Pioneer 14 years previously. The company had been in the state for 14 years, made substantial investments, but had not yet made a profit. The company was still operating at a loss. He asked members to consider what a net operating loss meant in the context of a production tax system. He relayed that all in meant was that Caelus made more expenditures (the company invested more capital and paid additional money) every year

than generated revenues. All businesses started out similarly.

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Mr. Foley introduced his PowerPoint Presentation: "House Finance CS HB 247 (RES) Testimony." He began with slide 2: "Caelus Energy Alaska: Key Facts & Information." He reminded members that when he was discussing Caelus he was also including Pioneer's history. Since the company came to the state in 2002 it had invested over \$2 billion in capital. In 2016 the company had a capital budget of \$300 million. Currently the company had 70 full-time employees in Alaska and had approximately 400 contractors working on the Slope at present. When he summed the information together and took into account the fact that it took 2 bodies to do 1 position and some of the jobs were seasonal it represented about 600 full time positions.

Mr. Foley spoke to the accomplishments of his company. The company had produced 23 million barrels of oil since 2008. In 2015 the company made 4 million barrels of oil. Many people questioned Caelus' small size and commented about its safety records and technical expertise. However, he was proud of the company's safety record, its environmental record, and its technical standpoint. The company was drilling some of the longest wells on the North Slope. In all of its wells the company employed super giant frack technology. The company pumped about 2.6 million pounds of proppant in its wells. It was the largest frack job on the North Slope. Not only was he the expert in Net Operating Losses, he was also becoming the expert in trying to make money on tight crummy reservoirs (that was all the company had). The company's reservoirs, the Torok and the Nuiqsuk, required very intensive capital and fracking. The company took reservoir rocks that would make a small amount of production and employed very large fracks on them (costing about \$10 million to frack a producer). The results were that the wells had initial production IP rates in the 5000, 6000, and 7000 barrels per day. After a year the wells had sustained rates of about 1500 barrels per day. Caelus had found a way to take difficult reservoirs that had been left behind by other companies on the North Slope and found a way to be profitable requiring very large capital. The company was profitable at reasonable prices. However, today oil was not at reasonable prices. He admitted that his company was struggling to exist. He thought he could say

the same about every other oil company. He thought it was probably the same for the State of Alaska. He reported that in the current day the price of oil was \$37 per barrel. Although the company was struggling to exist it did not mean the company was at risk of going out of business. It meant that Caelus was at risk of not being able to make further capital investments and continue to grow its business.

Mr. Foley explained that the state received production out of the producers that received the state's tax credits. The state also received royalty monies equaling close to \$70 million and production taxes of about \$60 million to date.

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Mr. Foley moved to slide 3: "North Slope Exploration & Development Program." He pointed to the left top portion of the slide. He reported that out at Smith Bay in Tulumaniq Caelus had drilled 2 very exciting exploration wells. The wells were very expensive and the company would be spending well over \$100 million to drill the 2 wells. He reported that currently the operations were finishing, the company was encouraged by the results, and it had started making plans to be back in the near future to continue its appraisal. At Ooguruk, the cornerstone of the company's business, the costs were higher than most of the North Slope fields because it was a remote island site. The company produced anywhere from 10 thousand to 20 thousand barrels per day because of the frack nature of production. Caelus drilled wells all year, fracked them, and brought them online. The company saw really high production rates in the summertime and then they depleted. In the following year they would drill all over again. He pointed to the next picture of Nuna, a project in the process of being developed. It was a project Caelus committed to at higher oil prices. He admitted that the company was struggling to keep the pad that had nothing on it. Lastly, the company had acquired a 325 thousand acre block in the far eastern portion of the North Slope. It was to the East of Prudhoe Bay and to the west of Point Thomson. Even before the oil and gas leases were issued Caelus had begun a high resolution seismic 3D acquisition program. Caelus was chasing the same reservoirs at Smith Bay, Ooguruk, Nuna, and in the East. They were the same type crummy reservoirs that the company thought it would be the master of unlocking.

Vice-Chair Saddler asked about the term he had used, "crummy" reservoir.

Mr. Foley responded, "Sadly I did say crummy."

Vice-Chair Saddler thought there was some technical term he was missing.

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Representative Wilson asked about the odds of Caelus coming back if the state started changing its tax regime again.

Mr. Foley indicated that he had a slide that specifically addressed Nuna, potential opportunities, and what would have to happen for Caelus to move forward with its investment.

Mr. Foley turned to slide 4: "Alaska: An Attractive Investment Opportunity?" He had mentioned before that he had worked internationally as a negotiator and in a strategic planning group. The group evaluated new opportunities by answering several questions that were listed on the slide. The questions included whether the resource was world class, whether there was access to infrastructure, whether there were leases available, whether there was an expert community of contractors, and whether the regulatory environment could be managed. Alaska received fairly high marks in the answers to these questions. However, there were some downsides to investment opportunities in Alaska. First, Alaska was an expensive, cold, and remote operating environment. Another question his group answered was whether Alaska's fiscal regime was favorable. He relayed that under SB 21 it was very favorable. The changes currently being contemplated would make the regime unfavorable. Another question to answer was whether the fiscal regime was stable and predictable. In his history he had seen about 5 or 6 tax regime changes in the prior 10 years. Alaska received very poor marks in fiscal regime stability. Caelus was a company that went to outside sources for its capital. The company's investors needed to have confidence in the system. He reported that investors were very nervous about continuing to invest in Alaska.

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Mr. Foley advanced to slide 5: "Alaska Oil Tax Policy - Integrated Tax System." He acknowledged that the slide was borrowed from analytica. The slide showed the government's take over a broad range of prices. He explained that government take was determined by profit and distribution. Gross revenues minus costs equaled profit which was then shared. He relayed that SB 21 reflected a fiscal system that was flat over a very broad range of prices. He pointed to the dotted line on the chart that depicted the government take over a range of prices. He highlighted that from \$70 and up the government take remained shockingly flat. At the lowest end, reflecting current prices, 100 percent of the take went to the state. There was nothing left for the investor.

Representative Wilson wondered if there was an issue with SB 21 or with the price of oil.

Mr. Foley answered that the company was struggling first because of price. Secondly, the company was concerned about what would happen in the future. He furthered that under SB 21, an integrated balanced system, companies were allowed to earn tax credits by doing work. He suggested members to think of it as an early assistance provided by the state to fund and move projects forward. In exchange, companies would pay a larger piece once a project got off the ground and became profitable.

Representative Wilson had heard of the benefits of SB 21 at high oil prices such as \$90, \$100, and \$120. The reason a change was being considered was because the legislature had not properly considered the regime at low prices of the present day. She asked if Mr. Foley agreed with her statement.

Mr. Foley agreed that oil at high prices was the only scenario people had envisioned. He did not think that anyone had contemplated oil at \$37 per barrel.

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Representative Wilson asked if Mr. Foley thought the changes being considered would fix the situation the state was in.

Mr. Foley thought the changes exacerbated the problem rather than helping the problem.

Vice-Chair Saddler asked if the dark blue or purple on the chart represented the producer take.

Mr. Foley suggested directing the question to enalytica. The dark blue was not represented in the key.

Mr. Foley moved on to slide 6: "Tax Program Changes & Impacts to Caelus." He explained that the slide represented the impacts that the original bill, HB 247, would have upon Caelus. The slide showed the net present value (NPV) on a life-cycle basis of the company's current project inventory. It included Ooguruk and Nuna using strip prices similar to current prices. Over the course of the following 5 years the price would creep up every year until, in about 5 years, the price would be about \$52 and it would be flat forever. He thought it was unsustainable. The slide tried to walk through the additive impacts of the various pieces of the initial bill offered by the administration. The first impact was the GVR fix. Caelus was one of the company that earned a net operating loss. The way the statues and regulations were written they allowed Caelus to basically increase its net operating loss by applying the GVR. Some people claimed it was an unintended consequence and needed to be removed. From his prospective he had assumed it was an intended consequence because the taxes were starting to increase under SB 21 and the credit system was changing. He saw it as something that could balance them. He understood the legislature's belief and the public's concern and suspected he would lose on the issue the result of which would erode the value of his business by about 13 percent. The bars on the graph demonstrated the impact on an NPV basis created by each proposed change.

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Vice-Chair Saddler asked about his NPV rate assumption and to define "strip price."

Mr. Foley responded that the graph represented a NPV discounted at 10 percent. The strip price was what the financial markets predicted would be the price of oil. Currently, they predicted that the price would be what it was at present. It assumed a very modest increase each year for the following 5 years at about \$52 per barrel.

Vice-Chair Saddler remarked that NPV at 10 percent was a fairly high assumption. He asked Mr. Foley to comment.

Mr. Foley answered that when companies made economic evaluations they considered what they would look like at various NPV amounts. The next bar depicted the negative impact of hardening the floor. At present, because the company was at a NOL position and because it was a small start-up business it could actually use all of its credits to go below the floor. He confirmed there was a gross minimum tax floor but the credits allow the company beneath that floor. Presently Caelus did not pay a production tax. If the legislature changed legislation resulting in the creation of a 4 percent hard floor it would erode the value of his business by (plus the GVR fix so they were additive) 31 percent. The next piece showed the impact of a \$25 million transferable credit limit which eroded the company's value down to 77 percent erosion. The final element of change that impacted the company's value was an increase in a hard firm floor from 4 percent to 5 percent. At the end of the day with the proposed changes his business would be worth 17 percent of what it was worth prior to HB 247.

Vice-Chair Saddler asked if he had any information regarding the effect on his business at the \$200 million credit limit.

Mr. Foley reported Caelus having a capital budget of about \$300 million and the company would earn NOL plus EIC credits equal to about \$100 million.

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Mr. Foley continued to slide 7: "Nuna: A Project on the Bubble." He explained that the project was ready to go: the gravel was installed, all of the engineering design was complete, and equipment was queued up for purchase. However, the project was placed on hold due to the oil price decline. The project would remain on hold until oil prices recovered and Alaska stabilized its tax policy. Originally, Caelus had anticipated having first oil for the Nuna project in the fourth quarter of 2017. Unfortunately the company would not be able to meet the timeline. He estimated at least a year delay. He relayed details of the project. Caelus owned 100 percent of the working interest.

There was just more than 100 million barrels of reserves. At peak production it would generate 20 thousand to 25 thousand barrels of oil per day. It would employ about 300 fulltime contractors for the first 2 years during construction. It would have 300 fulltime employees for 4 to 5 years of the drilling phase. He commented on all of the economic benefits the state would enjoy because of all of the direct jobs and the 20:1 multiplier effect. In addition, the project would bring future revenues to the state of approximately \$1.75 million. The payments came from the integrated fiscal system create by the state. There would be \$900 million royalty payments as well as \$500 million in net profit share lease payments. There would also be future production tax payments in the amount of about \$250 million and property tax payments of about \$100 million.

Mr. Foley reported that one question regularly posed was whether the state provided more credits than the company paid back in production tax. It showed that the Nuna project at the current prices earned NOL transferable cash payments of about \$250 million and in the future Caelus would pay that money back. Coincidentally, at the current price it would equal about \$250 million paid in future production tax payments. He considered it a wash. In addition, Caelus would pay \$1.5 billion in royalty, net profits, and property tax payments to the State of Alaska.

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Representative Gara asked if Nuna was a GVR field.

Mr. Foley answered that both Nuna and Ooguruk were GVR fields. He reminded members that they were GVR fields at the rate of 20 percent. At the time SB 21 came about it was a field intended to be eligible for a 30 percent GVR. However, SB 21 was written such that it excluded any leases with a field with a one-eighth royalty. At the time he believed that his lease would qualify because it was a one-eighth plus lease. However, it turned out that he was not eligible for a 30 percent GVR.

Representative Gara asked what oil price Mr. Foley had assumed in his estimation of \$1.7 billion in future payments.

Mr. Foley responded that the work was done at \$70. He noted that it did not make sense to do it at strip prices because otherwise Nuna would not likely happen.

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Mr. Foley turned to slide 8: "Closing Thoughts." He urged members, as they contemplated changes, to make sure that the changes the legislature made would incent the behaviors that the state wanted. He believed SB 21 was a very balanced system. He thought that SB 21 and the credit system were the reasons why Caelus was in Alaska. He reported that when Caelus had evaluated opportunities in Alaska it came to the conclusion that there were great opportunities even though prices were high and the fiscal regime was unfriendly. Under SB 21 because of the credit system it incented Caelus to close on the purchase with Pioneer and to commit to the Nuna project, buy 325 thousand acres of leases in the East, shoot a high resolution 3D, and drill 2 exciting exploration wells at Smith Bay.

Representative Wilson asked if he had been consulted by the administration about any possible proposals and their potential impact.

Mr. Foley indicated that he had had more than one opportunity to speak with the administration. He was able to share his concerns. He could not say anything more than the bill was what it was.

Representative Wilson asked about the per barrel price it would need to reach to be profitable and to allow for the continuation of the project.

Mr. Foley stated that the work was done at \$70 per barrel oil. He was unsure of the price necessary to move on with the project. He estimated that it was in the neighborhood of \$70 million.

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Representative Pruitt asked if he had seen an increase in taxes in any other regimes Caelus operated.

Mr. Foley relayed that the company only acted in Alaska.

Representative Pruitt referred to slide 7 and pointed to the \$250 million in NOL cash payments from the State of Alaska as well as the other benefits. He asked about whether the project would move forward if the legislation moved forward.

Mr. Foley answered that, in regards to tax law changes, the company needed to reach a certain economic threshold. The more erosion the company suffered due to tax change the more the price would have to increase to offset costs. For example, if the project was done at \$70 per barrel and the system changed it would take a higher price. Representative Pruitt asked if the company was looking to invest in other projects.

Mr. Foley responded in the affirmative. He added that Caelus' large exploration block out to the East was one of them. He hoped to drill some wells in the future. He hoped for a follow up season at Smith Bay which he also hoped would lead to development. He mentioned that the one underlying theme that keeps coming about was the concern that the payment of transferable NOL credits was a drag on the system. There was a fear that the amount of monies that the state would have to pay for the credits would be very high. He argued that it was a problem that sadly was self-correcting. He explained that at high prices the projects would go forward and would likely earn credits but it would be in a time when Alaska's economy was more robust and the state would have the ability to fund those credits. In a very low price environment like the state was currently, sadly the projects would not go forward and there would not be investments and there would not be NOL's that the state had to reimburse.

Representative Pruitt asked if Caelus had already received credits from the state for the Nuna project and Oooguruk project. He wondered if it was fair to say that if the projects did not go forward the state paid money on something it would not receive a benefit.

Mr. Foley responded, "Yes, we have made expenditures on a project like Nuna. We have incurred losses. We have earned transferable NOL credits and, you are exactly right, if the project does not go forward, there would be no future revenue to the state for that project."

Vice-Chair Saddler thanked Mr. Foley for his testimony. He directed him to submit his written testimony.

SB 247 was HEARD and HELD in committee for further consideration.

Vice-Chair Saddler discussed the agenda for the following meeting.

ADJOURNMENT

5:05:41 PM

The meeting was adjourned at 5:05 p.m.