

**ALASKA STATE LEGISLATURE  
HOUSE RESOURCES STANDING COMMITTEE**

February 26, 2020

2:10 p.m.

**MEMBERS PRESENT**

Representative Geran Tarr, Co-Chair  
Representative Grier Hopkins, Vice Chair  
Representative Sara Hannan  
Representative Chris Tuck  
Representative Ivy Spohnholz  
Representative Dave Talerico  
Representative George Rauscher  
Representative Sara Rasmussen

**MEMBERS ABSENT**

Representative John Lincoln, Co-Chair

**COMMITTEE CALENDAR**

PRESENTATION(S): ANALYSIS OF "FAIR SHARE ACT"

- HEARD

**PREVIOUS COMMITTEE ACTION**

No previous action to record

**WITNESS REGISTER**

RICH RUGGIERO, Chief Executive Officer  
IN3ENERGY  
Houston, Texas

**POSITION STATEMENT:** Co-provided a PowerPoint presentation, titled "190GTX Review Alaska Legislature February 2020."

CHRISTINA RUGGIERO, Managing Member  
IN3ENERGY

Houston, Texas

**POSITION STATEMENT:** Co-provided a PowerPoint presentation, titled, "190GTX Review Alaska Legislature February 2020."

**ACTION NARRATIVE**

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CO-CHAIR GERAN TARR called the House Resources Standing Committee meeting to order at 2:10 p.m. Representatives Hannan, Talerico, Spohnholz, Hopkins, Rauscher, and Tarr were present at the call to order. Representatives Tuck and Rasmussen arrived as the meeting was in progress.

**PRESENTATION(S): ANALYSIS OF "FAIR SHARE ACT"**

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CO-CHAIR TARR announced the only order of business would be an analysis of the Fair Share Act Initiative [2020 190GTX Ballot Measure].

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RICH RUGGIERO, Chief Executive Officer, IN3ENERGY, explained that both presiding officers of the Alaska State Legislature had requested an analysis of the wording of the Fair Share Act Initiative from the standpoint of IN3ENERGY's experience in writing legislation, regulation, and contracts. He said IN3ENERGY studied the initiative and, with its background in oil taxation and AS 43.55, put together its analysis. He pointed out that the slides of the PowerPoint presentation do not contain everything that is in the memorandum [from Mr. Ruggiero to Representative Tuck, dated 2/25/20, included in the committee packet]; therefore, he encouraged the committee to ask questions within each section, as needed.

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CHRISTINA RUGGIERO, Managing Member, IN3ENERGY, directed attention to a PowerPoint presentation entitled, "190GTX Review Alaska Legislature February 2020" [hard copy included in the committee packet]. She noted that slide 4 contained a glossary to clarify that in the presentation, "190GTX" would be called "Initiative." She further noted that the oil producing asset that meets the qualification criteria in Section 2 of the Initiative would be referred to as "40/400."

MR. RUGGIERO further clarified 40/400 refers to 40,000 barrels of oil per day (bopd) and 400 million in cumulative production. He remarked that IN3ENERGY does not know the definition of field or a "non-unitized reservoir," and he said he would be discussing that later. He explained that IN3ENERGY wanted to

keep terms generic so as not to form opinions about what they meant.

MS. RUGGIERO restated that the IN3ENERGY analysis is based only on the two-page Initiative and IN3ENERGY's prior knowledge and experience. She drew attention to slide 6, which provided a summary of the Initiative, and she discussed the bullet points on slide 6, which read as follows [original punctuation provided]:

- Based on our petroleum fiscal policy experience we conducted a review of 19OGTX, the Initiative, that looks to raise additional revenue from production taxes
- In general, the Initiative lacks necessary specificity making it improbable that a common interpretation could be reached. Alternative interpretations of the Initiative are possible
- The Initiative seems to be written to satisfy a goal of increasing revenue from production tax in the near term. It does not contain any provisions which are designed to encourage or incentivize investment and production
- If the voters approve it, there will very likely be an extended period of uncertainty within the petroleum industry as all interested and impacted parties attempt to push their interpretation of what is written

MS. RUGGIERO addressed the bullet points on slide 7, a summary of the Initiative, which read as follows [original punctuation provided]:

- Producers pay the state 4 different types of taxes:
  - Royalty
  - Property Tax
  - Production Tax
  - Corporate Income Tax
- The Initiative only makes changes to the Production Tax
  - Creates increased gross minimum tax
  - Creates a net tax on PTV
  - Maintains the 'greater of' structure

- The Initiative eliminates the use of the GVR and non-GVR per-barrel credits for assets that qualify under Section 2

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MS. RUGGIERO moved on to slide 9, which addresses Section 1 of the Initiative. Section 1, as shown on slide 9, read as follows [original punctuation provided]:

**Section 1.** The uncodified law of the State of Alaska is amended by adding a new section to read:

SHORT TITLE. This Act shall be know as the "Fair Share Act."

**Notwithstanding Any Other Statutory Provisions to the Contrary, the Oil and Gas Production Tax in AS 43.55 Shall Be Amended as Follows:**

MS. RUGGIERO covered the bullet points shown on slide 9, which read as follows [original punctuation provided]:

- Titled the "Fair Share Act" , there is no language to define what constitutes a fair share of certain oil revenues for Alaska. Without a defined goal, where ambiguity exists numerous interpretations will be possible
- With the inclusion of the term "Notwithstanding" it appears the language of the Initiative is to override existing production tax calculations contained in AS 43.55 for assets that qualify under Section 2
- The only direct reference to a particular part of AS 43.55 and changes to it are in Section 4 paragraph (a), the per barrel credits

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MR. RUGGIERO, in response to Representative Tuck, said "Fair Share Act" appears in the title but, to his understanding, not anywhere in AS 43.45. In response to a follow-up question, he emphasized the ambiguous nature of the Act and reasserted that the result would be litigation, and one of the determinations that would need to be made would be what "Fair Share" meant.

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MR. RUGGIERO, in response to a question from Representative Rasmussen, clarified his observation that while the Act would raise taxes, it does not include language that "incentivized anything." He said usually there would be credits as incentivization, but outside of those already in AS 43.55, there is no further incentivization. He said that when an investor does not know how the investment dollar will be treated, that has "a significant negative impact on economics." He said that during his "big oil days," this [Act] would have given him pause, and he would have asked his "folks" to "hold off on anything that we weren't committed to until we found out exactly how this was going to work if this initiative passed." In response to another question from Representative Rasmussen, he said based on the research of IN3ENERGY, there is no chance of increasing oil production in the immediate future, which he speculated meant a couple of years before there was any certainty about "what's going to happen here."

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CO-CHAIR TARR, in response to Representative Rauscher, explained the origin of the short title of the Initiative.

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MS. RUGGIERO, in response to Representative Spohnholz, said no incentives were being offered through the Initiative.

MR. RUGGIERO, in response to a follow-up question, confirmed that any incentives already in AS 43.55 would remain; the Initiative does not add any new incentives.

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MR. RUGGIERO, in response to Representative Rasmussen, said the "existing language" creates the right incentives, as evidenced by the number of tax credits created. People spent money as a result of the incentives. He clarified that "the business uncertainty" would cause either a slowing down or halting of spending by "various parties." In response to a follow-up question, he confirmed that even with the existing incentives in place, he thinks the Initiative would have a major [negative] impact on the business decisions that would be made.

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MR. RUGGIERO returned to the PowerPoint presentation, to slide 11, which addresses Section 2 of the Initiative and the applicability of the new law. He remarked that he was "adding up all the ambiguity." Section 2, as shown on slide 11, read as follows [original punctuation provided]:

**\*Section 2, Applicability.** The provisions in Sections 3 and 4 only apply to oil produced from fields, units, and nonunitized reservoirs north of 68 degrees north latitude that have produced in excess of 40,000 barrels of oil per day in the previous calendar year and in excess of 400,000,000 barrels of total cumulative oil production. For other oil production, the tax shall be unchanged by the Act.

MR. RUGGIERO covered the bullet points on slide 11, which read as follows [original punctuation provided]:

- This section is used to define which North Slope oil and gas assets will be subject to the new taxes in the Initiative
- It applies to "fields, units and nonunitized reservoirs"
- Producing assets qualify if they have produced in excess of 40,000 bopd and have produced more than 400,000,000 barrels over the life of the asset (hereinafter referred to as "40/400 Assets")
- While we believe the description was to isolate three fields, the above language is not straightforward and raises several questions

MR. RUGGIERO said he cannot reason why the drafters of the Initiative would use terms that were not used in AS 43.55. He moved on to slide 12, which highlighted "fields, units, and nonunitized reservoirs" and covered the following [original punctuation provided]:

- AS 43.55 primarily uses "leases and properties" throughout to refer to oil and gas operations in the state. We did not find any usage of the phrase "fields, units or nonunitized reservoirs" in any statute or regulation governing the taxation of oil and gas

- We are unable to discern why terms not common to AS 43.55 would be chosen to assess against the qualification criteria
- It is unclear whether it defines three types of assets, i.e. fields, units and nonunitized reservoirs, or whether that term is to be interpreted as a singular grouping. Likewise, there is no reference to determine what the intended definition(s) is(are) for fields, units and nonunitized reservoirs

MR. RUGGIERO said IN3ENERGY made the assumption that the drafters of the Initiative intended for fields, units, and non-unitized reservoirs to be considered "three different types of assets."

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MR. RUGGIERO shared the bullet points on slide 13, which read as follows [original punctuation provided]:

- While the term 'field' is very common in the oil and gas industry, we looked in statute and regulations for a more precise Alaska definition
- Various Alaska agencies describe operations and publish data for wells, pads, leases, pools, participating areas, fields, units and general areas such as North Slope, Middle Earth and Cook Inlet
- AS 31.05.170 defines, for that particular chapter, "field" as a general area which is underlain or appears to be underlain by at least one pool, and includes the underground reservoir containing oil or gas. More than one pool can be part of a defined field

MR. RUGGIERO explained that although "field" is a common term used in the industry, it is important to consider how terms are used by the State of Alaska in order to consider the Initiative. He indicated that IN3ENERGY's research through Alaska regulations showed the term "field" defined loosely depending on which source was used.

MR. RUGGIERO directed attention to the bullet points on slide 14, which read as follows [original punctuation provided]:

- Neither AS 43.55 nor the Initiative provide any guidance on what grouping of wells constitute a 'field'
- Under AS 43.55.900 "unit" is defined and means a group of tracts of land that is subject to a cooperative or a unit plan of development or operation that has been certified by the commissioner of natural resources under AS 38.05.180(p)
- The North Slope contains a number of "units". Each unit contains a number of pools and fields

MR. RUGGIERO named Prudhoe Bay Unit, Kuparuk River Unit, and Pikka Unit as units with which the committee would be well aware. He noted that AS 43.55 addresses taxation.

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MR. RUGGIERO paraphrased the bullet points on slide 15, which read as follows [original punctuation provided]:

- It appears there are two ways to qualify as a 40/400 Asset: (1) the combined daily production and the combined cumulative production of all the pools and fields in a unit meet the two threshold levels, or (2) a single 'field' within a unit meets the two threshold levels which by definition then the field and entire 'unit' of which it is part of would both qualify as a 40/400 Asset
- The 'fields' qualifying as 40/400 Assets are Alpine, Kuparuk and Prudhoe Bay. Because those fields qualify then the Colville River Unit, Kuparuk River Unit and Prudhoe Bay Unit are 40/400 Assets as well

MR. RUGGIERO said he thinks that primarily, either a field - when its definition is determined - or a unit qualifies, but the interesting question is, "What if a field is also part of the unit?" He explained that upcoming was language that would require a tax return for each field and each unit; therefore, there is a question of whether there may be double taxation or "all sorts of very interesting regulations on how to sort that out," because the Initiative appears to require separate tax returns.

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CO-CHAIR TARR summarized that under the Initiative, it is possible, for example, that the Prudhoe Bay field could qualify other fields within the unit to also be taxed.

MR. RUGGIERO directed attention to the map on slide 16, with red circles around the areas that would likely qualify as 40/400 assets: Colville River Unit, Kuparuk River Unit, and Prudhoe Bay Unit. He drew attention to slide 17, which shows that the Colville River Unit consists of the following six pools: Alpine Oil, Fiord Oil, GMT1 Undef Oil, Nan-K Oil Term, Nanuq Oil, and Qannik Oil. He continued:

So, I don't know whether Alpine field is just Alpine Oil or whether it's Alpine plus the other five that are there. If it's just the Alpine Oil pool, then also the Colville River Unit will qualify as a 40/400 asset .... We've got both the field, and then the unit that it's a part of, and then that pulls in all the smaller pools, as well, to be qualified in there.

MR. RUGGIERO showed slides 18 and 19, which list the oil pools in the Kuparuk River Unit and Prudhoe Bay Unit, respectively. He reiterated that in terms of qualification, the reach could be broad or narrow depending on the definition of terminology.

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MR. RUGGIERO, paraphrased the bullet points on slide 20, which read as follows [original punctuation provided]:

- We were unable to find any definition for "nonunitized reservoir" in Alaska statute or regulation.
- In industry a "unitized" reservoir is a reservoir that crosses ownership boundaries. That agreement decides on how much of the reserves are owned by each party, what the optimum development plan and the naming of the operator. A unitization agreement is for the operation of a single reservoir.
- Units in Alaska do not represent the unitization of a reservoir.

- One alternative interpretation is that all wells that produce from the same reservoir could be deemed a "nonunitized reservoir"

MR. RUGGIERO said in Alaska there are formations that run across the North Slope; therefore, it could be said that every well that is in the same formation and the same reservoir would, if they all met the requirements, become a 40/400 asset. For example, if everything in West Sak, which "goes across the [North] Slope," becomes part of a nonunitized reservoir, then "collectively all that could work towards qualifying for being covered under Section 2."

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MR. RUGGIERO paraphrased confusing aspects of the Initiative regarding production, shown in the bullet points on slide 21, as follows [original punctuation provided] :

- It is unclear whether production has to average over 40,000 bopd for an entire year or only exceed 40,000 bopd on a single day in the previous year
- Use of a couple extra words, such as "averaged" or "produced on any day" would have easily provided clarity
- For 40/400 Assets, do the new taxes apply beginning January in the following year? Do they apply for an entire calendar year if during a year the production falls below 40,000 bopd? The Initiative provides no direction or clarity

MR. RUGGIERO discussed further points of confusion, shown in the bullet points on slide 22, as follows [original punctuation provided] :

- In the future, some new units may have production above 40,000 bopd but have not yet reached the cumulative criteria of 400,000,000 barrels
- Once the cumulative production exceeds 400,000,000 barrels do the new taxes apply immediately or do they apply at the start of the next calendar year? There is no language to guide this decision

- Where is production to be measured? Barrels sold to the market? Barrels into TAPS [Trans-Alaska Pipeline System]? Or, wellhead barrels? How are barrels consumed in field operations counted? Section 2 just mentions barrels
- Does Section 2 refer to the production of total barrels or taxable barrels? As much as a +/- 12% difference

MR. RUGGIERO said there can be a 5-10 percent difference between wellhead and market; a 10 percent difference on 400 million is a lot of barrels and days of production where "you're either in or you're not in, under Section 2, as a [40/400] asset." He said these are significant questions as to when this would actually take effect.

MR. RUGGIERO gave a summary of Section 2 of the Initiative, which is shown in the bullet points on slide 23, as follows [original punctuation provided]:

- It appears the intent is to raise taxes only for the large legacy fields of Alpine, Kuparuk and Prudhoe Bay
- Depending on how fields, units and nonunitized reservoirs are defined, there are numerous possible interpretations, some which could have much more of the current North Slope production qualifying as 40/400 Assets
- Other than being immediately applicable to the three large fields, it is unclear when the new taxes begin to apply and when they stop applying

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MR. RUGGIERO responded to questions from the committee. In response to Representative Rauscher, he explained that the confusion he had expressed regarding a starting date had to do with what day the taxes under the Initiative would "kick in." He said, "This Initiative is silent on when that would occur." In response to a question from Representative Rasmussen, as to whether fiscal year versus calendar considerations would have any impact on investment, he said the taxation is set by calendar year, which is offset from Alaska's fiscal year. In response to a follow-up question, he emphasized that any confusion created under the Initiative would lead to "a high

degree of uncertainty from the producers as to what game they're playing in," which would result in producers holding back until they understand the rules of the game.

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MR. RUGGIERO, in response to Co-Chair Tarr, suggested that clearer articulation might be: "all units on the North Slope that exceed 40/400." He explained that the units are a known factor.

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MS. RUGGIERO proffered that Mr. Ruggiero was referring to an option in which a term is used that is already defined or a definition is created where there is none. She added, "But using the field, units, and nonunitized reservoirs -- there's a possibility of interpretation that sets a very wide net and in which case the state would be taxing more areas than is likely intended."

MR. RUGGIERO, in response to Representative Rasmussen, said IN3ENERGY did not look for any prior court cases, and he said he is not "aware of anything like that."

MS. RUGGIERO added that even if there was a case somewhere else, she would seek for clarity in Alaska's terminology.

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MR. RUGGIERO, in response to Representative Hannan, confirmed that Alpine, Kuparuk River, and Prudhoe Bay Units have all met the 40/400 measure. In response to a follow-up comment, he noted that in the past, smaller units have been consumed into larger units for purposes optimization. Some newer players could be concerned that if consumed into a larger unit, they would be considered from day one to be 40/400 assets, even though they had not yet produced, because the larger unit into which they were captured was already qualified.

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MR. RUGGIERO, in response to Representative Hopkins, clarified that sometimes an independent unit goes through its initial "exploration, appraisal, and development plan," and there is nothing to prevent Alaska Oil and Gas Conservation Commission (AOGC) or others to decide it is better if that independent unit

is consumed into another existing unit. He said it does not have anything to do with "whether or not they know what's under the ground." He explained, "How units here are created are at the convenience of operations and optimization, whereas elsewhere units are created because it's a common reservoir." In response to a follow-up question, he confirmed that the common reservoir is where the lease applications would impact taxation.

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MR. RUGGIERO, in response to a question from Representative Talerico, confirmed that one issue is that there are operators in Alaska that are operating more than one unit. In response to a follow-up comment, he said he would be addressing the creation of multiple tax returns when addressing Sections 5 and 6.

MR. RUGGIERO, in response to Representative Hannan, said AS 43.55.160 creates a series of six or seven ringfences in Alaska for tax purposes. An operator with operations in each of those ringfences would have to do six or seven tax returns; however, an operator operating only on the North Slope, for example, would submit only one tax return. In response to Co-Chair Tarr, he said it's just one tax return on the North Slope, "unless gas is used in state," which he indicated was addressed under AS 43.55.160(b).

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MR. RUGGIERO, in response to a question from Representative Hopkins as to whether producers have the ability to designate the field units in their reservoirs or whether that is done by AOGCC or some other entity, said he does not know the process.

MR. RUGGIERO, in response to a comment from Representative Tuck that the presentation was not intended for guessing at the intent of the Initiative but to look at the language as written, said he agrees; however, some ambiguities could result in the difference of millions of dollars. For example, he said while there may not be much pushback regarding the average for the year or a single day, in terms of whether the language is "barrels" or "taxable barrels" there is a difference of 50 million barrels to get to the cumulative, and that is a lot of oil that either does or does not get taxed under the Initiative. He said there could be "a good fight over that," especially since everything in AS 43.55 addresses taxable barrels - not total barrels.

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MS. RUGGIERO brought the committee's attention back to the PowerPoint and began discussion of Section 3(a), the language of which was shown on slide 25, as follows:

**\*Section 3, Alternative Gross Minimum Tax** For oil production from fields, units, and nonunitized reservoirs that meet the conditions in Sec. 2, the amount of tax due for each calendar month shall be no less than:

(a) 10 percent of the gross value at the point of production when the average per-barrel price for Alaska North Slope crude oil for sale on the United States West Coast (La. Basin) during the calendar month for which the tax is due is less than \$50;

MS. RUGGIERO paraphrased the bullet points on slide 25, which read as follows [original punctuation provided]:

- This is a monthly gross tax that appears to replace the current gross minimum tax that ranges from 0% to 4% of the GVPP with a new gross tax ranging from 10% to 15% of the GVPP
- The Initiative does not contain any language specifically altering the definition of GVPP from how it is defined in current statute
- It is unclear why the parenthetical (La. Basin) has been added to the definition of the ANS WC trigger price and what change that would cause from current statute

MS. RUGGIERO explained that since the definition of gross value at the point of production (GVPP) is not altered in the Initiative, IN3ENERGY assumes it remains the same as it is in AS 43.55. She moved on to slide 26, which showed Section 3(b), as follows [original punctuation provided]:

(b) an additional 1 percent of the gross value at the point of production for each \$5 increment by which the average per-barrel price for Alaska North Slope crude oil for sale on the United States West Coast (La. Basin) during the calendar month for which the tax is due is equal to or exceeds \$50. The maximum

tax rate calculated in this section shall not exceed 15 percent, which is reached when the price per barrel is equal to or exceeds \$70; and

MS. RUGGIERO directed attention to the bullet points on slide 26, which read as follows [original punctuation provided]:

- The language is not clear if the 1% gross minimum tax increase at prices above \$50 per barrel is in step increments of \$5 or if the increase is continuous (like progressivity) at the rate of 1% per \$5 increase
  - e.g. at \$53 ANS WC is the applicable tax rate  
11% [10%+1% >\$50 but<\$55] or 10.6%  
[10%+1%\*(\$3/\$5)]
- A step function would be consistent with current gross minimum tax language. This could have been made clear and unambiguous
- For some reason the last sentence does not define where the price per barrel is to be taken from

MS. RUGGIERO turned to slide 27, which illustrated the gross tax changes between current statute and initiative when a step function and \$70 Alaska North Slope crude sales price on the West Coast of the United States (ANSWC) are assumed. She explained that under the current system, "you top out at the 4 percent at \$25 per barrel and above," and under the Initiative there would be a 10 percent tax on amounts up to \$50 and "anything above \$70 would be taxed at the 15 percent."

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MR. RUGGIERO drew attention to Section 3(c), on slide 28, which read as follows [original punctuation provided]:

(c) No credits, carried-forward lease expenditures, including operating losses, or other offsets may reduce the amount of tax due below the amounts calculated in this section.

MR. RUGGIERO discussed the bullet points on slide 28, which read as follows [original punctuation provided]:

- Under AS 43.55, when calculating the applicable gross tax there are no provisions for adjusting the

GVPP, through the use of credits, net operating losses ("NOLs") or similar

- Deductions from GVPP are allowed under AS 43.55 to derive the PTV
- As such, we do not see why paragraph (c) is included in this Section versus Section 4
- If the intent was to make the gross tax calculation a hard floor, that could have been explicitly written

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MR. RUGGIERO, in response to Co-Chair Tarr, clarified what he meant by "pierce the floor." He said under AS 43.55, a gross minimum tax is calculated, and then the net tax is calculated, and then "you take the greater of the gross or the net." He offered an example to show that "there are things that ... pierce that minimum floor, and there are other things that cannot." He said IN3ENERGY thinks the intent of the Initiative is that no other deductions or credits would be allowed to pierce the floor.

MR. RUGGIERO indicated that IN3ENERGY was asked what an offset was. He noted that AS 43.55 does not use the term "offsets." He surmised that the drafter of the Initiative was including "a catchall" to "make it as big as they want" or "as narrow as they want" by using an undefined term.

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MR. RUGGIERO, in response to Representative Hopkins, said AS 43.55 uses the term "ANS West Coast price" and, for some reason, the drafter of the Initiative has added "(La. Basin)". He said it was unclear whether the term was being added to imply a difference. He said in this instance, "La." refers to Los Angeles, and he interprets the Initiative to mean that for the purpose of the gross tax, the price at the "La." Basin would be used. In response to Representative Hopkins, he confirmed his understanding that this was not just about Alaska oil but about oil sold in the "La." Basin.

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MR. RUGGIERO continued the PowerPoint presentation and discussed Section 4 of the Initiative, which is written on slide 30, as follows [original punctuation provided]:

**\*Section 4, Tax on Production Tax Value.** For production from fields, units, and nonunitized reservoirs that meet the conditions in Sec. 2:

(a) The per-taxable-barrel credit in AS 43.55.024(i) and (j) shall not be used; and

(b) An additional production tax shall be paid for each month for which the producer's average monthly Production Tax Value of taxable oil is equal to or more than \$50. The additional tax shall be the difference between the average monthly Production Tax Value of a barrel of oil and \$50, multiplied by the volume of taxable oil produced by the producer for the month, multiplied by 15 percent.

MR. RUGGIERO highlighted the first bullet point on slide 30, which read as follows [original punctuation provided, with a technical change]:

- [Subsection] (a) clearly and explicitly states that the credits now allowed in AS 43.55.024 (i) and (j) shall not be used for 40/400 Assets

MR. RUGGIERO then directed attention to slide 31, which focused on [subsection](b) of Section 4. He paraphrased the bullet points, which read as follows [original punctuation provided]:

- Under AS 43.55 both the gross tax on GVPP and the net tax on PTV are referred to as a "production tax"
- Given the above, it is unclear whether "An additional production tax" means (1) another production tax in addition to the Section 3 production tax; or (2) an additional tax on top of other production taxes currently in AS 43.55
- Nowhere in the Initiative is there any direct or implied reference to the current applicable net tax on PTV in AS 43.55

MR. RUGGIERO directed attention to slide 32, where "of taxable oil" and "of a barrel of oil" in [subsection] (b) of Section 4 are shown outlined in gold boxes. He paraphrased the

information in the bullet points, which read as follows [original punctuation provided]:

- Two different definitions of PTV are used, PTV "of taxable oil" and PTV "of a barrel of oil"
- PTV "of taxable oil" defines the gross income. It is sales revenues minus transportation and lease costs. It will always exceed \$50
- PTV "of a barrel of oil" is the PTV divided by applicable production to derive a per barrel unit value
- As worded, the additional tax will apply every month

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MR. RUGGIERO said Section 4 applies when the value of taxable oil is above \$50. He said he would bet all his money that every month, the PTV of a qualifying 40/400 asset would be above \$50. He said this means production of just two barrels. He stated, "So, this is always going to be live and always going to be applicable." He then used slide 33 to illustrate that "one is per taxable oil, and the other one is just per barrel of oil." He continued as follows:

So, to get unit value, I take the production tax value, the PTV, and I divide by the quantity of oil. If I'm dividing by total barrels, ... that's a larger number, so the unit value's going to be smaller than if I divide it by taxable barrels. So, again, when we're talking about ambiguity, we mixed PTV "of barrels" with PTV "per barrel," and we mixed taxable barrels with total barrels. So, we've got kind of a confusion. You could put a matrix here and have about 16 different alternative combinations of this, that, and the other to go through there.

MR. RUGGIERO said AS 43.55 always refers to production tax value per barrel of taxable oil. He added, "But that's not what's chosen here."

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MR. RUGGIERO brought attention to Section 5 of the Initiative, shown on slide 35, as follows [original punctuation provided]:

**\*Section 5, Separate Treatment.** For each producer, the taxes set forth in Sections 3 and 4 shall be calculated separately for the following:

- (a) For oil and for gas;
- (b) For each calendar month (annual lease expenditures shall be divided equally among the 12 months of the tax year); and
- (c) For each of the fields, units, and nonunitized reservoirs, the lease expenditures shall be calculated, deducted, and carried forward separately.

MR. RUGGIERO addressed the bullets points on slide 35, which read as follows [original punctuation provided]:

- Section 2 noted the taxes under Sections 3 & 4 can only apply to oil. Section 5 now states the taxes in Sections 3 & 4 apply to gas as well. Both can not be true
- The inclusion of gas here opens the door to any number of interpretations including that gas from 40/400 Assets would be ringfenced from other North Slope gas and taxed via Sections 3 & 4 and not current AS 43.55
- Another possible interpretation is that all costs related to gas are to be separate from oil, not combined as they are now under AS 43.55 and subtracted from oil revenue to determine oil taxes

MR. RUGGIERO directed attention to slide 36. He stated that the slide shows comparisons of disparate language from Sections 2, 3, 4, and 5, explained in the bullet points, which read as follows [original punctuation provided]:

- Note the changing terminology.
- Section 2 "only apply to oil"; then • Section 3 "for oil production"; but
- in Section 4 it only addresses "production" which generically means oil and gas, and then
- Section 5 states the taxes in Section 3 & 4 apply "for oil" and "for gas"

MR. RUGGIERO said, "This is going to be really hard for someone to sort out." He said he would not want to be the person who would have to write out the regulations.

[3:16:38 PM](#)

MR. RUGGIERO turned to slide 37. He said currently, under AS 43.55, there are monthly installments, with an annual "true up" on each producer's taxes on the North Slope. He shared the information on slide 37, which read as follows [original punctuation provided, with a technical change]:

- [Subsection] (b) changes the current monthly installment payments as part of an annual tax return to require a tax return be filed for each month for each 40/400 Asset
- Because the accurate value for 1/12th of the annual lease expenditures is not known until several weeks after the end of the year, an amended return will need to be filed for each month of the prior year for each and every 40/400 Asset
- The Initiative provides no guidance on how to apply tax credits, other carried forward credits or net operating losses to the monthly tax returns. Lacking guidance producers would appear to be free to use these items at their discretion to minimize tax payments

MR. RUGGIERO predicted that because producers cannot know what one-twelfth of an annual lease expenditure will be until the end of the year, each producer, for each asset, would have filed roughly 24 returns - [the 12 monthly ones and 12 corrected ones]. He emphasized that there is nothing in the Initiative that calls for an annual true-up return; it calls only for monthly tax returns.

MR. RUGGIERO, referring back to the terms field, unit, and nonunitized reservoir, said, "We may capture operations that actually have existing - or have generated some - losses or have some credits, et cetera." He said the Initiative does not address how those losses or deductions should be handled, "all of which are applicable against PTV when calculating your net tax." He said someone is going to have to write the rules for addressing this issue.

[3:19:41 PM](#)

MR. RUGGIERO directed attention to slide 38, and he covered the information in the bullet points, which read as follows [original punctuation provided, with a technical change]:

- [Subsection] (c) requires that lease expenditures be treated separately for each 40/400 Asset. Point forward, systems can be put in place to disaggregate future North Slope costs
- However, any existing carry-forward tax credits and operating losses [sic] resulted collectively from all operations a producer had on the North Slope
- The Initiative is silent on their use and likewise silent on how these aggregated amounts are to be separated for each 40/400 Asset. A mechanism will need to be put in place as to how they are to be used for 40/400 Assets. The Initiative provides no direction in this regard
- Costs for common facilities will also need to be identified and allocated to all users

MR. RUGGIERO indicated that there are operations [on the North Slope] that "do not qualify as a 40/400" that are "likely using some of these facilities jointly with a 40/400 asset." Because of the requirement to do separate accounting by each 40/400 qualifying entity, "you're going to have to break it up into all expenses, whether a common use, into the individual entities that use it." He added that he does not know whether that already occurs.

[3:20:46 PM](#)

MR. RUGGIERO, in response to a question from Representative Hannan regarding the gas issue posed on slide 35, proffered that at one time Prudhoe Bay was producing over 300 billion cubic feet per day, "using 400 or 500 for slope use and reinjecting the remainder; so, there is ... gas usage, because they're maintaining a gas cap for pressure. That helps push the oil out." Mr. Ruggiero responded to follow-up questions from Representative Hannan. As to whether any of that gas is currently being taxed, he supposed that there are provisions within AS 43.55 and the tax code wherein the revenue from

"entity A" selling gas to "entity B" would have to be "captured" and reflected in a tax return. As to whether that would be categorized under corporate taxes and expenses versus the state's production structure, he offered his understanding that as long as it is a reservoir captured under the production tax, it would be part of the production tax calculation.

[3:22:51 PM](#)

MR. RUGGIERO, in response to Representative Tuck's reference to the second bullet point on slide 37 and question as to whether there had previously been a one-twelfth monthly progressivity calculation under Alaska's Clear and Equitable Share (ACES) for lease expenditures, recollected that had been the case, although he said he had not reviewed ACES.

[3:23:31 PM](#)

MR. RUGGIERO confirmed Co-Chair Tarr's observation that the true up would have to be done looking back at 12 months. He said one interpretation is that it is a monthly tax return. He said those who write the regulation could choose the current system of a monthly return using an estimate of the one-twelfth, with a true up at the end of the year; however, there is no language within the Initiative that would "drive you to that conclusion."

[3:27:38 PM](#)

MR. RUGGIERO, in response to Representative Rasmussen, offered his understanding that the state audit for oil taxes is presently at 2014. In response to follow-up questions, he said he knows there is a process in place; the Department of Revenue (DOR) has communicated with the legislature, which has determined that the current number of people working on [the audits] is sufficient. He cautioned that if IN3ENERGY's interpretation is correct that there will be monthly returns under the Initiative that will drive the number of returns up exponentially, then that will be a challenge from the standpoint of completing audits. He confirmed that this would increase costs to both the state and the oil companies on the North Slope.

[3:29:07 PM](#)

MR. RUGGIERO, in response to a remark made by Representative Spohnholz, advanced to slide 40, which shows Section 6, as follows [original punctuation provided]:

**\*Section 6, Greater-of.** For each producer, for each month, and for each of the fields, units, and nonunitized reservoirs, the tax due shall be the greater of the tax under Section 3 or Section 4.

MR. RUGGIERO said he does not know how a producer would come up with the tax due figure without having done a tax return. He said there is nothing in the Initiative to indicate the monthly figure would be an estimate or installment, whereas currently under AS 43.55, it is clear that an installment is being paid monthly toward an annual tax return.

[3:32:06 PM](#)

MR. RUGGIERO returned to the PowerPoint and referred again to slide 40, on which the bullet points read as follows [original punctuation provided]:

- The language above explicitly states that the tax due from a producer for a 40/400 Asset shall be the greater of the tax under Section 3 or Section 4
- There is no Initiative reference, direct or implied, to the inclusion of any other taxes under AS 43.55 being applicable for a 40/400 Asset
- The language above only references the tax calculated under Section 4 and not Section 4 in addition to another tax such as AS 43.55.011(e)(2) the 35% tax on PTV
- Section 5 defined items that needed to be treated separately, but never called for each field, unit and nonunitized reservoir to have its own tax return. The use of "each of" above seems to imply that each of the fields, units and nonunitized reservoirs is ringfenced separately for tax purposes. If so, it raises the possibility of double taxation, once as a field and again as a unit

MR. RUGGIERO, regarding the third bullet point, said, "We almost get to the part where the gross tax will always be the controlling, because it's 10 to 15 percent gross on the GVPP, and Section 4 is a net tax only when the PTV's above \$50 a barrel." He said IN3ENERGY thinks Section 4 is not necessary, because Section 3 would be "controlling in all circumstances."

MR. RUGGIERO, in response to a previous comment from Representative Tuck, pointed out that Section 5 did not call for the monthly tax; that is found in Section 6. He explained that Section 6 would require a separate calculation "down to the smallest common denominator, based on whatever you finally agree to be field units and nonunitized reservoirs."

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CO-CHAIR TARR offered the following:

When we talk about getting that PTV: We have the wellhead price and subtract transportation costs, which we estimate around \$10 - that's our GVPP; minus the capital, minus the operating - this is the PTV. So, only after all of those expenses and circumstances where that number is \$50 or above is why you're saying that ... Section 3 is really the most important section relative to Section 4.

MR. RUGGIERO told Co-Chair Tarr that that was a good analysis.

[3:36:16 PM](#)

MR. RUGGIERO, in response to Representative Hannan, relayed that there was discussion about this presentation being given to the Senate, and he indicated that it would likely happen.

[3:37:03 PM](#)

MR. RUGGIERO, in response to Representative Tuck's reference to slide 31 and question as to whether it was clear that the additional tax should not be applied to the gross tax, said there is nothing in the language of the Initiative that "pulls in this bill the 35 percent base tax that currently resides in [AS] 43.55." He said someone had told him that it was obvious that since the Initiative does not overwrite the 35 percent, it must be brought in," to which he had replied that the gross tax in AS 43.55 was not specifically overwritten in the Initiative, "so instead of going from 10 to 15, you're going to go from 14 to 19." He emphasized that the same logic should be applied throughout.

MR. RUGGIERO, in response to Representative Tuck pointing to slide 9 and expressing his confusion over "notwithstanding," stated:

The way I read it is: Notwithstanding that there's a gross tax already there, here's the gross tax, Section 3; notwithstanding there's already a net tax in [AS] 43.55, here's a net tax in Section 4. That's how I read it. Like I said, but if one wants to argue that that's an incorrect interpretation and use of the term "notwithstanding", then again, you have to pull ... both the gross and the net tax that's currently in [AS] 43.55 into this bill.

MR. RUGGIERO, in response to a remark by Representative Tuck that "notwithstanding" could mean not conforming, said Representative Tuck was raising IN3ENERGY's "beginning, overall 100,000-foot view [that] this is technically challenged as a bill." He said the Initiative is unclear, and he reiterated that "it'll be real fun for whoever has to write the regulations to make it work."

[3:40:26 PM](#)

CO-CHAIR TARR announced that the committee would return to the presentation on Friday. She encouraged committee members to follow-up with Legislative Legal Services about the interpretation questions before the next meeting.

[3:42:46 PM](#)

#### **ADJOURNMENT**

There being no further business before the committee, the House Resources Standing Committee meeting was adjourned at 3:42 p.m.