

SENATE FINANCE COMMITTEE
February 12, 2020
9:00 a.m.

[9:00:44 AM](#)

CALL TO ORDER

Co-Chair Stedman called the Senate Finance Committee meeting to order at 9:00 a.m.

MEMBERS PRESENT

Senator Natasha von Imhof, Co-Chair
Senator Bert Stedman, Co-Chair
Senator Click Bishop
Senator Lyman Hoffman
Senator Donny Olson
Senator Bill Wielechowski
Senator David Wilson

MEMBERS ABSENT

None

ALSO PRESENT

Dan Stickel, Chief Economist, Economic Research Group, Tax Division, Department of Revenue; Conor Bell, Petroleum Economist, Department of Revenue; Senator Cathy Giessel.

SUMMARY

^ORDER OF OPERATIONS - OIL TAX REGIME

[9:03:07 AM](#)

DAN STICKEL, CHIEF ECONOMIST, ECONOMIC RESEARCH GROUP, TAX DIVISION, DEPARTMENT OF REVENUE, discussed, "Alaska Oil and Gas Production Tax Calculation ('Order of Operations')" (copy on file).

Co-Chair Stedman stressed that the meeting was only 90 minutes.

Mr. Stickel highlighted slide 2, "Acronyms":

- ANS - Alaska North Slope
- ANWR - Arctic National Wildlife Refuge
- Avg - Average
- Bbl - Barrel
- CBRF - Constitutional Budget Reserve Fund
- CIT - Corporate Income Tax
- DOR - Department of Revenue
- FY - Fiscal Year
- GVPP - Gross Value at Point of Production
- GVR - Gross Value Reduction
- NPR-A - National Petroleum Reserve Alaska
- OCS - Outer Continental Shelf
- PTV - Production Tax Value
- SB21 - Senate Bill 21, passed in 2013
- TAPS - Trans Alaska Pipeline System
- Ths - Thousands

Mr. Stickel addressed slide 3, "Overview":

- Oil and Gas Revenue Sources - how production tax fits in
 - FY 2018 - FY 2022 oil and gas revenues
- Production Tax Calculation "Order of Operations"
 - Detailed walk-through of each step of tax calculation
 - Defining commonly used terms
 - Focus on North Slope oil
 - FY 2018 - FY 2022 comparison

Mr. Stickel looked at slide 4, "Disclaimer":

- Alaska's severance tax is one of the most complex in the world and portions are subject to interpretation and dispute.
- These numbers are rough approximations based on public data, as presented in the Fall 2019 Revenue Sources Book and other revenue forecasts.
- The numbers on some slides may not appear to add up due to rounding.
- We are economists, not auditors. This presentation is not an official statement of the Department as to any particular tax liability, interpretation, or treatment. This is not tax advice or guidance. This presentation is solely for illustrative general purposes.

Mr. Stickel discussed slide 5, "Oil and Gas Revenue Sources":

- Royalty - based on gross value of production
 - Plus bonuses, rents, and interest
 - Paid to Owner of the land: State, Federal, or Private
 - Usually 12.5 percent or 16.67 percent in Alaska, but rates vary
- Corporate Income Tax - based on net income
 - Paid to State (9.4 percent top rate)
 - Paid to Federal (21 percent top rate, used to be 35 percent)
 - Only C-corporations* pay this tax
- Property Tax - based on value of oil and gas property
 - Paid to State (2 percent of assessed value or "20 mills")
 - Paid to Municipalities - credit offsets state tax paid
- Production Tax - based on "production tax value"
 - Paid to State - calculation to follow

Mr. Stickel pointed to slide 6, "Oil and Gas Revenue Sources: Five-Year Comparison of State Revenue."

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Co-Chair von Imhof noted that royalties were paid when wells were producing.

Mr. Stickel agreed. He stated that the royalty number included a small amount in bonuses and rent.

Co-Chair von Imhof surmised that wells must be producing in order to provide royalty income to the state, and non-producing wells did not provide income to the state.

Mr. Stickel agreed. He stated that the producer would pay the bonus at the acquisition of the lease.

Mr. Stickel looked at slide 7, "Fiscal System: Overall":

Order of Operations
Royalties (State, Federal, or Private)
Property Tax
Production Tax

State Corporate Income Tax
Federal Corporate Income Tax

Mr. Stickel addressed slide 8, "Production Tax 'Order of Operations': FY 2021."

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Mr. Stickel discussed slide 9, "Production Tax 'Order of Operations': FY 2021":

1. Royalty and Taxable Barrels

Co-Chair Stedman noted that shifting the downstream was in order to move the oil to the next sale point.

Mr. Stickel agreed.

Mr. Stickel looked at slide 10, "Production Tax 'Order of Operations': FY 2021":

2. Gross Value At Point of Production (GVPP)

Senator Hoffman queried the direction of the \$9.78 per barrel has been going in the last decade.

Mr. Stickel replied that there was a general upward direction.

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Senator Olson wondered whether some of the ships leaving Valdez were below capacity.

Mr. Stickel replied that the shippers were optimizing the marine shipping.

Senator Olson surmised that the answer was possibly yes.

Mr. Stickel agreed to follow up on the inquiry.

Co-Chair Stedman felt that there were less shipments. He noted that the Trans-Alaska Pipeline System (TAPS) ran at full capacity, but was slower.

Mr. Stickel agreed.

Mr. Stickel addressed slide 11, "Production Tax 'Order of Operations': FY 2021":

3. Lease Expenditures

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Mr. Stickel thought the slide gave a measure of the tax impact of the lease expenditures. He pointed out a forecast \$4.6 billion in deductible lease expenditures.

Senator Bishop was interested in seeing what was allowable for deductible lease expenditures.

Co-Chair Stedman stated that Mr. Stickel was correct in referencing IRS guidelines.

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Co-Chair von Imhof commented on the \$1.3 billion in non-deductible lease expenditures carried forward. She asked about the \$4.6 billion.

Mr. Stickel clarified overall lease expenditures forecast was a significant increase from prior years.

Co-Chair Stedman asked Mr. Stickel to explain why the \$1.3 billion could not be deducted.

Mr. Stickel explained that production tax value was essentially the net income of the company.

Co-Chair von Imhof remarked that there would be a large cost initially, but there could be an amortization schedule. She felt that it was a normal course of business to make improvements on assets.

Mr. Stickel agreed.

Co-Chair Stedman felt that there must be allowance for deduction of expenditures, but the question was the timing.

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Senator Wielechowski queried the types of deductions in other oil producing states.

Mr. Stickel was not prepared to speak to the other tax regimes.

Senator Wielechowski recalled the number being zero, because the other states had a gross royalty and tax number.

Mr. Stickel replied that it was addressed in the prior year, and believed there was some nuance to the issue. He agreed to provide that information.

Co-Chair Stedman stated that the consultants could address that issue.

Senator Wielechowski remarked that the number was down in 2020.

Mr. Stickel felt that the number was probably correct. He stressed that the goal of the presentation was about how the system worked.

Senator Wielechowski asked about the capital investments.

Mr. Stickel replied that capital expenditures dropped off with the oil price crash, and bottomed out at \$1.7 billion in FY 18.

Mr. Stickel recapped slide 11.

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Mr. Stickel looked at slide 12, "Production Tax 'Order of Operations': FY 2021":

4. Production Tax Value (PTV)

Mr. Stickel addressed slide 13, "Production Tax 'Order of Operations': FY 2021":

5. Gross Minimum Tax

Co-Chair Stedman noted that the starting points were different on the two taxes.

Mr. Stickel agreed, and explained the two taxes.

Mr. Stickel looked at slide 14, "Gross Value Reduction:

- Gross Value Reduction (GVR) is an incentive program for new fields.
- Available for the first seven years of production and ends early if ANS prices average over \$70 per barrel for any three years.
- Allows companies to exclude 20 percent or 30 percent of the gross value from the net production tax calculation.
- In lieu of sliding scale Non-GVR Per-Taxable Barrel Credit, qualifying production receives a flat \$5 GVR Per-Taxable-Barrel Credit.
- The \$5 GVR Per-Taxable-Barrel Credit can be applied to reduce tax liability below the minimum tax floor, assuming that the producer does not apply any sliding scale Non-GVR Per-Taxable Barrel Credits.

Senator Bishop wondered whether the GVR was adjusted in 2016 or 2017.

Co-Chair Stedman stated that the information could be provided at a later time.

Mr. Stickel highlighted slide 15, "Production Tax 'Order of Operations': FY 2021":

6. Net Tax and Gross Value Reduction (GVR)

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Mr. Stickel discussed slide 16, "Production Tax 'Order of Operations': FY 2021":

7. Tax Credits against Liability

Senator Wielechowski requested the aggregated per barrel credits provided at each of the legacy fields and the aggregated lease expenditures at each of the legacy fields.

Mr. Stickel agreed to provide that information, to the best of their ability.

Co-Chair Stedman felt that the information might be difficult to obtain.

Mr. Stickel would provide the level of detail available.

Mr. Stickel addressed slide 17, "Production Tax 'Order of Operations': FY 2021":

8. Adjustments and Total Tax Paid

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Co-Chair Stedman noted that there was a request to always provide the net, so there could be an appropriate discussion of the different taxes.

Mr. Stickel displayed slide 18, "Order of Operations: Five-Year Comparison."

Co-Chair Stedman wanted the data set to begin with 2010.

Mr. Stickel agreed to provide that information.

Co-Chair von Imhof wondered why the minimum tax was different.

Mr. Stickel replied that the primary driving factor was the change in price as well as the change in company investment.

Co-Chair Stedman felt that they were close to the tipping point.

Mr. Stickel agreed.

Senator Wielechowski noted that there was a gross of around 15 or 16 percent. He wondered how it compared to the history, because he felt that it was the lowest in history.

Co-Chair Stedman felt that the history should be to at least 2010.

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CONOR BELL, PETROLEUM ECONOMIST, DEPARTMENT OF REVENUE, pointed to slide 21, "Distribution of Cash Flows: North Slope Oil":

- Share of net cash flows after transportation costs and lease expenditures that go to government vs company
- Modeled two ways
 - o Typical non-GVR production
 - o All North Slope production and spending

Co-Chair Stedman stressed that there was an attempt to reduce the foundation, because the public had so much different information in the public.

Mr. Bell highlighted slide 22, "Distribution of Cash Flows: North Slope Oil Typical Non-GVR Production":

- Charts shown are produced using DOR "Snapshot" model
- Assumes a single company with all deductible costs
- Simplifying assumptions such as non-GVR oil only; North Slope only; etc.
- Transportation costs, production, and lease expenditures, and other assumptions from Fall 2019 forecast for FY 2021
- Prices are expressed in nominal terms

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Mr. Bell discussed slide 23, "Distribution of Cash Flows from One Barrel of Typical Non-GVR Production, FY 2021":

Co-Chair Stedman wondered whether the federal law was considered.

Mr. Bell replied in the affirmative.

Co-Chair Stedman wondered whether there were modifications to the potential subchapter new members to the oil basin and the impact on the tax.

Mr. Bell replied that it was not taken into account.

Senator Wielechowski requested an aggregated account of the legacy fields.

Co-Chair Stedman felt that the consultants could address that issue.

Mr. Stickel remarked that slide 23 looked at a typical barrel of production from non-GVR eligible fields.

Co-Chair Stedman surmised that it included a 21 percent tax rate.

Mr. Stickel agreed.

Co-Chair Stedman noted that it was also the 2021 expenditures.

Mr. Stickel indicated in the affirmative.

Mr. Bell highlighted slide 24, "Government Take at Range of Prices from Typical Non-GVR Production."

Co-Chair Stedman remarked that the fixed components impacted the oil price. He wanted further explanation on that issue from the consultants.

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Mr. Bell displayed slide 25, "Distribution of Cash Flows: North Slope Oil Using All Slope-wide Production and Costs":

- Charts shown are produced using DOR "Snapshot" model
- Assumes two companies with all costs (one GVR, one non-GVR)
- Simplifying assumptions such as oil only; North Slope only; etc.
- Transportation costs, production, and lease expenditures, and other assumptions from Fall 2019 forecast for FY 2021
- Prices are expressed in nominal terms

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Co-Chair Stedman wondered whether there was an attempt to use even non-producing field expenditures in the chart.

Mr. Bell replied in the affirmative.

Co-Chair Stedman remarked that it was interesting information.

Mr. Bell looked at slide 26, "Distribution of Cash Flows from One Barrel, Using All Slope-wide Production and Costs, FY 2021":

Producer: 34.3 percent
Federal: 9.1 percent
State/Muni 56.6 percent
Lease expenditures ex-property tax
Transportation

Mr. Bell highlighted slide 27, "Government Take at Range of Prices from All Slope-wide Production and Costs."

Co-Chair Stedman wondered whether the difference between the two columns was the "subject to no state income tax."

Mr. Bell replied in the affirmative.

Co-Chair Stedman wondered whether there was an inclusion of all expenditures or only deductible expenditures.

Mr. Bell replied that all expenditures were included.

Co-Chair Stedman surmised that there was an addition of the \$1 billion.

Mr. Bell replied that the \$1.3 billion of the lease expenditures were included in the slide.

Mr. Bell discussed slide 28, "Impact of Corporate Structure on Cash Flows, an Illustration Using Slope-wide Production and Costs, FY 21":

Assuming All Production Subject to State Corporate
Income Tax
 Producer 34.3 percent
 Federal 9.1 percent
 State/Muni 56.6 percent

Assuming No production Subject to State Corporate
Income Tax
 Producer 36.7 percent
 Federal 9.8 percent
 State/Muni 53.5 percent

Co-Chair Stedman requested the slide, but in dollar form.

Mr. Bell agreed to provide that information.

Co-Chair Stedman asked for a column to replicate the per barrel cost.

Mr. Bell replied in the affirmative.

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Mr. Bell addressed slide 29, "FY 2021 Tax Calculation, Assuming Varying Non-GVR Per-Taxable-Barrel Credit Rates."

Co-Chair Stedman requested a breakdown of \$5 per barrel.

Mr. Bell agreed to provide that information.

Co-Chair Stedman asked that the information be taken down by the per barrel deduction.

Co-Chair von Imhof recalled a graph that showed the price forecast and crossover point. She wanted a per barrel credit on a number line, and where it affected the numbers.

Mr. Bell replied that the next slide might speak to the question.

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Mr. Bell highlighted slide 30, "FY 2021 Production Tax Sensitivity, Assuming Varying Non-GVR Per-Taxable-Barrel Credit Rates."

Co-Chair von Imhof noted that the slide was helpful, because of the sensitivity analysis.

Co-Chair Stedman stated that he would provide a table addressing Co-Chair von Imhof's concerns.

Mr. Stickel stated that the forecast did not quite reach \$100 per barrel. He noted that there was a response to the committee that would examine the expected crossover point of gross and net tax.

Co-Chair Stedman understood that there were several moving components.

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Senator Wielechowski requested a reasoning behind the calculations.

Co-Chair Stedman asked for percentages to be included in that analysis.

[10:15:52 AM](#)

Mr. Stickel agreed to provide that information.

Mr. Bell looked at slide 31, "'Count the Cash': Petroleum Net Fiscal Impact, valuing carry-forward expenditures at net tax rate."

Senator Wielechowski wondered whether the number was applied in the difference.

Mr. Bell replied that it applied the 35 percent tax value.

Co-Chair Stedman wanted to understand the net cash position and the potential impact on the net cash of credits coming against the treasury.

Mr. Bell discussed slide 32, "'Count the Cash': Petroleum Net Fiscal Impact assuming no value to carry-forward expenditures."

Co-Chair Stedman stressed that the slide may not come against in 2021, but would at the point of production.

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Mr. Bell pointed to slide 33, "State Petroleum Revenue by Land Type."

Senator Hoffman wondered whether there was a timeframe for the consultants addressing the committee.

Co-Chair Stedman replied in the negative, but felt that there would be some discussions probably in March.

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ADJOURNMENT

[10:22:48 AM](#)

The meeting was adjourned at 10:22 a.m.