

SB

85

<TARGET><BILL>SB 85</BILL><SUBJECT>SB
85</SUBJECT><COMM>SRES27</COMM></TARGET>



Official Business

ALASKA STATE LEGISLATURE

SENATOR THOMAS H. WAGONER,

Co-Chair: Senate Resources Committee

Member: C&RA Committee

Member: LB&A Committee

Member: Regulatory Review

Member: World Trade

Session: January - May

State Capitol, #427

Juneau, AK 99801

Phone: 907-465-2828 Fax: 907-465-4779

Interim: May - December

145 Main Street Loop; Suite 226

Kenai, AK 99611

Phone: 907-283-7996 Fax 907--283-8127

Senate Bill 85 Sponsor Statement TAX CREDIT FOR NEW OIL & GAS DEVELOPMENT

This bill authorizes credits for 100% of the costs of the qualified development expenditures that were incurred after a "pool" is discovered and before production of oil or gas in paying quantities.

The Alaska Oil and Gas Conservation Commission (AOGCC) determines the date the "pool" was discovered and the Department of Natural Resources (DNR) determines the date of commencement of production from that pool. Eligible costs for the credit are those that are qualified capital expenditures (AS 43.55.023) or lease expenditures (AS 43.55.165).

The credit is required to be taken within five years, is not transferable and may not be used to reduce a tax liability to below zero.

Alaska's declining oil production has extremely serious ramifications on the Trans Alaska Pipeline System (TAPS), the revenues of the State of Alaska, and on the domestic production for the United States of America.

Alaska's production is about one-third of the peak 2.1 million barrels per day in 1988 and projected to continue declining 5-6% per year. ¹ Without reversals in the current decline, the continuation of the entire system is at risk.

This new credit is expected to produce increased activity in oil production and thus, an increase in the through-put in the TAPS system.

The legislation is patterned after revisions recently made to Alberta's royalty taxing regime (May 2010). As a result of the revisions, Alberta expects industry reinvestments of \$700 million per year and creation of 8,000 jobs in 2011-2012.

¹ Alyeska pipeline May 2010
SS SB 85 S(RES) 2-23-11/mj



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Senate Bill 85

Sectional Analysis

TAX CREDIT FOR NEW OIL & GAS DEVELOPMENT

Section 1: Existing law prohibits multiple tax credits, this adds the new credits established in this bill, **43.55.026**.

Section 2: Adds new credits established in this bill, **43.55.026**, to existing law that restricts multiple tax credits..

Section 3: sets out new **43.55.026** for the new tax credit.

- (a) Directs that the new credit applies to qualified expenditures that were incurred prior to production of oil or gas in paying quantities for a lease or a property taxable under AS 43.55.011(e)¹ and that is not and has not been within a unit, or produced oil or gas, as of December 31, 2010.
- (b) Establishes that the credit amount is 100% of the qualified development expenditures incurred after completing the drilling of the first well that discovers a pool (capable of commercial production) and before production (in paying quantities) commences. Those dates are determined by the Department of Revenue (DOR), in consult with
 1. Alaska Oil and Gas Conservation Commission (AOGCC) for establishing the date on which the first well drilled discovered a pool (capable of commercial production); and
 2. Department of Natural Resources (DNR), for establishing the date that production (in paying quantities) commences.

¹ (AS 43.55.011(e) establishes the oil and gas production tax that replaced the ELF production tax in 2006.).

- (a) Establishes that the credit may be applied against the production tax during the five years immediately following the date of production commencement, or, if the credit is fully applied before the end of the five year period, until the credits for the expenditures are fully applied, whichever occurs first. Credits expire if not taken within that five year period and may not be applied against the production tax from a lease or property not eligible for the credit.

Essentially, there is a five year "holiday" from the production tax under this new credit or the time required to recoup 100% of the development costs, whichever occurs first.

- (b) Restricts the use of the new credit so there are not multiple credits.
- (c) Establishes that the credit or any portion of the credit is not transferable and may not reduce the tax liability below zero for AS 43.55.011(e) (the production tax) for any calendar year.

Essentially, the tax credit stays with the drilling site and the new credit may not allow the tax payer to obtain a refund from the state in any calendar year.

- (d) Allows the DOR to adopt regulations needed to administer the new credit.
- (e) Establishes procedures so that when a lease or property that utilizes this new credit becomes part of a unit under AS 38.05.180(p)², the credit is applied only to the production tax due for the lease or property that qualified for the credit.
- (f) Defines:
1. "production in paying quantities".
 2. "qualified development expenditure".

Section 4: Amends existing law to include new section for this tax credit in **43.55.026**.

Section 5: Establishes an immediate effective date for the legislation.

² AS 38.05.180(p) (oil and gas and gas only leasing statutes regarding unitization)



TRANS ALASKA PIPELINE SYSTEM

The 800-mile-long Trans Alaska Pipeline System (TAPS) is one of the world's largest pipeline systems. Starting in Prudhoe Bay on Alaska's North Slope, TAPS stretches through rugged and beautiful terrain to Valdez, the northernmost ice-free port in North America. Since pipeline startup in 1977, Alyeska - TAPS' operator - has transported more than 15 billion barrels of oil.

In 1968, oil was discovered at Prudhoe Bay in the North Slope, located in northern Alaska between the Brooks Range Mountains and the Beaufort Sea (part of the Arctic Ocean). A consortium of oil companies planning to produce the oil determined that a pipeline offered the best means to transport crude oil from the North Slope to a navigable port in southern Alaska where it could be shipped by tanker to refineries in the continental United States.

ABOUT ALYESKA PIPELINE SERVICE COMPANY

Alyeska Pipeline Service Company, named after the Aleut word Alyeska meaning mainland, was established in 1970 and charged with designing, constructing, operating, and maintaining TAPS. At the time, construction of the pipeline was the largest privately financed construction project ever attempted, and cost over \$8 billion when completed. Pipeline construction began in March 1975 and was finished in June 1977. Crude oil began flowing in the pipeline on June 20, 1977 and the first tanker filled with North Slope crude oil left Valdez on August 1, 1977.

The consortium of companies that own TAPS today includes: BP Pipelines Alaska (46.93%), ConocoPhillips Transportation Alaska, (28.29%), ExxonMobil Pipeline Company (20.34%), Unocal Pipeline Company (1.36%), and Koch Alaska Pipeline Company, L.L.C., (3.08%).

PIPELINE FACTS

The 48-inch diameter steel pipeline runs 800 miles and crosses three mountain ranges and 800 rivers or streams. Moving "hot" oil across the permafrost rich soil of Alaska presented a special challenge to pipeline designers. Typical pipeline construction at the time involved burying most pipelines, but because of the permafrost through most of Alaska, large segments of the trans-Alaska pipeline were elevated above ground to keep the permafrost from melting. About half of the 800 mile pipeline is buried in a conventional manner.

More than 16 billion barrels have moved through the Trans Alaska Pipeline System since start up in 1977. The volume of oil flowing through the pipeline has decreased from a peak of 2.1 million barrels per day in 1988 to about 671,000 bpd in 2010. Alaska today supplies nearly 17% of the United States' domestic crude oil production.

Over 19,000 oil tankers have been loaded with Alaska crude oil in Valdez since the pipeline began operation. The Marine Terminal cost \$1.4 billion to build, covers 1,000 acres, and includes 18 oil storage tanks with a total capacity of over 9 million barrels.

SPILL PREVENTION AND RESPONSE

Alyeska Pipeline spends over \$60 million annually to oil spill prevention and response in Prince William Sound, and has dedicated over 300 personnel to this effort, mostly through its Ship Escort/Response Vessel System (SERVS). Created in July 1989, SERVS is considered one of the best oil spill prevention and response forces in the world. The SERVS mission is three fold: prevention, preparation, and response. Each laden tanker is escorted through Prince William Sound to the Gulf of Alaska by response vessels capable of assisting a distressed tanker. In addition, oil spill response equipment has been pre-stationed throughout the Sound for rapid response.

Between 60-70 drills are held annually so personnel and equipment along all 800 miles of TAPS are ready 24/7 to respond to any contingency.



THROUGHPUT, FLOW RATE AND CRUDE OIL

- Approximately 650,000 barrels of oil per day currently move through the pipeline at about 3 mph (one barrel = 42 gallons).
- Transport time is about 14 days from Prudhoe Bay to Valdez.
- Maximum daily throughput was 2,145,297 barrels on January 14, 1988.
- Five separate oil streams enter TAPS at Pump Station 1. The commingled oil is approximately 112 degrees F and cools to approximately 54 degrees F during its trip to Valdez.
- Oil volume is measured as it enters and leaves the pipeline and at metering stations along the pipeline route. Metering is essential for accounting and leak detection.
- 178 mainline valves control oil flow and protect the environment by limiting the potential size of spills, especially near stream crossings and other environmentally sensitive areas.
- 83 check valves automatically prevent reverse flow of oil.
- 71 gate valves can block oil flow in either direction.



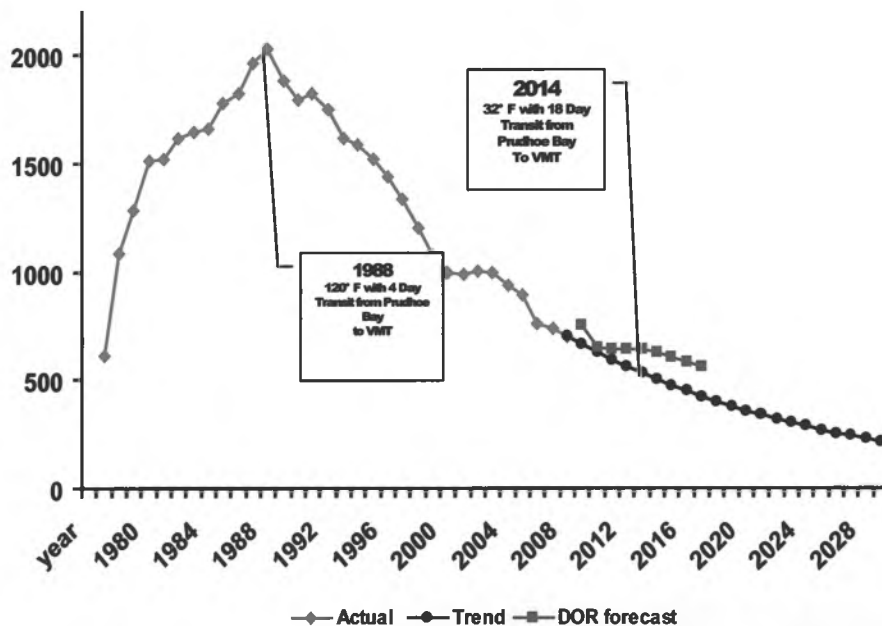
ALASKA OIL PRODUCTION IN DECLINE

- Production is now only about one third of what it was at its peak in 1989.
- Production is projected to continue declining 5-6% per year. Even new fields being developed won't be enough to offset the declining output of the Prudhoe Bay field.
- At this rate, TAPS will be transporting less than 500,000 barrels of oil per day in five to six years.

The technical challenges of low throughput (wax and water buildup, frost heaves, ice crystals and plugs, etc.) can and will be solved.

Economics are the biggest challenge. What will happen when current oil fields are depleted (as depicted on the chart above) or when it is no longer profitable for oil companies to transport oil in TAPS?

TAPS currently supplies approximately 15% of the U.S. oil production. What will happen if this source of domestic oil stops?



Mary Jackson

From: Longan, Sara W (DNR) [sara.longan@alaska.gov]
Sent: Thursday, March 03, 2011 3:29 PM
To: Jeff Stepp; Mary Jackson
Cc: Banks, Kevin R (DNR); Fulton, Trevor M (DNR)
Subject: SB 85 SRES follow-up
Attachments: Discov to Prod.ppt

Here are two answers from questions that were raised during SRES hearing on SB 85. Please forward to the committee and let us know if there are any further questions.

1) What's the development cost of a typical new project?

Recent examples of new project costs include: Nikaitchuq is expected to cost \$1.45 billion to fully develop (published in 2009)

Costs to develop Oooguruk are \$550 million (from Pioneer's 2007 capital budget report)

2) What's the duration between exploration and first production?

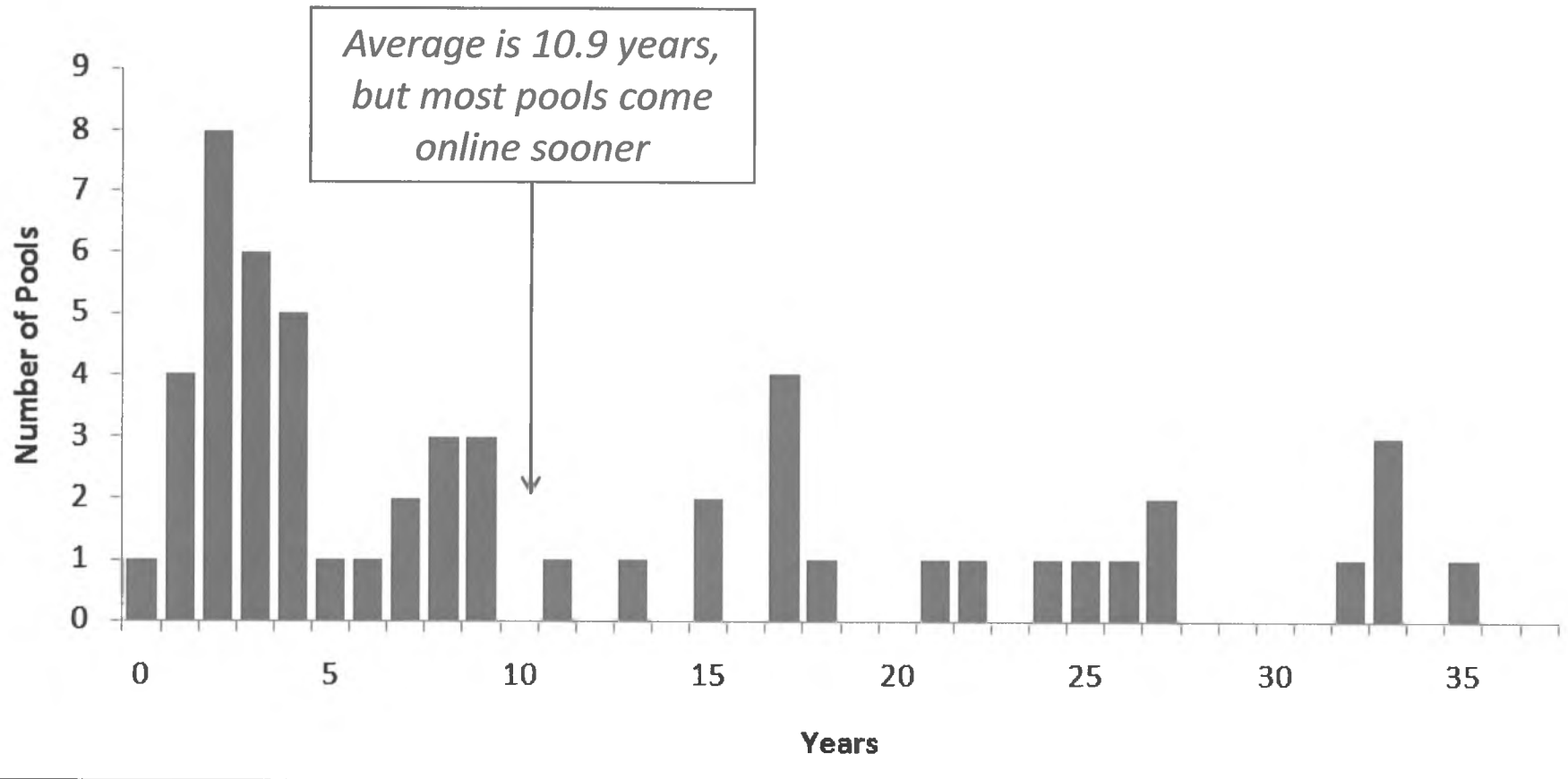
Based on 54 Alaskan oil pools statewide, the average time between exploration and first production is 10.9 years, but most fields come on considerably sooner, and some others can take decades for a variety of holdups to be resolved. Many of the longest waits are for pools with heavy oil, or other "puddles" near the major fields that had to wait for facilities capacity, etc. before they could be produced.

Best,

Sara W. Longan

State of Alaska
Legislative and Policy Advisor
Department of Natural Resources
Division of Oil and Gas
550 W. 7th Ave., Suite 1100
Anchorage, Ak 99501-3560
Ph: 907-269-8802
sara.longan@alaska.gov

Time Between Discovery and Production Alaskan Oil Pools



CS for Senate Bill 85

Version:

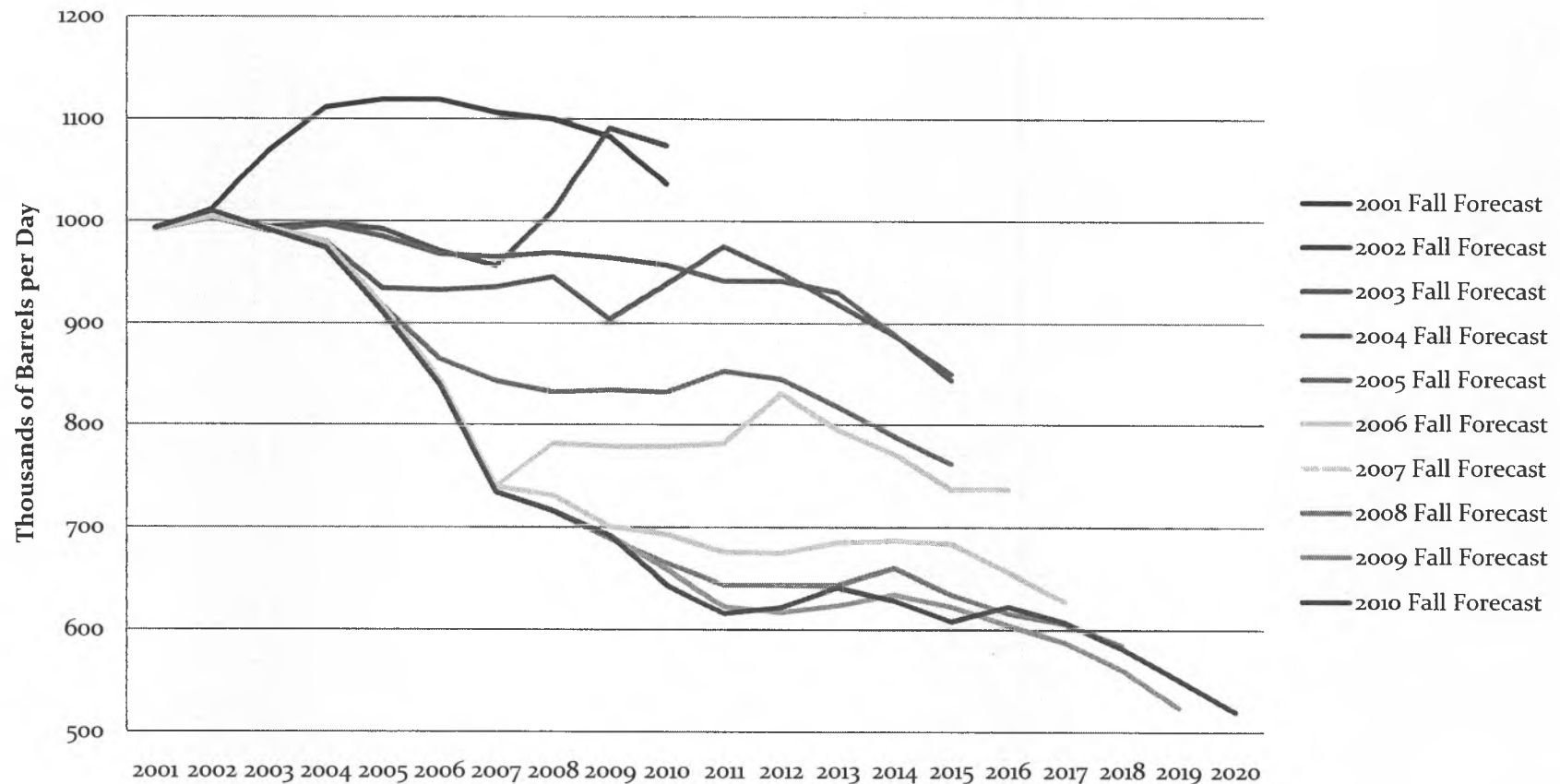
An act providing a tax credit applicable to the oil and gas production tax based on the capital cost of developing new oil and gas production; establishing the Oil and Gas Competitiveness Review Board; and providing for an effective date.

Presentation prepared by: Michael Pawlowski, aide to Senator McGuire and Mary Jackson, aide to Senator Wagoner

3/24/2010

The Challenge: *Oil Production is Declining*

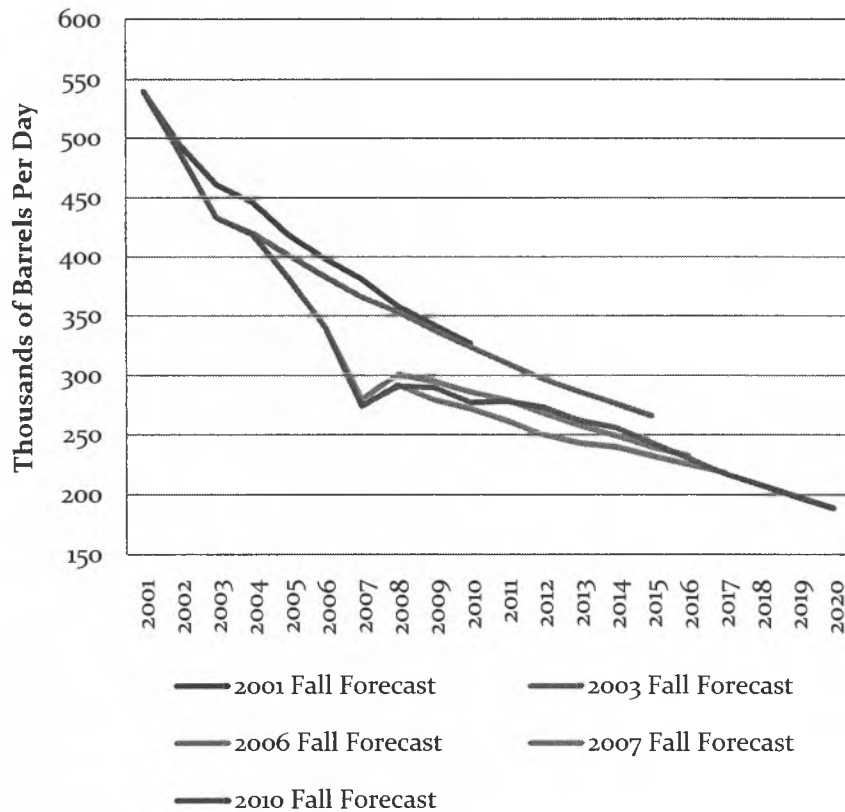
AK Department of Revenue Forecasts



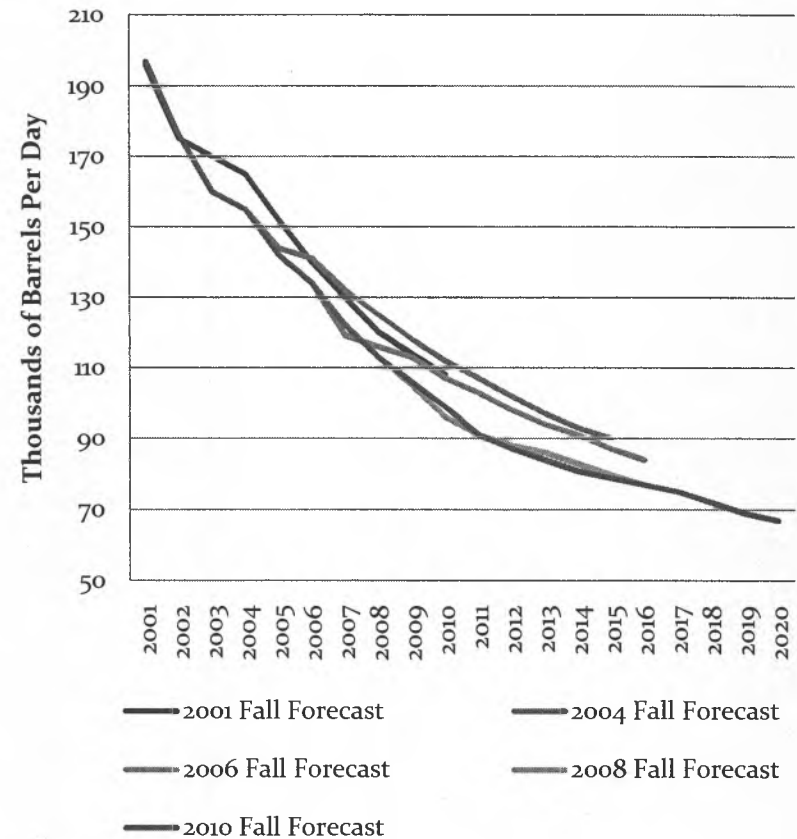
Source: Alaska Department of Revenue Fall Revenue Forecasts ; <http://www.tax.alaska.gov/programs/sourcebook/index.aspx>

Prudhoe Bay (PBU) and Kuparuk (KRU) Projections

AK DOR Production Forecasts: Prudhoe Bay
2001-2010



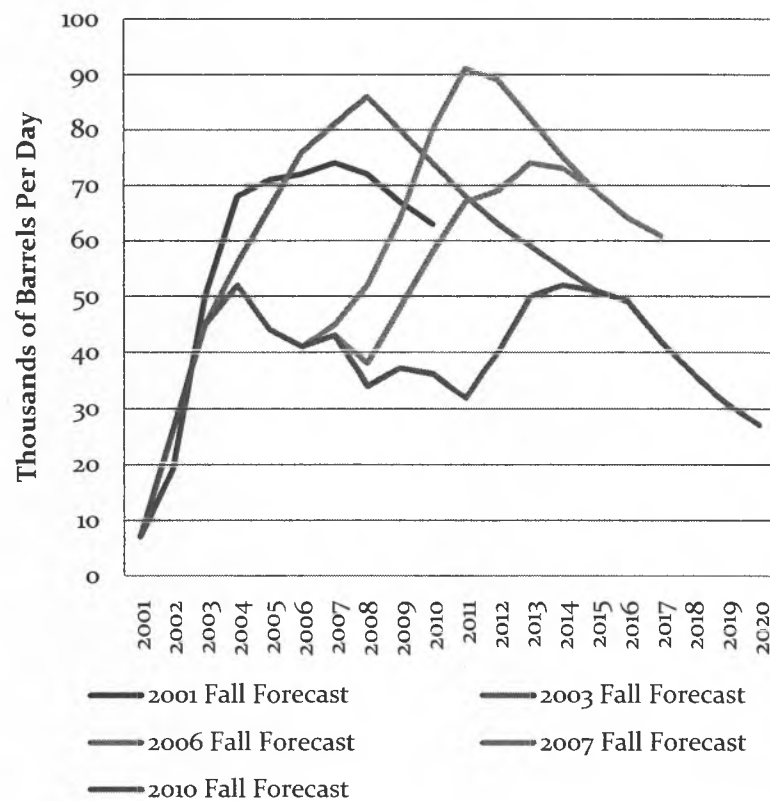
AK DOR Production Forecasts: Kuparuk
2001-2010



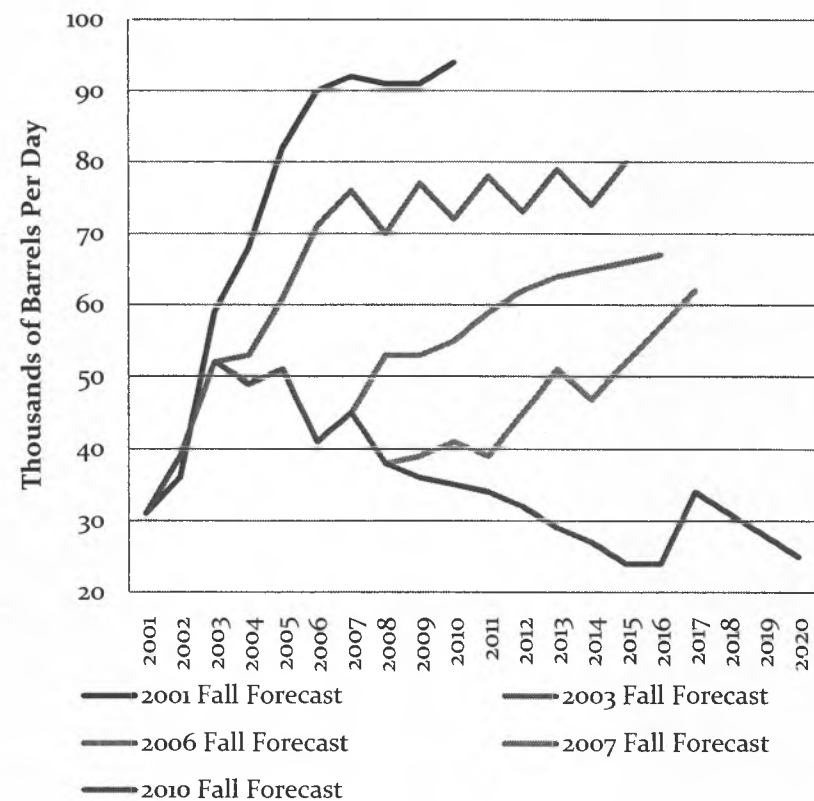
Source: Alaska Department of Revenue Fall Revenue Forecasts ; <http://www.tax.alaska.gov/programs/sourcebook/index.aspx>

PBU Satellite and KRU Satellite Projections

**AK DOR Production Forecasts:
Prudhoe Bay Satellites 2001-2010**



**AK DOR Production Forecasts:
Kuparuk Satellites 2001-2010**

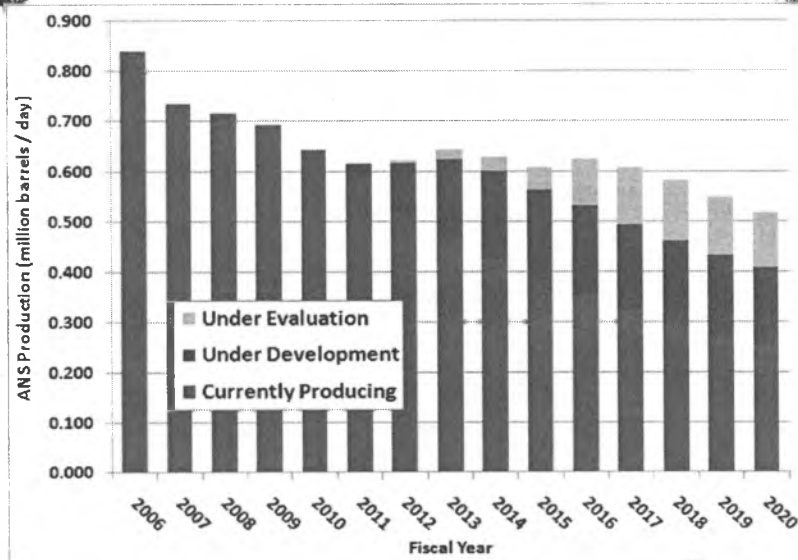


Source: Alaska Department of Revenue Fall Revenue Forecasts ; <http://www.tax.alaska.gov/programs/sourcebook/index.aspx>

The “Under Development” & “Under Evaluation” Components in the Fall 2010 Forecast



Investment needed in new & old fields alike



Source: Fall 2010 Revenue Sources Book

Figure 4-11. New Oil as a Percentage of Total Oil (million barrels per day)

Fiscal Year	Total New Oil	ANS Total	Percent New Oil
2011	0.032	0.616	5.2%
2012	0.102	0.622	16.4%
2013	0.178	0.642	27.7%
2014	0.203	0.629	32.3%
2015	0.222	0.608	36.5%
2016	0.270	0.623	43.3%
2017	0.284	0.607	46.8%
2018	0.286	0.582	49.1%
2019	0.277	0.551	50.3%
2020	0.265	0.520	51.0%

Source: Alaska Department of Revenue Fall 2010 Revenue Sources Book p. 42

Source: Alaska Department of Revenue Presentation to House Resources; Feb 7, 2011



The target of SB 85 is NEW oil

- Senate Bill 85 proposes a new credit:
- **AS 43.55.026: Development Cost Credit** (p. 2, lines 12-16)
 - 100% of qualified development expenditures (CAPEX)
 - Minus credits issued under 43.55.023 (a) [20% of qualified capital expenditures]
 - and 43.55.023 (b) [25% of net operating loss]
- **For undeveloped properties and pools** (p. 2, lines 7-11)
 - A lease or property that as of December 31, 2010 has not been directly involved in *sustained production*; or
 - A pool that as of December 31, 2010 has not been involved directly in sustained production.



Example: \$10 million capital expenditure

Producer with a tax liability

CAPEX: \$10,000,000
.023(a): (\$2,000,000)

.026 Credit: \$8,000,000

Producer with no tax liability

CAPEX: \$10,000,000
.023(a): (\$2,000,000)
.023(b): (\$2,500,000)¹

.026 Credit: \$5,500,000

¹Assuming that the producer had a carry forward loss for the purposes of .023 (b) of \$10,000,000.



Limitations on the .026 credit

- The .026 credit may not be transferred and may not be used to reduce a person's tax liability under AS 43.55.011(e) below zero. (p. 2, line 30 – p. 3, line 1)
- The .026 credit may not be taken against the tax levied by AS 43.55.011(e) until there is production.
 - For the purposes of applying the .026 credit the tax shall be allocated in proportion to the volume of production from that lease or property. (p. 3, lines 6-13)
 - Example: If production from the new pool within an existing unit is only 10% of production from the unit the credit may only be applied against a maximum of 10% of the tax due from the unit.

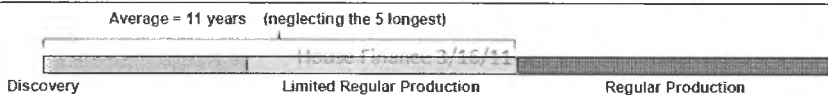
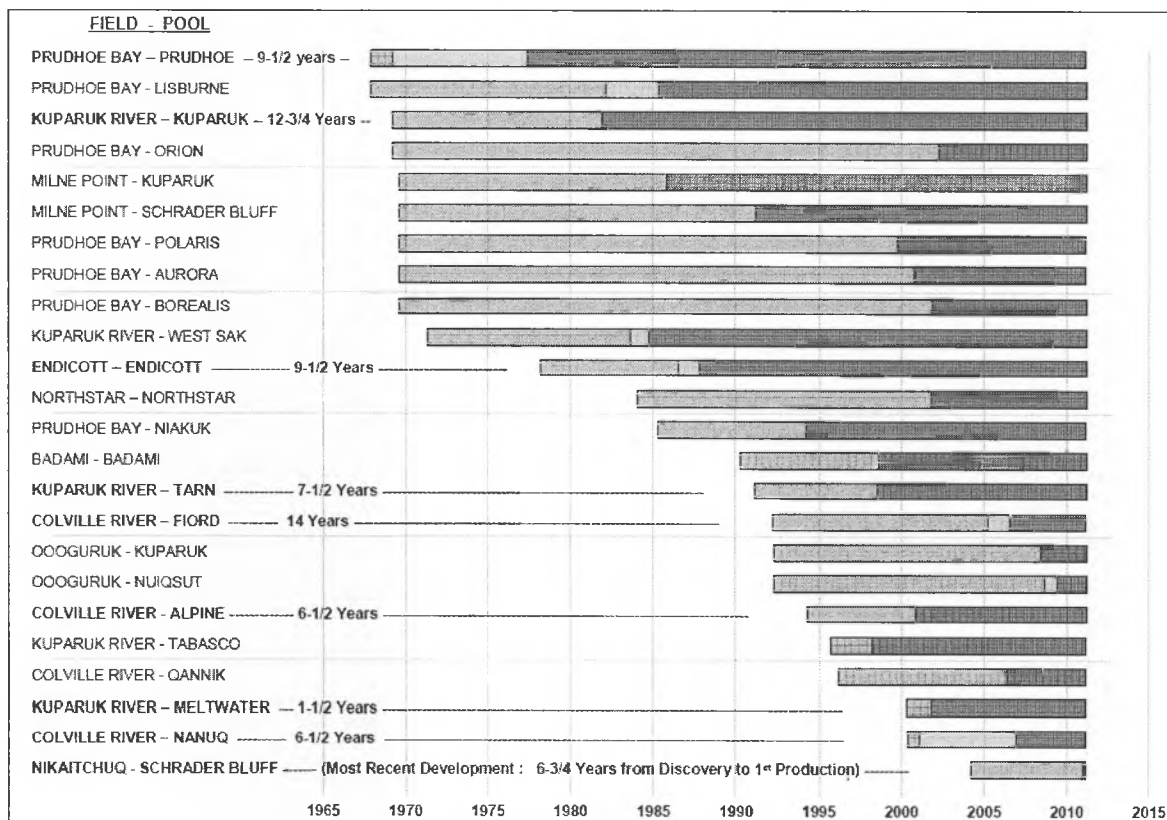
Creating a stampede.

- In order to qualify for the proposed credit, qualified development expenditures must be made before 2018

(p. 2, line 1)



Development Timeline for North Slope Oil Fields



The proposed .026 credit is for expenditures made after discovery and before sustained production (p. 2, lines 12-21).

In the AOGCC chart to the left, that is for primarily the blue, and possibly the tan sections of the timeline.

AOGCC

March 14, 2011

Source: AOGCC Presentation to House Finance (3/16/2011)



Monitoring the future; making Alaska Competitive for the long term.

- Section 4 of CS for Senate Bill 85 establishes the Alaska Oil and Gas Competitiveness Review Board.
- The Board is comprised of: (Page 4, lines 6-30)
 - Two members of the Legislature (one from the Senate appointed by the President, one from the House appointed by the Speaker).
 - The members of the Legislature serve as the co-chairs of the Board.
 - The Commissioners of DNR and DOR (or their designees).
 - Five public members appointed by the Governor
 - A geologist
 - A petroleum engineer
 - An economist
 - A member of an environmental or conservation group
 - A member of the public



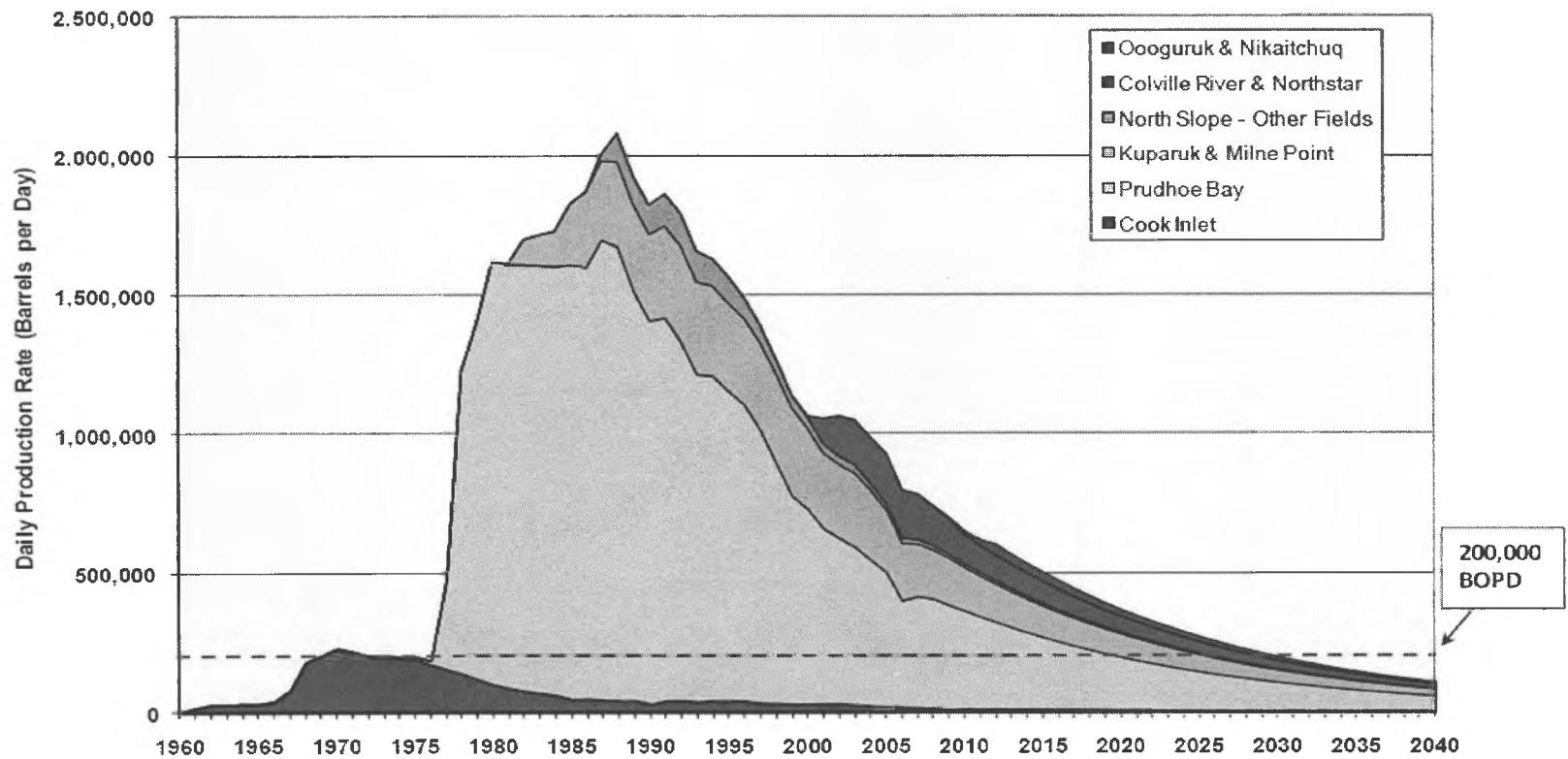
Duties and Reports

- The duties of the Board are to:
 - Review Historical, current and potential levels of investment;
 - Identify factors that affect investment;
 - Review the competitive position of the state
 - Make written findings before December 1 of each year (p. 5, lines 14-25) regarding:
 - Changes to the State's regulatory environment
 - Changes to the State's fiscal regime
 - Alternative means for increasing the state's ability to attract and maintain investment in and development of the state's oil and gas resources.

Looking Forward

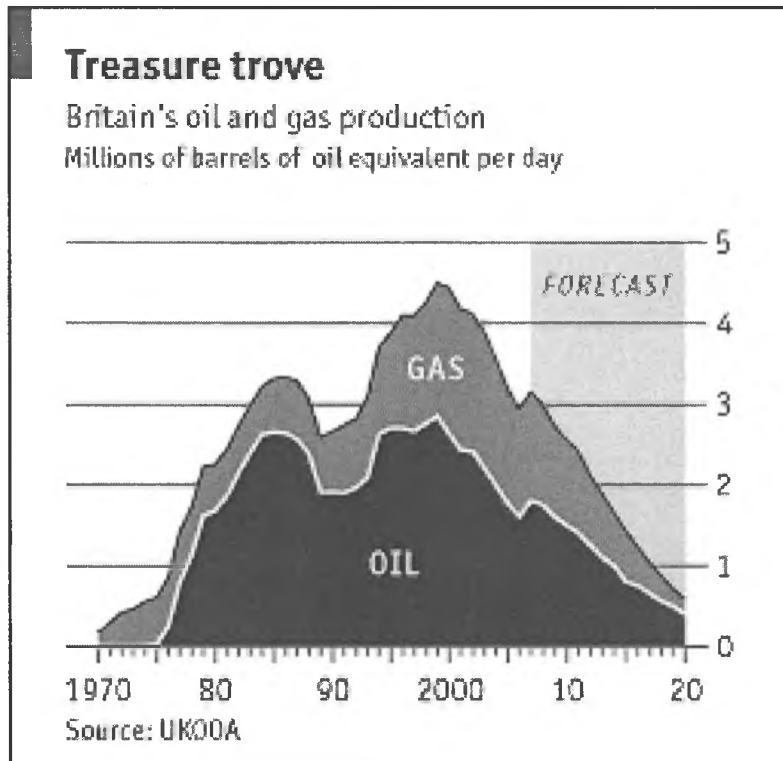
Slide Prepared by Alaska Oil and Gas Conservation Commission (AOGCC)

Alaska's Average Daily Oil & NGL Production Rate (6% Annual Decline Rate)

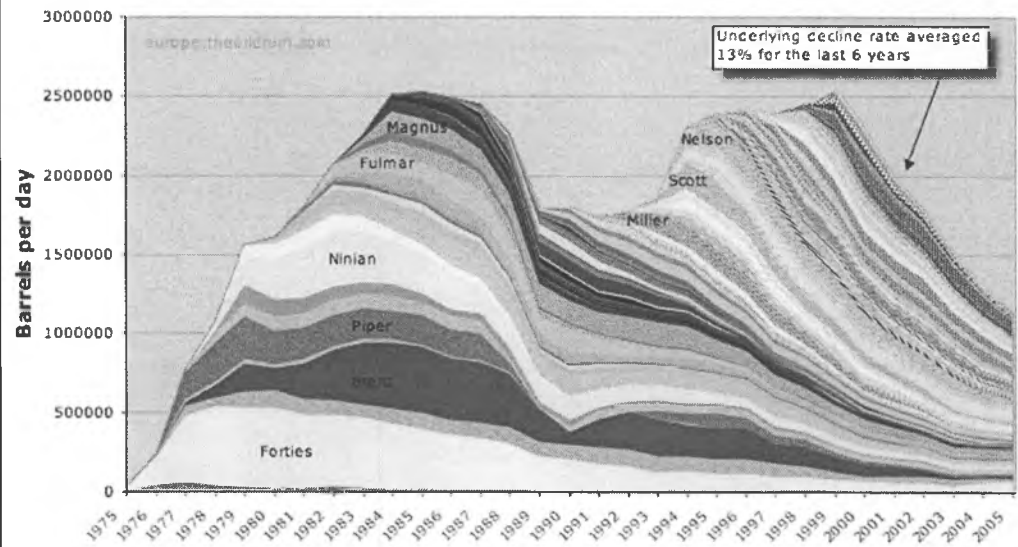


Source: AOGCC Presentation to House Finance (3/16/2011)

The U.K. North Sea



http://offalnews.blogspot.com/2007_07_01_archive.html



Source: <http://europe.theoil drum.com/node/5836>

Alaska?

Alaska North Slope Oil Production Forecasts
(Producing, Known Undeveloped, and Undiscovered)

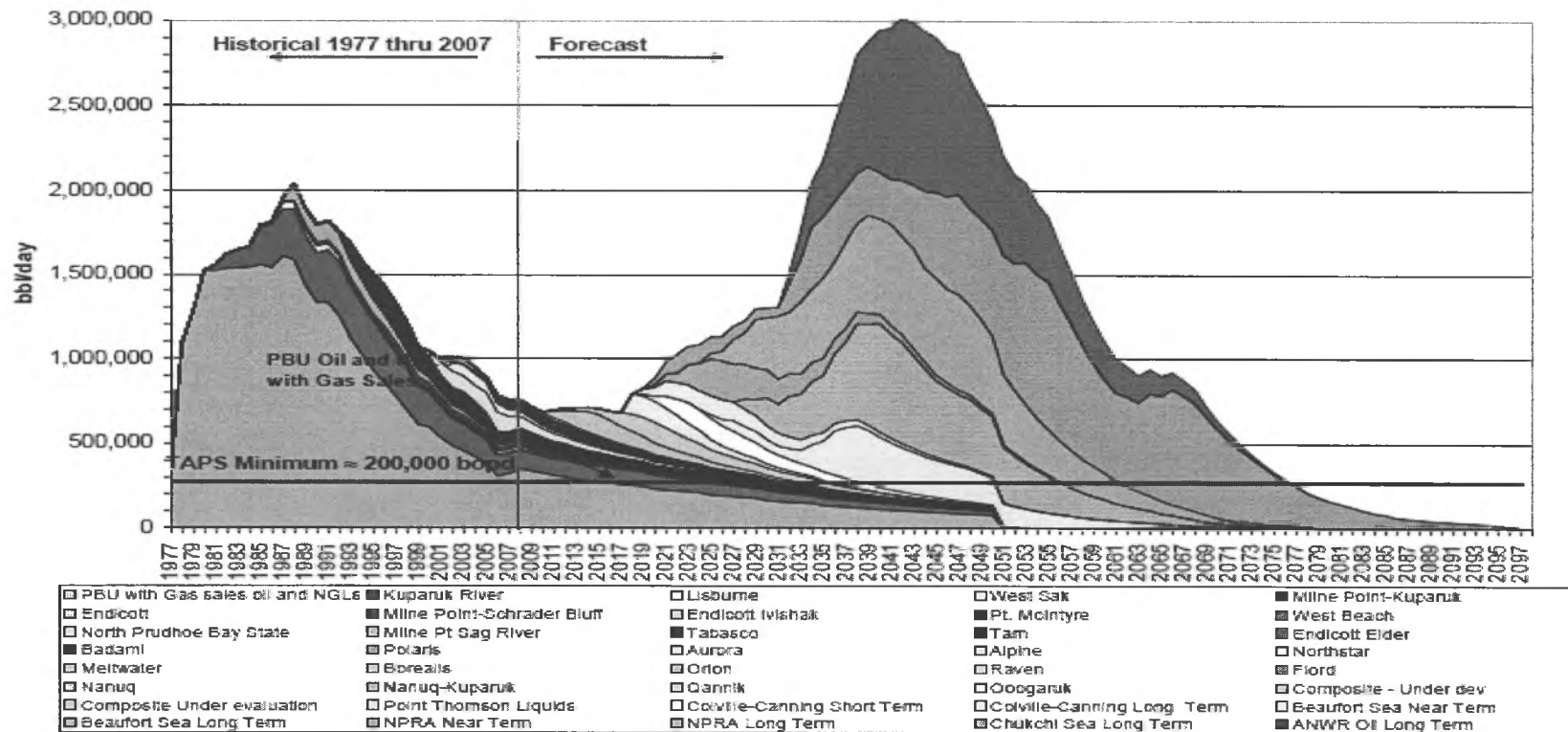


Figure 3-55. Alaska North Slope historical and forecast oil production from producing fields, known undeveloped fields, and undiscovered fields.

Source: U.S. DOE/NETL: Alaska North Slope Oil and Gas, A Promising Future or an Area in Decline

http://www.netl.doe.gov/technologies/oil-gas/publications/AEO/ANS_Potential.pdf

Contacts:

Mary Jackson, aide to Senator Tom
Wagoner: 907-465-2828

Mary_Jackson@legis.state.ak.us

Michael Pawlowski, aide to Senator
Lesil McGuire: 907-465-2995

Michael_Pawlowski@legis.state.ak.us



27-LS0484\E

Bullock

3/24/11

CS FOR SENATE BILL NO. 85()
IN THE LEGISLATURE OF THE STATE OF ALASKA
TWENTY-SEVENTH LEGISLATURE - FIRST SESSION

BY**Offered:****Referred:****Sponsor(s): SENATORS WAGONER, Stevens, McGuire, Huggins, Dyson, Giessel, Menard**

A BILL

FOR AN ACT ENTITLED

1 **"An Act providing for a tax credit applicable to the oil and gas production tax based on**
2 **the capital cost of developing new oil and gas production; establishing the Oil and Gas**
3 **Competitiveness Review Board; and providing for an effective date."**

4 **BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:**

5 *** Section 1.** AS 43.20.043(g) is amended to read:

6 (g) A taxpayer that obtains a credit for a qualified capital investment or cost
7 incurred for qualified services under this section may not also claim a tax credit or
8 royalty modification for the same qualified capital investment or cost incurred for
9 qualified services under AS 38.05.180(i), AS 41.09.010, AS 43.55.023, [OR]
10 43.55.025, or 43.55.026. However, a taxpayer may elect not to obtain a credit under
11 this section in order to qualify for a credit provided under AS 38.05.180(i),
12 AS 41.09.010, AS 43.55.023, [OR] 43.55.025, or 43.55.026.

13 *** Sec. 2.** AS 43.55 is amended by adding a new section to read:

14 **Sec. 43.55.026. Development cost credit.** (a) This section applies to a credit

1 for a qualified development expenditure incurred before 2018 and before the start of
2 sustained production that is taxable under AS 43.55.011(e). The qualified development
3 expenditure must be incurred for development outside of the Cook Inlet sedimentary
4 basin and outside of the Point Thomson unit established under AS 38.05.180(p) as the
5 area of the Point Thomson unit existed on December 31, 2010. The qualified
6 development expenditure must be for the development of a

7 (1) lease or property that, as of December 31, 2010, contains land that
8 is not or previously had not been within a unit or is not or had not previously been
9 involved directly in sustained production; or

10 (2) pool that, as of December 31, 2010, is not directly involved in or
11 had not previously been involved directly in sustained production.

12 (b) The total amount of the credits under this section is equal to 100 percent of
13 the qualified development expenditures that are incurred after the completion of the
14 first well drilled that discovers a pool capable of commercial production from the lease
15 or property and before the start of sustained production, less the amount of credits
16 taken under AS 43.55.023(a) and (b). In consultation with the Alaska Oil and Gas
17 Conservation Commission, the department shall determine the date

18 (1) on which the first well drilled discovered a pool capable of
19 production; and

20 (2) of the start of sustained production from the pool, lease, or
21 property.

22 (c) A credit under this section may be applied against the tax levied by
23 AS 43.55.011(e) for the pool, lease, or property that is the basis for the credit until the
24 credit for qualified development expenditures has been fully applied.

25 (d) A qualified development expenditure that is taken as a credit under this
26 section may not be used as an expenditure for which a credit may be taken under
27 AS 43.20.043. A credit under AS 43.55.023 may not be taken against the tax levied by
28 AS 43.55.011(e) for the pool, lease, or property that is the basis for a credit during the
29 same month in which a credit is taken under this section.

30 (e) A credit or portion of a credit under this section is not transferable and may
31 not be used to reduce a person's tax liability under AS 43.55.011(e) to below zero for

1 any calendar year.

2 (f) The department shall adopt regulations describing the procedures for
3 determining the amount of the credit, record keeping, verification of the accuracy of
4 the credit claimed, allocating expenditures to a pool eligible for a credit under (a)(2) of
5 this section, and other regulations necessary to administer this section.

6 (g) If a pool, lease, or property for which a credit may be taken under this
7 section subsequently becomes a part of a unit, or a pool that is in a unit first begins
8 sustained production after December 31, 2010, the credit may be applied only against
9 the tax levied by AS 43.55.011(e) for the production of oil and gas attributable to the
10 pool, lease, or property that qualified for the credit. For the purpose of applying the
11 credit, the tax shall be allocated to the pool, lease, or property that qualified for the
12 credit in proportion to the volume of production from that pool lease or property
13 within the unit.

14 (h) In this section,

15 (1) "pool" has the meaning given in AS 31.05.170;

16 (2) "qualified development expenditure" means an expenditure, other
17 than an expenditure for exploring for new oil or gas reserves, that may be recognized
18 as a qualified capital expenditure as defined in AS 43.55.023;

19 (3) "sustained production" has the meaning given in AS 43.55.025(l).

20 * **Sec. 3.** AS 43.55.180(a) is amended to read:

21 (a) The department shall study

22 (1) the effects of the provisions of this chapter on oil and gas
23 exploration, development, and production in the state, on investment expenditures for
24 oil and gas exploration, development, and production in the state, on the entry of new
25 producers into the oil and gas industry in the state, on state revenue, and on tax
26 administration and compliance, giving particular attention to the tax rates provided
27 under AS 43.55.011, the tax credits provided under AS 43.55.023 - 43.55.026
28 [AS 43.55.023 - 43.55.025], and the deductions for and adjustments to lease
29 expenditures provided under AS 43.55.160 - 43.55.170; and

30 (2) the effects of the tax rates under AS 43.55.011(i) on state revenue
31 and on oil and gas exploration, development, and production on private land, and the

1 fairness of those tax rates for private landowners.

2 * **Sec. 4.** AS 44.99 is amended by adding new sections to read:

3 **Article 06. Oil and Gas Competitiveness Review Board.**

4 **Sec. 44.99.600. Oil and Gas Competitiveness Review Board established. (a)**

5 The Oil and Gas Competitiveness Review Board is established.

6 (b) The board shall consist of nine members as follows:

7 (1) one senator appointed by the president of the senate;

8 (2) one representative appointed by the speaker of the house of
9 representatives;

10 (3) five members of the public appointed by the governor, including
11 one member who is a petroleum engineer, one member who is a geologist, one
12 member who is an economist, and one member who is a member of an environmental
13 or conservation group;

14 (4) the commissioner of natural resources or the commissioner's
15 designee; and

16 (5) the commissioner of revenue or the commissioner's designee.

17 (c) The senator and representative appointed to the board under (b)(1) and (2)
18 of this section shall be cochaurs.

19 (d) Each legislative member serves for the duration of the legislature during
20 which the member is appointed. Each public member serves for three years. An
21 individual who has served on the board may be reappointed.

22 (e) A vacancy on the board shall be filled in the manner of the original
23 appointment.

24 (f) A member of the board may be removed and replaced at the discretion of
25 the person appointing that member.

26 (g) The public members of the board serve without compensation but shall
27 receive per diem and travel expenses authorized for boards and commissions under
28 AS 39.20.180.

29 (h) The board may enter into contracts for professional services and may
30 employ staff for administrative support for the board.

31 **Sec. 44.99.610. Duties.** The duties of the board include the following:

1 (1) review historical, current, and potential levels of investment in the
2 state's oil and gas sector;

3 (2) identify factors that affect investment in oil and gas exploration,
4 development, and production in the state, including tax structure, rates, and credits;
5 royalty requirements; infrastructure; workforce availability; and regulatory
6 requirements;

7 (3) review the competitive position of the state to attract and maintain
8 investment in the oil and gas sector in the state as compared to the competitive
9 position of other regions with oil and gas resources;

10 (4) in order to facilitate the work of the board, establish procedures to
11 accept and keep confidential information that is beneficial to the work of the board,
12 including the creation of a secure data room and confidentiality agreements to be
13 signed by individuals having access to the confidential information;

14 (5) make written findings and recommendations, together with
15 suggested legislation, to the Alaska State Legislature before December 1 of each year,
16 or as soon thereafter as practicable, regarding

17 (A) changes to the state's regulatory environment that would be
18 conducive to encouraging increased investment while protecting the interests
19 of the people of the state and the environment;

20 (B) changes to the state's fiscal regime that would be conducive
21 to increased and ongoing long-term investment in and development of the
22 state's oil and gas resources; and

23 (C) alternative means for increasing the state's ability to attract
24 and maintain investment in and development of the state's oil and gas
25 resources.

26 **Sec. 44.99.620. Information to be provided to board.** (a) The commissioner
27 of natural resources, the commissioner of revenue, the commissioner of environmental
28 conservation, and other commissioners and state agencies that have responsibility for
29 and maintain information related to oil and gas investment and activity in the state
30 shall, at the request of the board, provide information required by the board to carry
31 out the duties described in AS 44.99.610.

1 (b) At the request of the board, and except for information that is confidential
2 under AS 43.05.230, a commissioner may disclose to the board information that is
3 otherwise confidential after each member of the board and each staff member for the
4 board with access to the information signs a confidentiality agreement prepared by the
5 commissioner making the disclosure. Information that is confidential under
6 AS 43.05.230 may not be disclosed to the board.

7 **Sec. 44.99.630. Definition.** In AS 44.99.600 - 44.99.630, "board" means the
8 Oil and Gas Competitiveness Review Board.

9 * **Sec. 5.** AS 44.99.600, 44.99.610, 44.99.620, and 44.99.630, added by sec. 5 of this Act,
10 are repealed June 30, 2021.

11 * **Sec. 6.** This Act takes effect immediately under AS 01.10.070(c).

Prepared 3-24-11: mj & mp

NOTE: Comparison of SB 85 to Draft CS SB 85 version 27-LS0484\E

Shaded is new language

Double strike through is deleted language

SENATE BILL NO. 85

"An Act providing for a tax credit applicable to the oil and gas production tax based on the capital cost of developing new oil and gas production; establishing the Oil and Gas Competitiveness Review Board, and providing for an effective date."

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

* **Section 1.** AS 43.20.043(g) is amended to read:

(g) A taxpayer that obtains a credit for a qualified capital investment or cost incurred for qualified services under this section may not also claim a tax credit or royalty modification for the same qualified capital investment or cost incurred for qualified services under AS 38.05.180(i), AS 41.09.010, AS 43.55.023, [OR]43.55.025, or 43.55.026. However, a taxpayer may elect not to obtain a credit under this section in order to qualify for a credit provided under AS 38.05.180(i), AS 41.09.010, AS 43.55.023, [OR] 43.55.025, or 43.55.026.

~~* **Sec. 2.** AS 43.55.023(a) is amended to read:~~

~~(a) A producer or explorer may take a tax credit for a qualified capital expenditure as follows:~~

~~(1) notwithstanding that a qualified capital expenditure may be a deductible lease expenditure for purposes of calculating the production tax value of oil and gas under AS 43.55.160(a), unless a credit for that expenditure is taken under AS 38.05.180(i), AS 41.09.010, AS 43.20.043, [OR] AS 43.55.025, or 43.55.026, a producer or explorer that incurs a qualified capital expenditure may also elect to apply a tax credit against a tax levied by AS 43.55.011(e) in the amount of 20 percent of that~~

~~expenditure; however, not more than half of the tax credit may be applied for a single calendar year;~~

~~(2) a producer or explorer may take a credit for a qualified capital expenditure incurred in connection with geological or geophysical exploration or in connection with an exploration well only if the producer or explorer~~

~~(A) agrees, in writing, to the applicable provisions of AS 43.55.025(f)(2);~~

~~(B) submits to the Department of Natural Resources all data that would be required to be submitted under AS 43.55.025(f)(2).~~

* **Sec. 2 3.** AS 43.55 is amended by adding a new section to read:

Sec. 43.55.026. Development cost credit. (a) This section applies to a credit for a qualified development expenditure incurred before 2018 and before the start the date of sustained production of oil or gas in paying quantities for a lease or property that is taxable under AS 43.55.011(e). The qualified development expenditure must be incurred for development outside of the Cook Inlet

Prepared 3-24-11: mj & mp

sedimentary basin and outside of the Point Thomson unit established under AS 38.05.180(p) as the area of Point Thomson existed on December 31, 2010. The qualified development expenditure must be for the development of a

- (1) lease or property that, as of December 31, 2010 and that contains land that, as of December 31, 2010, is not or previously had not been within a unit or is not or had not previously been involved directly in sustained production or; or produced oil or gas in paying quantities.
- (2) Pool that, as of December 31, 2010, is not directly involved in or had not previously been involved in sustained production.

(b) The total amount of the credit under this section is equal to 100 percent of the qualified development expenditures that are incurred after the completion of the first well drilled that discovers a pool capable of commercial production from the lease or property and before the start commencement of sustained production in paying quantities, less the amount of credits taken under AS 43.55.023(a) and (b). The department, In consultation with the

- (1) Alaska Oil and Gas Conservation Commission, the department shall determine the date (1) on which the first well drilled discovered a pool capable of production from a lease or property for which the credit is taken; and
- (2) Department of Natural Resources, shall determine the date of the commencement start of sustained production from the pool, lease or property, in paying quantities from the lease or property for which the credit is taken.

(c) A The credit under this section may be applied against the tax levied by due under AS 43.55.011(e) for the pool, lease, or property that is the basis for the credit until the credit for qualified development expenditures has been fully applied. during the five year period immediately following the date of the commencement of production in paying quantities, or, if the credit is fully applied before the end of the five year period, until the date the credits for qualified development expenditures have been fully applied against the tax due under AS 43.55.011(e), whichever occurs first. A credit for a qualified expenditure expires if not taken within five years after the date of the commencement of production in paying quantities and may not be applied to the tax due under AS 43.55.011(e) for the production of oil or gas from a lease or property not eligible for the credit under this section.

(d) A qualified development expenditure that is taken as a credit under this section may not be used as an expenditure for which a credit may be taken under AS 43.20.043 or AS 43.55.023. A credit under AS 43.55.023 may not be taken against the tax levied by due under AS 43.55.011(e) for the pool, lease, or property that is the basis for a credit during the same month in which a credit is taken under this section.

(e) A credit or portion of a credit under this section is not transferable and may not be used to reduce a person's tax liability under AS 43.55.011(e) to below zero for any calendar year.

(f) The department shall adopt regulations describing the procedures for determining the amount of the credit, record keeping, verification of the accuracy of the credit claimed, allocating expenditures to a pool eligible for a credit under (a)(2) of this section and other regulations necessary to administer this section.

Prepared 3-24-11: mj & mp

(g) If a pool, lease or property for which a credit may be taken under this section subsequently becomes a part of a unit, or a pool that is in a unit first begins sustained production after December 31, 2010, under AS 38.05.180(p), the credit may be applied only against the tax levied by ~~due~~ under AS 43.55.011(e) for the production of oil and gas attributable to the pool, lease or property that qualified for the credit in proportion to the volume of production from that pool, lease or property within the unit .

(h) In this section,

(1) "pool" has the meaning given in AS 31.05.170; ~~"production in paying quantities" means production of oil and gas in quantities sufficient to recover the cost of operating and marketing, although the quantity may be insufficient to recover the cost of drilling;~~

(2) "qualified development expenditure" means an expenditure, other than an expenditure for exploring for new oil or gas reserves, that may be recognized as a ~~(A) qualified capital expenditure as defined in AS 43.55.023; or (B) lease expenditure under AS 43.55.165 if oil or gas had been produced from the lease or property at the time the qualified development expenditure was incurred.~~

(3) "sustained production" has the meaning given in AS 43.55.025(l).

* **Sec. 3 4.** AS 43.55.180(a) is amended to read:

(a) The department shall study

(1) the effects of the provisions of this chapter on oil and gas exploration, development, and production in the state, on investment expenditures for oil and gas exploration, development, and production in the state, on the entry of new producers into the oil and gas industry in the state, on state revenue, and on tax administration and compliance, giving particular attention to the tax rates provided under AS 43.55.011, the tax credits provided under **AS 43.55.023 - 43.55.026** [AS 43.55.023 - 43.55.025], and the deductions for and adjustments to lease expenditures provided under AS 43.55.160 - 43.55.170; and

(2) the effects of the tax rates under AS 43.55.011(i) on state revenue and on oil and gas exploration, development, and production on private land, and the fairness of those tax rates for private landowners.

*Sec. 4 AS 44.99 is amended by adding new sections to read:

Entire Section 4 in version \E is new (page 4, line 2 to page 6 line 8) Oil and Gas Competitiveness Review Board.

* Sec. 5 AS 44.99.600, 44.99.610, 44.99.620 and 44.99.630, added by sec. 5 of this Act are repealed June 30, 2021.

* **Sec. 6 5.** This Act takes effect immediately under AS 01.10.070(c).



Official Business

ALASKA STATE LEGISLATURE

SENATOR THOMAS H. WAGONER,

Co-Chair: Senate Resources Committee

Member: C&RA Committee
Member: Regulatory Review

Member: LB&A Committee
Member: World Trade

Session: January - May
State Capitol, #427
Juneau, AK 99801
Phone: 907-465-2828 Fax: 907-465-4779

Interim: May - December
145 Main Street Loop; Suite 226
Kenai, AK 99611
Phone: 907-283-7996 Fax 907--283-8127

Draft CS Senate Bill 85 version \E 3-24-11 **Sectional Analysis** **TAX CREDIT FOR NEW OIL & GAS DEVELOPMENT**

TITLE: Adds new Oil and Gas Competitiveness Review Board.

Section 1: Existing law prohibits multiple tax credits claimed against corporate income, this adds the new credits established in this bill, **43.55.026**.

Section 3: sets out new **43.55.026** for the new tax credit.

(a) Directs that the new credit applies to qualified development expenditures that were incurred before 2018 and before sustained production occurs. Excludes the credit from the Cook Inlet Basin and the Point Thomson unit. Restricts the credit to:

- (1) A lease or property not within a unit or previously been within a unit, or
- (2) A pool that is not or previously had not been involved with sustained production.

NOTE: effect is that a pool within a unit is eligible if it is not now or previously had been under sustained production. Exclusion specifically of Point Thomson unit compared to subsection (1) is duplicative and should be deleted.

(b) Establishes that the credit amount is 100% of the qualified development expenditures incurred after completing the drilling of the first well that discovers a pool (capable of commercial production) and before production (in paying quantities) commences. The Department of Revenue (DOR), in consultation with the Alaska Oil and Gas Commission (AOGCC) establishes the date of the credit from the first well drilled to the start of sustained production from that pool, lease or property.

- (c) Establishes that the credit may be applied against the production tax levied until the credits for the expenditures are fully applied, whichever occurs first.

Essentially, the production tax liability is used to offset the development costs and the production tax liability is the determining factor for the amount of credit.

- (d) Restricts the use of the new credit so there are not multiple credits.
- (e) Establishes that the credit or any portion of the credit is not transferable and may not reduce the tax liability below zero for AS 43.55.011(e) (the production tax) for any calendar year.

Essentially, the tax credit stays with the drilling site and the new credit may not allow the tax payer to obtain a refund from the state in any calendar year.

- (f) Allows the DOR to adopt regulations needed to administer the new credit.
- (g) Establishes procedures so that when a lease or property that utilizes this new credit becomes part of a unit under AS 38.05.180(p)¹, the credit is applied only to the production tax due for the lease or property that qualified for the credit.
- (h) Defines:
 1. "pool" by referencing existing statute AS 31.05.170.
 2. "qualified development expenditure".
 3. "sustained production" by referencing existing statute AS 43.55.025(l).

Section 4: Establishes a new Oil and Gas Competitiveness Review Board.

Section 5: This is the repeal section for the new Oil and Gas Competitiveness Review Board.

Note that it references "sec. 5" which is incorrect – should read "sec. 4".

Amends existing law to include new section for this tax credit in **43.55.026**.

Section 6: Establishes an immediate effective date for the legislation.

¹ AS 38.05.180(p) (oil and gas and gas only leasing statutes regarding unitization)

70 & 148, LLC

• 1421 Blake Street • Denver, CO 80202 •
Phone 303-623-1821 • Fax 303-623-3019

March 29, 2011

Honorable Tom. Wagoner
Co-chair, Senate Resources Committee
State Capitol
Juneau, AK 99801

Re: Senate Bill 85

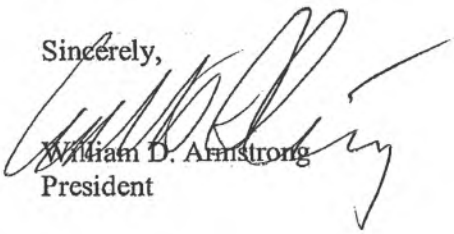
Dear Chairman Wagoner -

We are appreciative of your efforts behind the introduction of Senate Bill 85. As you know, our experiences under ACES has proven to be difficult in attracting new investment to Alaska's North Slope.

The proposed 100% capital credit program, as proposed in your legislation, would clearly provide a meaningful incentive for new investment on the North Slope.

Again, we appreciate your efforts to modify Alaska's burdensome tax regime. It is important that Alaska make changes this legislative session. We will continue to monitor the progress of your legislation.

Sincerely,


William D. Armstrong
President

Mary Jackson

From: Sen. Tom Wagoner
Sent: Wednesday, March 30, 2011 2:33 PM
To: Mary Jackson
Subject: FW: Amended Written Public Testimony on SB49
Attachments: Senate Natural Resources Committee Co.docx

From: Jwmelliott [<mailto:jwmelliott@aol.com>]
Sent: Wednesday, March 30, 2011 12:40 PM
To: Sen. Tom Wagoner
Cc: Sen. Joe Paskvan; Sen. Gary Stevens; Sen. Johnny Ellis; Judy Stewart
Subject: Amended Written Public Testimony on SB49

Senator Wagoner, I inadvertently confused your bill, SB85, with that of Governor Parnell's, SB49. Therefore, I have amended my public testimony to correct my error. I would be most appreciative if you would substitute my amended written public testimony, which is the Attachment to this email message, for my earlier submission containing my aforementioned inadvertent error, i.e., mixing up SB85 with SB49.

Respectfully,

/s/ James W. Elliott



Fax Cover Sheet

Anchorage Legislative Information Office
Office - (907) 269-0111 Fax - (907) 269-0229

To: Senators Paskivan & Wignner Fax: _____ Phone: _____

From: MR. JAMES ELLIOT

Instructions: *AMENDED* Testimony

Date: 3-30-2011 Time: _____

Number of Pages: 2 (including cover sheet)



Alaska State Legislature

Please enter into the record my testimony to the Senate Resources Committee

Bill/Subject: SB49

Date: March 30, 2011

.....
**SB49 Emailed Written Public Testimony (Amended) to Senate Natural Resources Committee
 through Senator Wagoner' Office - March 30, 2011**

Senate Natural Resources Committee Co-Chairs Sen. Paskvan and Sen. Wagoner, I am unable to attend today's public hearing on the subject bill. Therefore, I respectfully request that my written testimony, which follows, be entered in the public record of today's hearing on SB49.

First, I wish to thank you and the other members of the Senate Natural Resources Committee for your service on-behalf of the people of Alaska. The Alaska Legislature is an esteemed institution, and your job of charting a fiscally sound course for our great State regarding its natural resources is a daunting responsibility.

Second, I am pleased to have this opportunity to submit my testimony, albeit in writing, on SB49. Specifically, with respect to Governor Parnell's proposed tax reductions and incentives to the big oil producers, ConocoPhillips, BP, Exxon, Shell, et al., I have the following concerns and comments:

1. What exactly is the Governor's justification for Alaska giving some the largest, most profitable corporations on the planet tax breaks and incentives to find and produce a product that, by all accounts, is in high demand and for which there is a limited supply globally? To date, the Governor has failed to present any convincing evidence in support of his proposal to reduce taxes and provide incentives to the major oil companies.
2. Where are the data, analyses, and oil industry commitments that would lend credibility to the Governor's proposed fiscal strategy for creating more jobs and increasing future oil revenues for the State if his planned is approved by the Legislature?
3. By the Governor's own estimation, his tax breaks and incentives to the oil companies will cost Alaska \$5 billion in revenue over the next five fiscal years. Some in the Legislature have estimated that his proposal could cost the State, depending on the price of oil, as much as \$2 billion in revenue annually. Can Alaska afford the Governor's plan? I suggest it cannot.
4. I am just a four-acre farmer, but the last time I checked the advice of reputable economic and fiscal experts, the Governor's wishful thinking-cross your fingers approach to fiscal planning is not sound policy. Don't Alaskans deserve a more fiscally prudent plan than our Governor's roll of the dice?
5. To offset his projected loss in State revenue, Governor Parnell proposes that Alaska dip into its savings to cover any deficits necessary to balance its annual operating budgets. Would it not be more prudent to forego his tax breaks and incentives to the oil companies in favor of the more conservative fiscal policy of paying for current year expenditures from current year revenues? Using one-time, non-recurring savings to cover budget deficits, as the Governor proposes, is a slippery slope fiscally.
6. According to the National Petroleum Council's Global Oil & Gas Study, which was made available July 18, 2007, "The major oil and gas companies are increasingly turning their attention to overseas development opportunities, leaving U.S. production largely in the hands of independent oil and gas companies." That being the case, one ought to ask just how practical is Governor Parnell's proposal to place Alaska in the unenviable position of having to deficit spend annually and drain down its savings to offset said annual operating budget deficits on the decidedly uncertain bet that his plan will attract more exploration and production activities from the major oil companies, like ConocoPhillips, BP, Exxon, and Shell?

Per the concerns and comments expressed above, I am opposed to SB49, urge you to vote against it, and support Senator Wagoner's proposed legislation, SB86, instead.

/s/ James W. Elliott

2440 East Tudor Road #1135

Anchorage, Alaska 99507

Senate Bill 85
Senate Resources Committee
Testimony by AVCG, LLC

Ken Thompson
Managing Director of AVCG, LLC
March 30, 2011

Discussion

Purpose: Present *ideas to re-incentivize investment and increase the competitiveness of Alaska relative to other oil basins with one common State & Industry Goal in mind:*

LEVEL ALASKA'S OIL PRODUCTION

- Thanks...and Introduction to Alaska Venture Capital Group (AVCG)
- Fundamental improvements to ACES to attract new investors for E&P
- The “**next frontiers**” for major developments on the NS
 - ✓ **Exploration with smaller fields sharing regional processing facilities**
 - ✓ **Low-permeability sands**
 - ✓ **Source rock shales**
 - ✓ **Major projects existing fields, ie “Big Fields Get Bigger”**
 - ✓ **NS viscous oil**
 - NS offshore oil
 - NS natural gas

AVCG & BRPC: Entity Comparison

AVCG LLC

Holding company

Own all leases

Assignments

ORRI

Production Revenues

Manage overall direction, strategy

BRPC budget, plan

Staffing

Negotiation of all business deals

My Main Job!!! → **Attract new investors & capital to Alaska**



Brooks Range Petroleum Corporation

Subsidiary of AVCG, LLC

Technical services for AVCG

JV companies as needed

Manage operations

office

staffing

misc. services

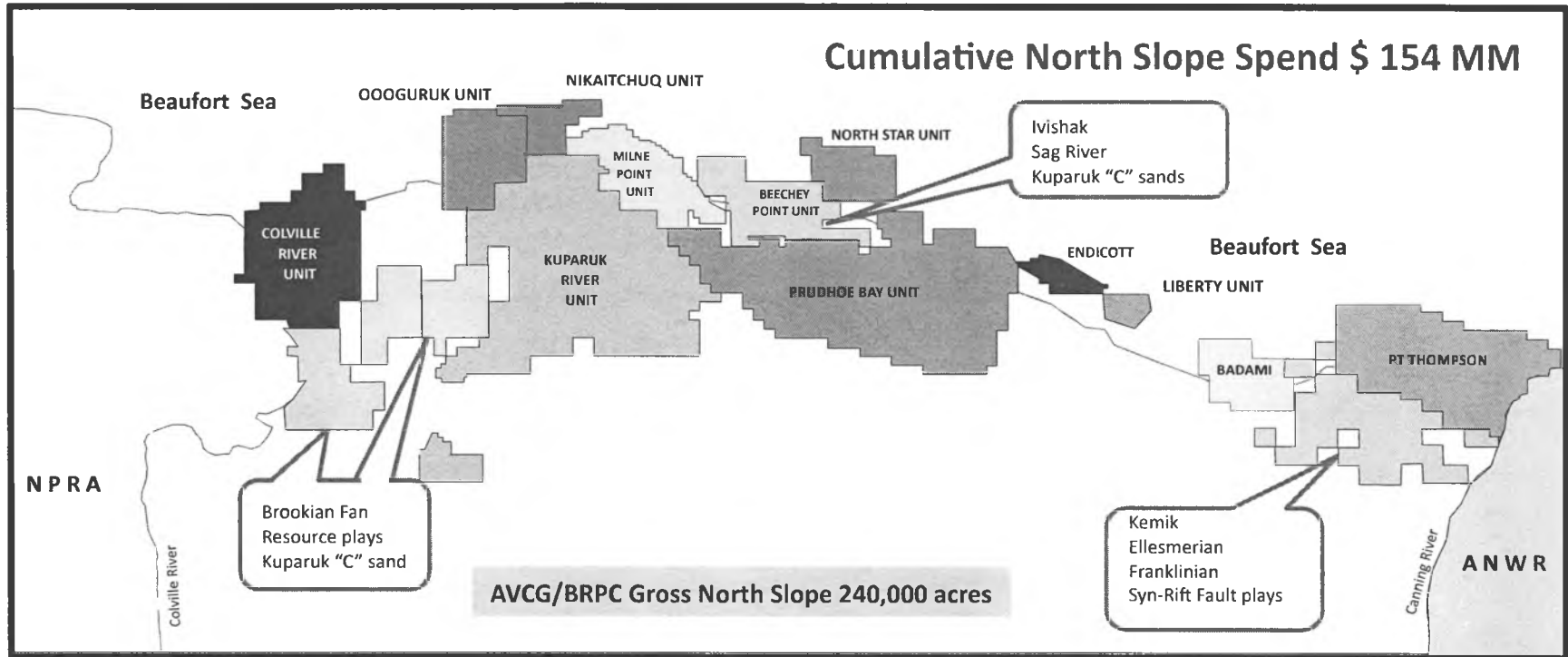
Administrative services

AVCG billings

accounting

lease administration

AVCG JV Leasehold Portfolio



Western – 94,142 acres

Central – 52,878 acres

Eastern – 89,800 acres

Activity

220 sq. mi. new 3 – D seismic
Drilled Kuparuk test & discovery

Activity

130 sq. mi. new 3 – D seismic
Drilled Ivishak, Sag River & Kuparuk tests
Ivishak & Sag River discoveries
Formed Beechey Point Unit
Acquired Pete's Wicked discovery

Activity

Purchased area 2 – D lines

Plan

Drill North Tarn Brookian/Kuparuk test
Progress 3D seismic and prospects
Exploit resource plays in area

Plan

Drill East Shore Kuparuk formation test
Progress Plan of Development of known reserves
Obtain approval of development sanctioning

Plan

Acquire 150 sq. miles of 3D seismic
Looking for partner on Shoot-to-Earn
Continue to progress 2D data
Monitor Point Thomson activities

Attracting New Investors In The Face Of Global Competition For Capital

Side note: effect upon AVCG relative to Bow Valley/Dana Petroleum, i.e. Dana Petroleum elected not to participate on North Slope because of better tax treatment and higher returns in North Sea

UK North Sea exploration/development

Substantial tax incentives enacted 2009 to encourage development

- NEW FIELDS EXEMPT FROM 20% SUPPLEMENTARY SURCHARGE TAX LEVIES ON TOP OF 30% CORPORATION TAX
- EXEMPTION APPLIES TO FIRST \$1.3 BILLION OF EACH FIELD'S TAXABLE INCOME

2010 vs 2009: 1Q drilling up 29%; drilling 2Q up 133%!

Anticipate significant new production

North Dakota to Surpass Alaska in Daily Production

Suspension of severance tax for initial development, i.e. "Severance Tax Holidays"

Expedited permitting by State

650 new wells drilled in 2010 with 168 per month in December!

Reserve estimates of 5-11 billion bbls compared to Prudhoe 13 bbl

Record oil production **ON THE INCLINE** to double this decade

370,000 BOPD to increase to 700,000 BOPD and surpass Alaska

Israel : Oil tax structure

Increase government take from 30% to 52% - 62%
Maintain 30% rate until producer recovers 200% of investment

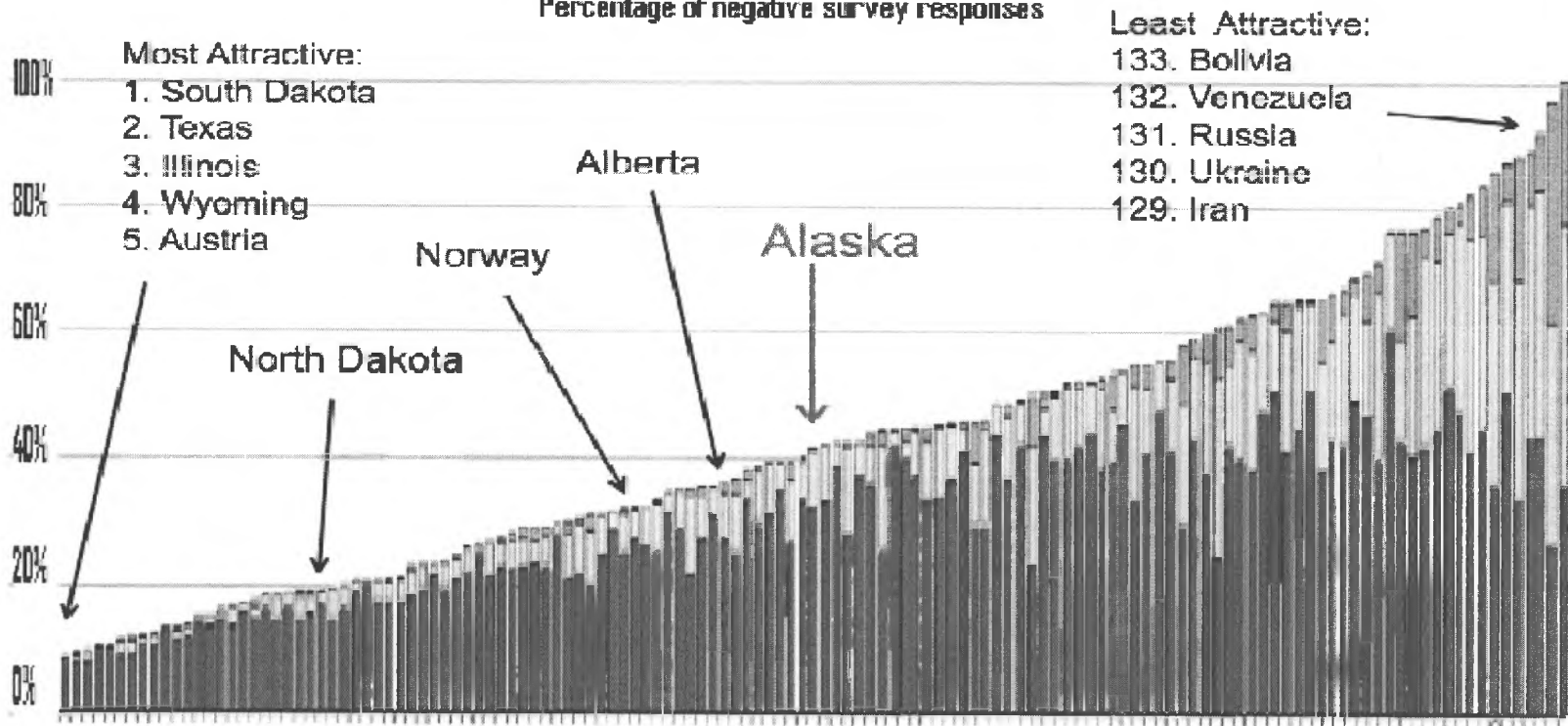
Attracting New Capital and/or New Investors To Alaska Are Keys To Increasing Activity That Will Level Production



Frasier: Alaska is #68 of 133 in terms of overall attractiveness



Frasier All-Inclusive Composite Index for 133 jurisdictions
Percentage of negative survey responses



Source: Frasier Institute 2010 Global Petroleum Survey

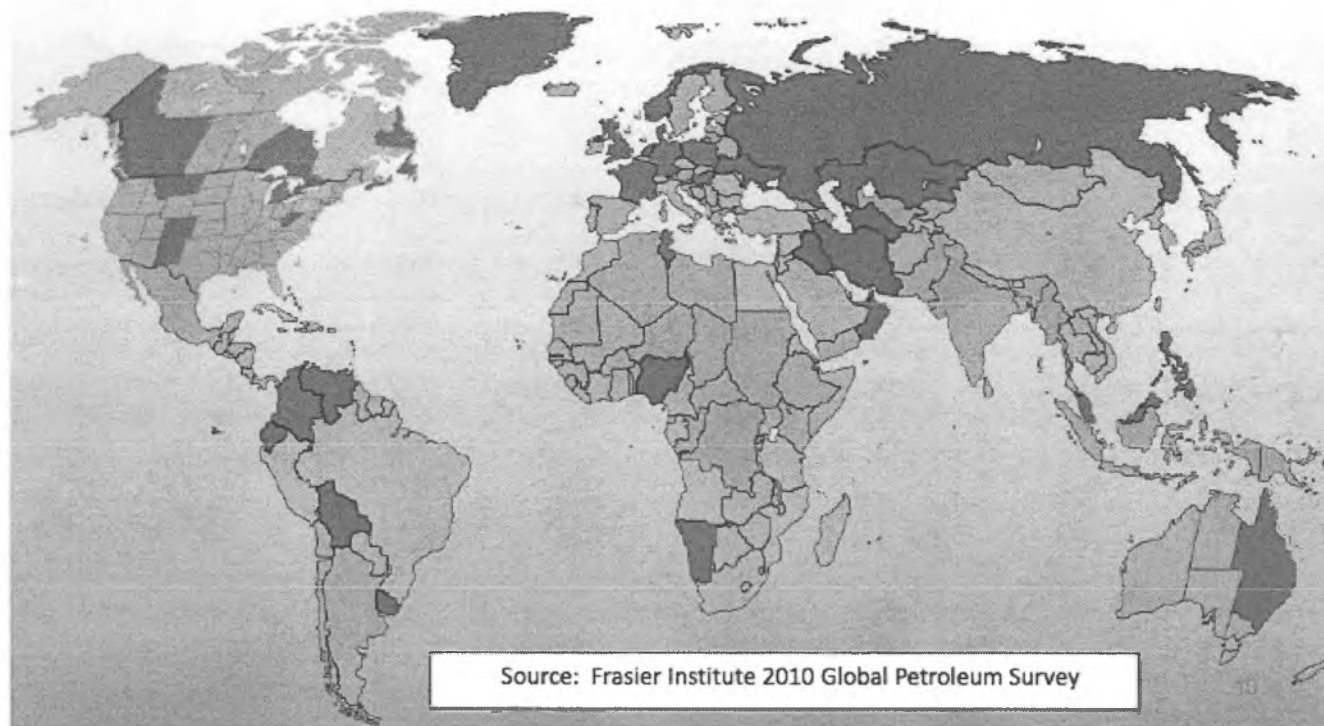
Source: SB 49 Dept of Revenue Presentation, 2/5/2011



Frasier: Alaska's investment climate is "in the middle" globally



Most attractive ■ 2nd Quintile ■ 3rd Quintile ■ 4th Quintile ■ Least attractive ■ Unmeasured ■



Source: Frasier Institute 2010 Global Petroleum Survey

Source: SB 49 Dept of Revenue Presentation, 2/5/2011

AVCG's Thoughts, Suggested Changes To SB 85

- 1) **AVCG supports the SB 85 Development Cost Credit for a credit of up to 100% of qualified CAPEX...would help us attract new investors & capital**
 - ✓ For AVCG's approach to development of "early on production" with stages of modular facilities rather than wait on one massive facility, there is significant – perhaps 50% - CAPEX for development wells and add-on modules 2 years or so after production startup
 - ✓ Modify credit to apply to all CAPEX in the approved Field Development Plan and not just CAPEX spent to start of production, eg Credits to the date the Department of Natural Resources attests that the formal Field Development Plan for CAPEX has been achieved ... or for CAPEX spent 2 years after initial production startup

- 2) **However, AVCG believes that to level production, comprehensive change must address ALL the "next frontiers" for major developments on the NS**
 - ✓ **Exploration with smaller fields sharing regional processing facilities**
 - ✓ **Low-permeability sands**
 - ✓ **Source rock shales**
 - ✓ **NS viscous oil**
 - ✓ **Major projects in existing fields/zones, ie "Big Fields Get Bigger"**
 - NS offshore oil
 - NS natural gas

- 3) **SB 85 addresses NEW oil, e.g. the first 3 items listed above...these may be insufficient to level the production...SB 49, however, addresses ALL oil sources which is needed**

AVCG's Recommends Merger of 49 & 85 To Achieve The Common Goal of "No Decline"

Merge ideas of SB 85 into the broader bill and support proposals in SB 49 :

- 1) Revise the progressivity surcharge to the "bracketed tax structure" with calculations made annually instead of monthly**
- 2) Cap the total tax at 50% when oil prices top \$92.50/bbl**
- 3) For development of new fields outside existing production units, the base tax rate will be 15% instead of 25% and cap the total tax at 40%..and introduce credit structure of HB 85**

A bracketed structure with reduced base rate and cap and a reduced base tax rate for new fields with a lower cap would attract more investor partners for AVCG et al to increase small field development and establishment of the North Slope's first "open access" facility sharing processing facilities.

- 4) Accelerate the payment for exploration and other qualified capital investments to one year vs. two years**

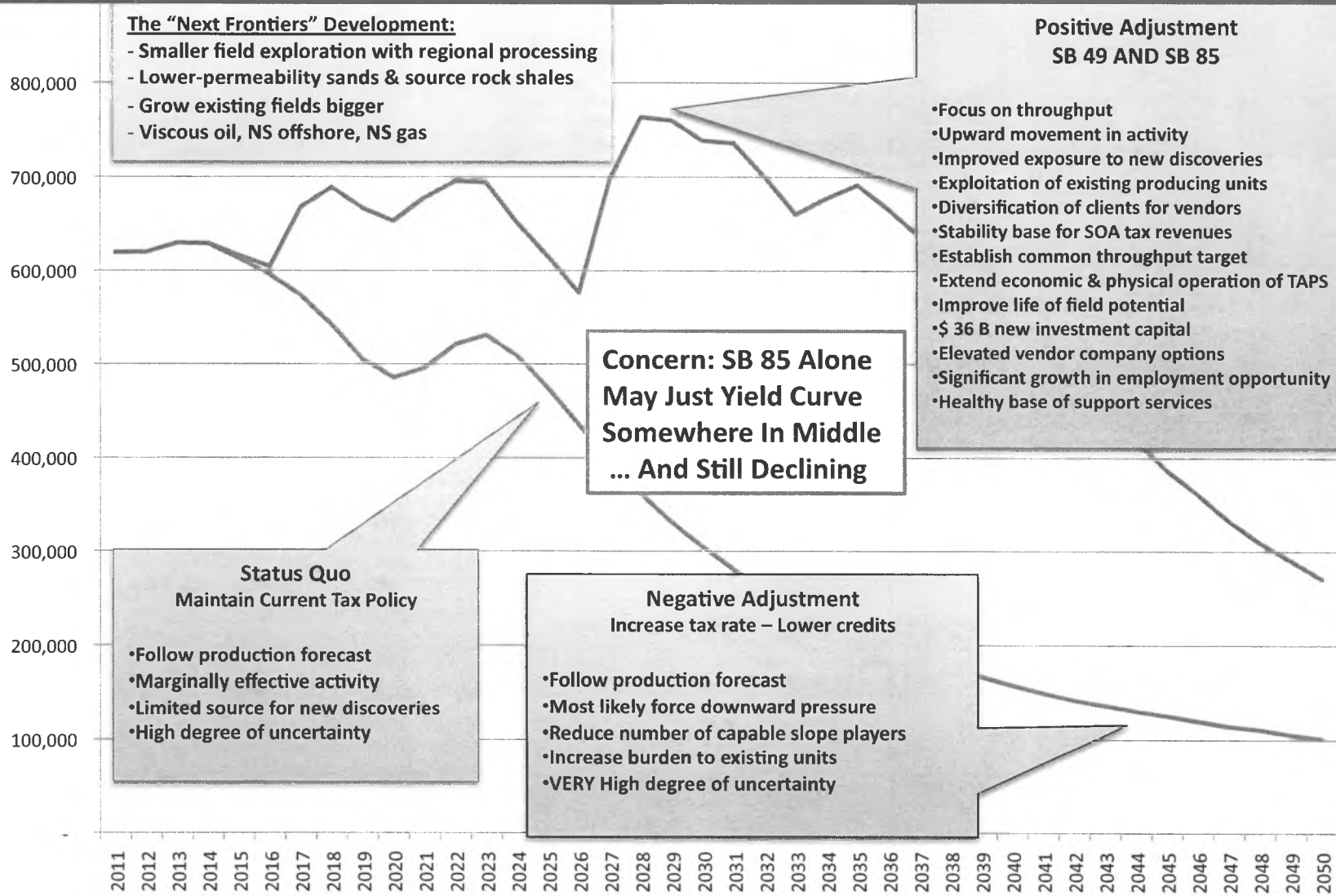
The acceleration of credit recovery payments to a one year cycle would allow for AVCG and its partners to consider drilling 3 exploration wells per year instead of an average of 2 per year...a chance for more discoveries sooner

- 5) Increase the tax credits for "qualified capital" investments from the current 20% to 40%...OR SB 85**

An increase in qualified capital credits to 40% would provide immediate impact to BRPC's project investment base and would extend our ability to encourage additional and continued capital investment from our current WIO's therefore providing more opportunities for successful discoveries and future development projects

- 6) Extend indefinitely the "Small Producer Tax Credit" of \$12MM a year from expiring on May 1, 2016 (or certainly extend another 5 years to May 1, 2021 then re-assess at that time). This is an item not currently in current bills but would be helpful in attracting new long-range development capital for BRPC and others like our company.**

Currently, we have a sanctioning proposal in front of our WIO's that projects first oil and revenues in 2013. With the Small Producers Credit expiring in May 2016, the development would be limited to a 3 year use of this credit. We would propose an extension through 2021 to allow our first project the full credit to attract new investors.





Official Business

ALASKA STATE LEGISLATURE

SENATOR THOMAS H. WAGONER,

Co-Chair: Senate Resources Committee

Member: C&RA Committee
Member: Regulatory Review

Member: LB&A Committee
Member: World Trade

Session: January - May
State Capitol, #427
Juneau, AK 99801
Phone: 907-465-2828 Fax: 907-465-4779

Interim: May - December
145 Main Street Loop; Suite 226
Kenai, AK 99611
Phone: 907-283-7996 Fax 907--283-8127

Changes to CS SB 85 version E (27-LS0484\E) in CS SB 85 version X (27-LS0484\X)

- Title:** No changes.
- Section 1:** No changes.
- Section 2:** The following changes were made to section 2.
1. 43.55.026 (a): The period during which a credit can be accrued has been changed to within 24 months after the completion of the first development well for a qualifying pool, lease or property. The reference to the Pt. Thomson unit in the E version has been removed.
 2. 43.55.026 (b): Credits earned for exploration expenditures under AS 43.55.025 have been added to the list of credits that are subtracted from the 100 percent of qualifying development expenditures. The timing of qualifying development expenditures and the consultation with AOGCC has been changed to conform to the change in subsection (a).
 3. 43.55.026 (c): No changes.
 4. 43.55.026 (d): Language relating to taking a credit under AS 43.55.023 during the same month in which a credit is taken has been deleted.
 5. 43.55.026 (e): No changes.
 6. 43.55.026 (f): Authority to promulgate regulations for allocating the tax levied by AS 43.55.011(e) for the purposes of (g) has been added to the powers granted to the department of Revenue.
 7. 43.55.026 (g): The allocation language has been simplified to clarify that a credit earned under AS 43.55.026 can offset a person's tax liability in proportion to the volume of production from the pool, lease or property for which the qualified development expenditure was incurred.
 8. 43.55.026 (h): The definition of qualified development expenditure has been limited to a qualified capital expenditure as defined in AS 43.55.023.
- Section 3:** Added a new section 3 that includes reference language to AS 43.55.160 (a) that conforms the change made in new section 4 to the calculation of production tax value.
- Section 4:** Added a new section 4 that adds a new subsection to AS 43.55.160 that increases the production tax value by the value of a credit received under AS 43.55.026.
- Section 5:** No changes to the section (previously section 3).

Changes to CS SB 85 version E (27-LS0484\E) in CS SB 85 version X (27-LS0484\X)

Page two of two

- Section 6: No changes to the section (previously section 4).
- Section 7: No changes to the section (previously section 5).
- Section 8: No changes to the section (previously section 6).

27-LS0484X
Bullock
4/1/11

CS FOR SENATE BILL NO. 85()
IN THE LEGISLATURE OF THE STATE OF ALASKA
TWENTY-SEVENTH LEGISLATURE - FIRST SESSION

BY

Offered:
Referred:

Sponsor(s): SENATORS WAGONER, Stevens, McGuire, Huggins, Dyson, Giessel, Menard

A BILL
FOR AN ACT ENTITLED

1 **"An Act providing for a tax credit applicable to the oil and gas production tax based on**
2 **the capital cost of developing new oil and gas production; relating to the determination**
3 **of the production tax value of oil and gas; establishing the Oil and Gas Competitiveness**
4 **Review Board; and providing for an effective date."**

5 **BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:**

6 *** Section 1.** AS 43.20.043(g) is amended to read:

7 (g) A taxpayer that obtains a credit for a qualified capital investment or cost
8 incurred for qualified services under this section may not also claim a tax credit or
9 royalty modification for the same qualified capital investment or cost incurred for
10 qualified services under AS 38.05.180(i), AS 41.09.010, AS 43.55.023, [OR]
11 43.55.025, or 43.55.026. However, a taxpayer may elect not to obtain a credit under
12 this section in order to qualify for a credit provided under AS 38.05.180(i),
13 AS 41.09.010, AS 43.55.023, [OR] 43.55.025, or 43.55.026.

14 *** Sec. 2.** AS 43.55 is amended by adding a new section to read:

1 **Sec. 43.55.026. Development cost credit.** (a) This section applies to a credit
2 for a qualified development expenditure incurred before 2018 and within 24 months
3 after the completion of the first development well for a qualifying pool, lease, or
4 property that is subject to the tax levied by AS 43.55.011(e). The qualified
5 development expenditure for which a credit may be authorized under this section must
6 be outside of the Cook Inlet sedimentary basin and for development of a

7 (1) lease or property that, as of December 31, 2010, contains land that
8 is not or previously had not been within a unit or is not or had not previously been
9 involved directly in sustained production; or

10 (2) pool that, as of December 31, 2010, is not directly involved in or
11 had not previously been involved directly in sustained production.

12 (b) The total amount of the credits under this section is equal to 100 percent of
13 the qualified development expenditures that are incurred within 24 months after the
14 completion of the drilling of the first development well for production from the lease
15 or property, less the amount of credits taken under AS 43.55.023(a) and (b) and
16 43.55.025 for the same expenditures. In consultation with the Alaska Oil and Gas
17 Conservation Commission, the department shall determine the date the drilling of the
18 first development well is completed for a pool capable of sustained production.

19 (c) A credit under this section may be applied against the tax levied by
20 AS 43.55.011(e) for the pool, lease, or property that is the basis for the credit until the
21 credit for qualified development expenditures has been fully applied.

22 (d) A qualified development expenditure that is taken as a credit under this
23 section may not be used as an expenditure for which a credit may be taken under
24 AS 43.20.043.

25 (e) A credit or portion of a credit under this section is not transferable and may
26 not be used to reduce a person's liability for the tax levied by AS 43.55.011(e) below
27 zero for any calendar year.

28 (f) The department shall adopt regulations describing the procedures for
29 determining the amount of the credit, record keeping, verification of the accuracy of
30 the credit claimed, allocating the tax levied by AS 43.55.011(e) to a pool, lease, or
31 property for the purposes of (g) of this section, and other regulations necessary to

1 administer this section.

2 (g) The credit under this section may be applied only against the tax levied by
3 AS 43.55.011(e) for the production of oil and gas attributable to the pool, lease, or
4 property for which a qualified development expenditure is incurred that qualifies for
5 the credit. For the purpose of applying the credit, the tax shall be allocated to the pool,
6 lease, or property that is subject to the credit in proportion to the volume of production
7 from that pool, lease, or property within the unit.

8 (h) In this section,

9 (1) "pool" has the meaning given in AS 31.05.170;

10 (2) "development well" means a well drilled to a pool capable of
11 sustained production;

12 (3) "qualified development expenditure" means a qualified capital
13 expenditure, as defined in AS 43.55.023, that is incurred after the drilling for the first
14 development well is complete;

15 (4) "sustained production" has the meaning given in AS 43.55.025(l).

16 * **Sec. 3.** AS 43.55.160(a) is amended to read:

17 (a) Except as provided in (b) of this section **and subject to the adjustment in**
18 **(f) of this section.** for the purposes of

19 (1) AS 43.55.011(e), the annual production tax value of the taxable

20 (A) oil and gas produced during a calendar year from leases or
21 properties in the state that include land north of 68 degrees North latitude is the
22 gross value at the point of production of the oil and gas taxable under
23 AS 43.55.011(e) and produced by the producer from those leases or properties,
24 less the producer's lease expenditures under AS 43.55.165 for the calendar year
25 applicable to the oil and gas produced by the producer from those leases or
26 properties, as adjusted under AS 43.55.170; this subparagraph does not apply
27 to gas subject to AS 43.55.011(o);

28 (B) oil and gas produced during a calendar year from leases or
29 properties in the state outside the Cook Inlet sedimentary basin, no part of
30 which is north of 68 degrees North latitude, is the gross value at the point of
31 production of the oil and gas taxable under AS 43.55.011(e) and produced by

1 the producer from those leases or properties, less the producer's lease
2 expenditures under AS 43.55.165 for the calendar year applicable to the oil and
3 gas produced by the producer from those leases or properties, as adjusted under
4 AS 43.55.170; this subparagraph does not apply to gas subject to
5 AS 43.55.011(o);

6 (C) oil produced during a calendar year from a lease or
7 property in the Cook Inlet sedimentary basin is the gross value at the point of
8 production of the oil taxable under AS 43.55.011(e) and produced by the
9 producer from that lease or property, less the producer's lease expenditures
10 under AS 43.55.165 for the calendar year applicable to the oil produced by the
11 producer from that lease or property, as adjusted under AS 43.55.170;

12 (D) gas produced during a calendar year from a lease or
13 property in the Cook Inlet sedimentary basin is the gross value at the point of
14 production of the gas taxable under AS 43.55.011(e) and produced by the
15 producer from that lease or property, less the producer's lease expenditures
16 under AS 43.55.165 for the calendar year applicable to the gas produced by the
17 producer from that lease or property, as adjusted under AS 43.55.170;

18 (E) gas produced during a calendar year from a lease or
19 property outside the Cook Inlet sedimentary basin and used in the state is the
20 gross value at the point of production of that gas taxable under
21 AS 43.55.011(e) and produced by the producer from that lease or property, less
22 the producer's lease expenditures under AS 43.55.165 for the calendar year
23 applicable to that gas produced by the producer from that lease or property, as
24 adjusted under AS 43.55.170;

25 (2) AS 43.55.011(g), the monthly production tax value of the taxable

26 (A) oil and gas produced during a month from leases or
27 properties in the state that include land north of 68 degrees North latitude is the
28 gross value at the point of production of the oil and gas taxable under
29 AS 43.55.011(e) and produced by the producer from those leases or properties,
30 less 1/12 of the producer's lease expenditures under AS 43.55.165 for the
31 calendar year applicable to the oil and gas produced by the producer from

1 those leases or properties, as adjusted under AS 43.55.170; this subparagraph
2 does not apply to gas subject to AS 43.55.011(o);

3 (B) oil and gas produced during a month from leases or
4 properties in the state outside the Cook Inlet sedimentary basin, no part of
5 which is north of 68 degrees North latitude, is the gross value at the point of
6 production of the oil and gas taxable under AS 43.55.011(e) and produced by
7 the producer from those leases or properties, less 1/12 of the producer's lease
8 expenditures under AS 43.55.165 for the calendar year applicable to the oil and
9 gas produced by the producer from those leases or properties, as adjusted under
10 AS 43.55.170; this subparagraph does not apply to gas subject to
11 AS 43.55.011(o);

12 (C) oil produced during a month from a lease or property in the
13 Cook Inlet sedimentary basin is the gross value at the point of production of
14 the oil taxable under AS 43.55.011(e) and produced by the producer from that
15 lease or property, less 1/12 of the producer's lease expenditures under
16 AS 43.55.165 for the calendar year applicable to the oil produced by the
17 producer from that lease or property, as adjusted under AS 43.55.170;

18 (D) gas produced during a month from a lease or property in
19 the Cook Inlet sedimentary basin is the gross value at the point of production
20 of the gas taxable under AS 43.55.011(e) and produced by the producer from
21 that lease or property, less 1/12 of the producer's lease expenditures under
22 AS 43.55.165 for the calendar year applicable to the gas produced by the
23 producer from that lease or property, as adjusted under AS 43.55.170;

24 (E) gas produced during a month from a lease or property
25 outside the Cook Inlet sedimentary basin and used in the state is the gross
26 value at the point of production of that gas taxable under AS 43.55.011(e) and
27 produced by the producer from that lease or property, less 1/12 of the
28 producer's lease expenditures under AS 43.55.165 for the calendar year
29 applicable to that gas produced by the producer from that lease or property, as
30 adjusted under AS 43.55.170.

31 * **Sec. 4.** AS 43.55.160 is amended by adding a new subsection to read:

1 (f) The production tax value determined under (a)(1)(A), (a)(1)(B), (a)(1)(E),
2 (a)(2)(A), (a)(2)(B), and (a)(2)(E) of this section shall be increased by the amount of
3 credit taken by a producer under AS 43.55.026 for a pool, lease, or property in an area
4 described in (a)(1)(A), (a)(1)(B), (a)(1)(E), (a)(2)(A), (a)(2)(B), and (a)(2)(E) of this
5 section.

6 * **Sec. 5.** AS 43.55.180(a) is amended to read:

7 (a) The department shall study

8 (1) the effects of the provisions of this chapter on oil and gas
9 exploration, development, and production in the state, on investment expenditures for
10 oil and gas exploration, development, and production in the state, on the entry of new
11 producers into the oil and gas industry in the state, on state revenue, and on tax
12 administration and compliance, giving particular attention to the tax rates provided
13 under AS 43.55.011, the tax credits provided under AS 43.55.023 - 43.55.026
14 [AS 43.55.023 - 43.55.025], and the deductions for and adjustments to lease
15 expenditures provided under AS 43.55.160 - 43.55.170; and

16 (2) the effects of the tax rates under AS 43.55.011(i) on state revenue
17 and on oil and gas exploration, development, and production on private land, and the
18 fairness of those tax rates for private landowners.

19 * **Sec. 6.** AS 44.99 is amended by adding new sections to read:

20 **Article 06. Oil and Gas Competitiveness Review Board.**

21 **Sec. 44.99.600. Oil and Gas Competitiveness Review Board established.** (a)

22 The Oil and Gas Competitiveness Review Board is established.

23 (b) The board shall consist of nine members as follows:

24 (1) one senator appointed by the president of the senate;

25 (2) one representative appointed by the speaker of the house of
26 representatives;

27 (3) five members of the public appointed by the governor, including
28 one member who is a petroleum engineer, one member who is a geologist, one
29 member who is an economist, and one member who is a member of an environmental
30 or conservation group;

31 (4) the commissioner of natural resources or the commissioner's

1 designee; and

2 (5) the commissioner of revenue or the commissioner's designee.

3 (c) The senator and representative appointed to the board under (b)(1) and (2)
4 of this section shall be cochairs.

5 (d) Each legislative member serves for the duration of the legislature during
6 which the member is appointed. Each public member serves for three years. An
7 individual who has served on the board may be reappointed.

8 (e) A vacancy on the board shall be filled in the manner of the original
9 appointment.

10 (f) A member of the board may be removed and replaced at the discretion of
11 the person appointing that member.

12 (g) The public members of the board serve without compensation but shall
13 receive per diem and travel expenses authorized for boards and commissions under
14 AS 39.20.180.

15 (h) The board may enter into contracts for professional services and may
16 employ staff for administrative support for the board.

17 **Sec. 44.99.610. Duties.** The duties of the board include the following:

18 (1) review historical, current, and potential levels of investment in the
19 state's oil and gas sector;

20 (2) identify factors that affect investment in oil and gas exploration,
21 development, and production in the state, including tax structure, rates, and credits;
22 royalty requirements; infrastructure; workforce availability; and regulatory
23 requirements;

24 (3) review the competitive position of the state to attract and maintain
25 investment in the oil and gas sector in the state as compared to the competitive
26 position of other regions with oil and gas resources;

27 (4) in order to facilitate the work of the board, establish procedures to
28 accept and keep confidential information that is beneficial to the work of the board,
29 including the creation of a secure data room and confidentiality agreements to be
30 signed by individuals having access to the confidential information;

31 (5) make written findings and recommendations, together with

1 suggested legislation, to the Alaska State Legislature before December 1 of each year,
2 or as soon thereafter as practicable, regarding

3 (A) changes to the state's regulatory environment that would be
4 conducive to encouraging increased investment while protecting the interests
5 of the people of the state and the environment;

6 (B) changes to the state's fiscal regime that would be conducive
7 to increased and ongoing long-term investment in and development of the
8 state's oil and gas resources; and

9 (C) alternative means for increasing the state's ability to attract
10 and maintain investment in and development of the state's oil and gas
11 resources.

12 **Sec. 44.99.620. Information to be provided to board.** (a) The commissioner
13 of natural resources, the commissioner of revenue, the commissioner of environmental
14 conservation, and other commissioners and state agencies that have responsibility for
15 and maintain information related to oil and gas investment and activity in the state
16 shall, at the request of the board, provide information required by the board to carry
17 out the duties described in AS 44.99.610.

18 (b) At the request of the board, and except for information that is confidential
19 under AS 43.05.230, a commissioner may disclose to the board information that is
20 otherwise confidential after each member of the board and each staff member for the
21 board with access to the information signs a confidentiality agreement prepared by the
22 commissioner making the disclosure. Information that is confidential under
23 AS 43.05.230 may not be disclosed to the board.

24 **Sec. 44.99.630. Definition.** In AS 44.99.600 - 44.99.630, "board" means the
25 Oil and Gas Competitiveness Review Board.

26 * **Sec. 7.** AS 44.99.600, 44.99.610, 44.99.620, and 44.99.630, added by sec. 6 of this Act,
27 are repealed June 30, 2021.

28 * **Sec. 8.** This Act takes effect immediately under AS 01.10.070(c).

Alberta Natural Gas and Conventional Oil Investment Competitiveness Study 2009





Our Approach

Vision

- **Alberta is a vibrant and attractive place to live, work, and invest, with outstanding opportunities for current and future generations.**
- **Alberta's fiscal and regulatory structure helps enable the natural gas and conventional oil sector to be competitive, successful, and sustainable, delivering maximum value for Albertans.**
- **Alberta's resource management framework reflects trusting and lasting relationships among all stakeholders.**

Building Blocks

Our building blocks for a successful project include:

- **Forming and maintaining strong lasting relationships with our stakeholders.**
- **Sharing industry and financial information with each other to inform investment competitiveness questions.**
- **Sharing questions and advising on the key question we all have for this study.**

Key Question

Is Alberta competitive for investment within the natural gas and conventional oil sector?

Project Overview

Project Goals

- Improved working relationship between Alberta Department of Energy, industry and the financial sector.
- A common understanding of Alberta's investment competitiveness within the natural gas and conventional oil sectors.
- Recommendations for consideration by the Minister of Energy and Executive Council.

Integrated Processes

- Stakeholder engagement.
- Effective dialogue – Two-way communication.
- Solid, well planned approach and timely execution.
- Strong and effective project management office.

Project Scope

- For the purposes of this investment competitiveness study, dialogue will be limited to the economic and financial aspects of investment competitiveness, including investors' perceptions.
- While tenure and regulatory issues are being addressed in separate processes, the *related* economic and financial aspects will be assessed in this study.
- We recognize that there are other stakeholders, however, the purpose of this study is to gather essential information around investment levels and competitiveness.

Our Expectations

The Investment Competitiveness Study Is:

- Looking at whether natural gas and conventional oil investment in Alberta is competitive for investment.
- Future-focused
- About validating and making recommendations on the current and expected future state of natural gas and conventional oil investment competitiveness.
- A cooperative joint approach from industry, government and the financial sector.

The Investment Competitiveness Study Is Not:

- Predetermining outcomes before discussion and debate.

Key Project Stakeholders

Project Management Committee

Government of Alberta

Oil and Gas Industry

Financial Sector

Pipelines Sector

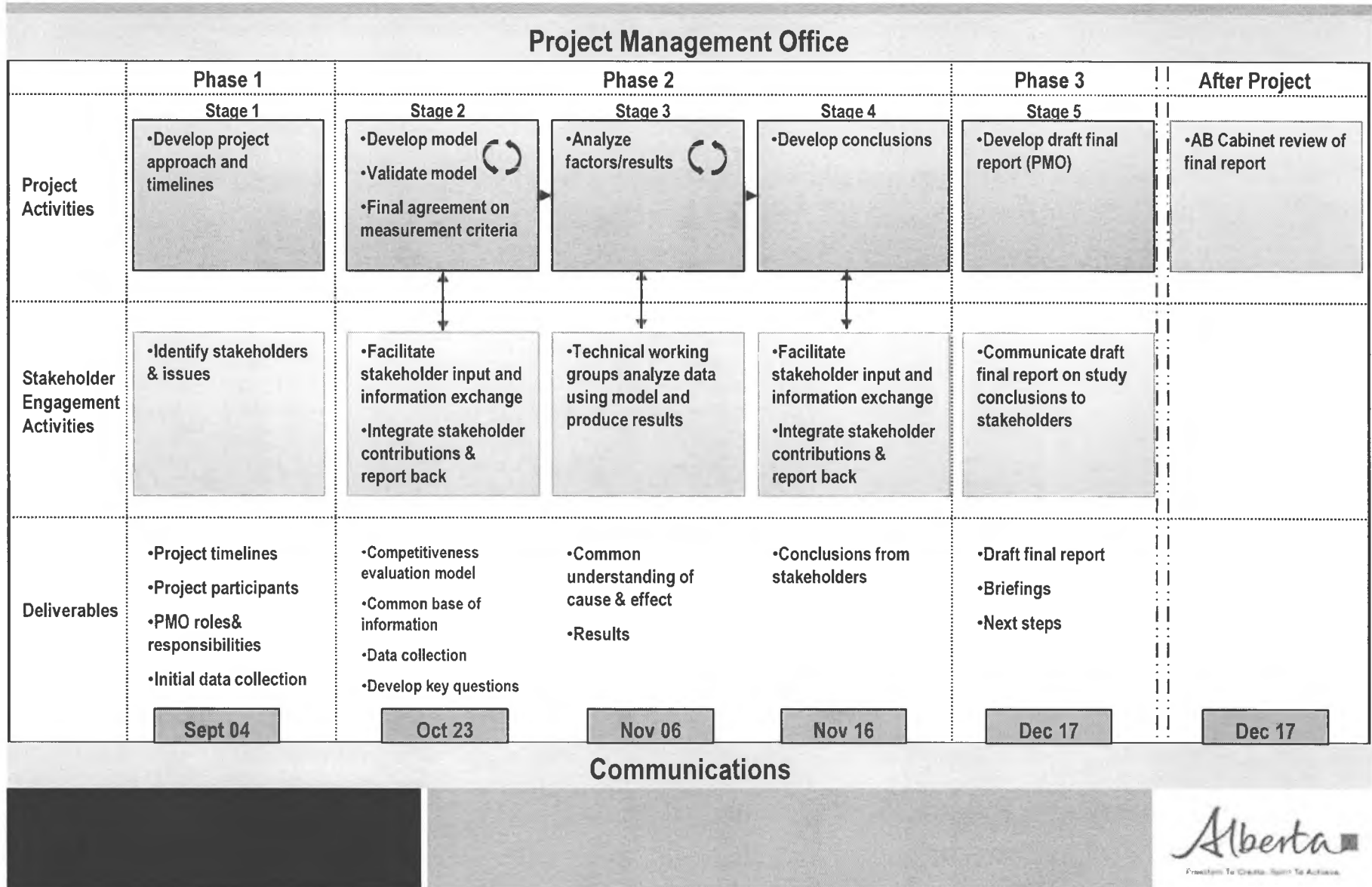
To inform, debate, validate and participate in, the investment competitiveness study, through a combination of interviews, interdisciplinary workshops and focus groups.

All stakeholder groups will be comprised of executives (CEO's) who will be interviewed, and technical/data experts who will form a large part of the working groups and inter-disciplinary team.

Decision-Making Process



Project Approach





Our Progress To-Date

Technical/Data Stream Update

Focus:

- To ensure an accurate understanding of Alberta's competitive position for natural gas and conventional oil.
- Investment competitiveness will be determined on the basis of discounted cash-flow analysis and established and accepted investment criteria.
- Participants include oil and gas companies, and related industry associations as well as the Alberta Department of Energy.
- Data acquisition kicked off July 20th.
- 27 natural gas submissions – data validation nearing completion.
- 11 Conventional oil submissions – data validation initiated; additional information required.

Technical/Data – Measures of Competitiveness

Factors of Competitiveness that are being reviewed:

- **Type Well Economics:**
 - **Rate of Return (IROR)**
 - **Cost per Unit (Barrel of Oil or Mcf of Natural Gas)**
 - **Net Present Value (NPV)**
 - **Degree of Fiscal Front End Loading**
 - **Expected Monetary Value (EMV)**
 - **Resource Owner Share**
 - **Profitability Ratio (PFR)**
 - **Price / Cost Ratio**
 - **Risked PFR**
 - **Payout Time (months)**
 - **Fiscal System Performance: Equity, Efficiency, Neutrality, and Robustness**
 - **Incremental Investment Impacts e.g., Company Taxable Position – full credit vs. stand alone, (new entrants)**

Technical/Data – Measures of Competitiveness

- **Resource Characteristics:**
 - Resource in place
 - Recoverable resources

- **Current Conditions:**
 - Recent & Existing production levels.
 - Recent & Existing activity levels: investment, producing wells, wells drilled by year.
 - Existing fiscal structures: statutory tax rates, royalty rates, other production levies.
 - Differences in cost structures (how much does the same well cost in different jurisdictions).
 - Relative returns (ROCE, ROE, ROI).

Project Management Office Team Progress

- **Project Management Office established.**
- **Roles, responsibilities, project timelines validated.**
- **Key Deputy Ministers briefed on current progress.**
- **Stakeholder engagement lists and processes completed.**
- **List of key questions to guide the study developed.**
- **Initial meetings and focus groups with industry and government groups facilitated.**
- **Detailed timeline developed for stakeholder engagement process and a calendar of events for workshops, meetings etc. with key stakeholders.**

List of Key Stakeholders

Stakeholder Category	Stakeholder Group (executive and technical experts who have the data)	Method(s) of Engagement
Government of Alberta	Executive Level (Premier, Cabinet, Ministers, Deputy Ministers, Special Committees)	Interviews/ Report/ Briefing (strategic)
	Alberta Energy	Interviews/ Focus Group/ Workshops (strategic and technical)
	Department of Finance and Enterprise	Focus Group/ Workshops (strategic)
	Treasury Board	Focus Group/ Workshops (strategic)
	Environment	Focus Group/ Workshops (strategic)
	ERCB	Focus Group/ Workshops (strategic)
Federal Government	National Energy Board	Workshops
Oil and Gas	Industry Associations (CAPP/ SEPAC)	Focus Group/ Workshops (strategic)
	Large CAPS (CEO's)	Interviews/ Workshop Rep (strategic)
	Small Producers/ Juniors and Mid-Caps	Focus Group/ Workshops (strategic)
	Working Groups (oil and gas)	Focus Group/ Workshops (strategic and technical)

List of Key Stakeholders

Stakeholder Category	Stakeholder Group (executive and technical experts who have the data)	Method(s) of Engagement
Financial Sector	Bankers: Corporate and Investment Banking	Interviews/ Workshops (strategic and technical)
	Investors: Public, Private and Institutional	Interviews/Workshops (strategic and technical)
Pipeline Sector	Trans Canada	Interviews/ Workshops
	Enbridge	



Next Steps

Next Steps

- **One-on-one executive interviews to discuss competitiveness factors, key issues, and industry success in the future.**
- **Analysis of data by the technical data team.**
- **Interdisciplinary team workshops and focus groups to develop and confirm competitiveness evaluation model, review results of the modeling and analysis, and develop conclusions and recommendations .**

Alberta Natural Gas and Conventional Oil Investment Competitiveness Study 2009

Stakeholder Briefing Document

I. Overview

Our Vision:

- 1) *Alberta is a vibrant and attractive place to live, work, and invest, with outstanding opportunities for current and future generations.*
- 2) *Alberta's fiscal and regulatory structure helps enable the natural gas and conventional oil sector to be competitive, successful, and sustainable, delivering maximum value for Albertans.*
- 3) *Alberta's resource management framework reflects trusting and lasting relationships among all stakeholders.*

A vibrant and successful natural gas and conventional oil industry is critical to Alberta and Canada's economic prosperity. The natural gas and conventional oil sector is the economic engine of Alberta, contributing to a standard of living for the province's citizens and for all Canadians that is among the highest in the world. A study by the University of Calgary shows that the oil and gas sector alone represents one-half of Alberta's economy.¹ Without the natural gas and conventional oil sector, our economic standard of living would most certainly be lower and the necessary tax burden would be higher.

North America's natural gas and conventional oil sector is at a crossroads. This means that Alberta's industry is also at a crossroads. Environmental responsibilities, rising costs due to a variety of factors including shortages of key labor skills and investment inputs ranging from steel to engineering and management, and the transformation of Alberta's largest market for natural gas from a net importer where supply is constrained to a situation where some at least speculate that the U.S. could become a net exporter, are just some of the recent developments that make it necessary to ensure that Alberta has the appropriate regulatory and fiscal environment to remain competitive for natural gas and conventional oil investment.

¹ "Energy and the Alberta Economy: Past and Future Impacts and Implications", Institute for Sustainable Energy, Environment, and Economy, December 2006

While there are most certainly competitive challenges, Alberta is fortunate to possess vast resources of natural gas (both conventional and unconventional) and huge conventional oil potential.² There is every reason to believe that Alberta will continue to be an attractive and competitive place to invest. What is critical at this juncture, however, is that a more strategic, inclusive and planned approach be taken to facilitate ongoing investment and success for Alberta. In an increasingly dynamic and competitive market economy, we cannot afford to assume that what clearly worked well in the past will remain appropriate for the future. It is critical to celebrate our past successes, and there are many, but it is prudent to plan for our future. Our past successes have not come from being passive observers. We must review our practices and investment strategies and take responsibility for our economic and financial future. This is why a competitiveness review is so important at this time.

It is Alberta Department of Energy's goal to have the fiscal and regulatory structure that helps enable Alberta's natural gas and conventional oil sector to remain vibrant and sustainable, and to deliver maximum value for Albertans. As key stakeholders, we need to work together to answer the fundamental question:

What does success look like for Alberta's natural gas and conventional oil future?

The challenges facing us demand that we work cooperatively. To do this we need a common understanding of the value of our resources, and recognition that both investors and resource owners need to benefit from the development of Alberta's natural resources. Success, therefore, has the following three components:

1. A common understanding of the value of our resources and the challenges in developing them;
2. Positive working relationships and constructive dialogue; and
3. A regulatory and fiscal framework that:
 - Facilitates the maximum production from the widest possible range of exploration and development opportunities, at the lowest possible costs, consistent with good conservation and environmental practices;
 - Recognizes that investors need to realize a reward for their investment and ingenuity, consistent with the level of risks undertaken; and

² The Alberta Research Council found that use of CO₂ enhanced recovery technology yielded additional recovery of oil in place of about 9 per cent "CO₂ Enhanced Hydrocarbon Recovery – Final Report Incremental Recovery and CO₂ Storage Potential in Alberta", March 31, 2009. Extending that finding across all light and medium oil resources in Alberta could yield additional oil recovery of up to 4.8 billion barrels.

- Recognizes that resource owners deserve to receive a competitive level of compensation for granting the right to develop and profit from their natural resources – the economic rent.

Alberta's history is characterized by a dynamic entrepreneurial spirit including the courage to adapt our key economic sectors to global realities in order to remain competitive and attractive for investors. Now is the time to once again revisit our strategy and ensure that we have the regulatory and fiscal environment to enable our natural gas and conventional oil sector to be vibrant and sustainable, and profitable for all stakeholders.

II. Rationale

To determine the investment competitiveness of Alberta's natural gas and conventional oil resources, in order to arrive at a common understanding of resource economics and re-establish positive working relationships between the Alberta Department of Energy and industry.

III. Compelling Questions

The compelling questions requiring your input are as follows:

How should we (DOE and industry) position Alberta's natural gas and conventional oil sector for ongoing success, in order to remain profitable, sustainable and competitive for the future?

What is industry's role? What is the Department of Energy's role?

IV. Guiding Principles

- Constructive dialogue among stakeholders is essential;
- Positive relationships need to be maintained and developed between industry and DOE;
- Industry deserves to be rewarded for their investment consistent with the level of risks undertaken; and
- Resource owners deserve to be compensated for granting the right to develop and profit from their natural resources.

To ensure that the positive relationships between the Department of Energy and industry are facilitated, it is necessary to keep the following touchstones in mind:



Only through strong trusting relationships, the sharing of leading-edge data and a future-focused competitive framework can the ADOE and the natural gas and conventional oil industry help to shape the foundation and future of Alberta and position Alberta for success.

V. Approach

Our approach is based on the belief that the success of this study can only be achieved through constructive interaction and dialogue. This will be done by talking directly to the key stakeholders utilizing methods such as interviews, focus groups and workshops. In addition, we will develop a reporting back process to the key stakeholders to ensure that we build positive relationships. We will communicate to the key stakeholders who participated in the process and the ideas generated in the discussions. Issue resolution and risk management strategies will also be employed to ensure that the project remains on task and that stakeholders' contributions are noted as required.

Two-levels of stakeholder engagement will be required to ensure that both an executive and technical analyst perspective will be represented in the investment competitiveness study. These two-levels of stakeholder engagement will take the form of interviews, focus groups and a cross-sector workshop made up of the government, industry, and banks. The executive group will include high-level administrators from government, natural gas and conventional oil industries and the financial sector in Alberta. This group will provide high-level strategic, economic and financial advice on Alberta's investment competitiveness and will also be a forum for continued improvement of relationships between industry and the Alberta Department of Energy. The second level of stakeholder engagement will be the technical (data) analysts who will use their technical

expertise and data knowledge to assist in informing the executive group and in examining the suggestions relating to Alberta's future investment competitiveness within the natural gas and conventional oil sector.

VI. Scope

The Alberta Department of Energy will lead a focused investment competitiveness study that will compare the investment competitiveness of Alberta's natural gas and conventional oil sector with that of appropriate competing jurisdictions, both domestic and international.

The study will take into account conventional oil, conventional gas, and unconventional gas (coal bed methane, shale gas and tight sands). Oil Sands will not be included in the scope of this work.

Recognizing that Alberta companies have opportunities nationally and internationally to invest, the study will provide details about competing jurisdiction's resources and production profiles; resource conditions, market conditions; finding, development, and operations costs; fiscal terms; and regulatory environment. Such details will include:

- Oil and Gas Reserves, Pool Sizes, Production Profiles, Drilling Success Rates and Future Potential
- Resource Conditions – Depth, Location, Reservoir Characteristics, Access Restrictions
- Market Conditions – Transportation Costs and Netback Prices
- Costs - Finding, Development, and Operations:
 - Well Drilling – Drilling, Completion, Equipment, and Tie-In
 - Regulatory
 - Land Access and Seismic
 - Lifting, Gathering, and Compression
 - Processing Costs
 - Overhead, and General and Administrative Costs
- Fiscal Terms – Royalties, Corporate Income Taxes, other Taxes (including Severance Taxes and Property Taxes) Rentals and Fees, and Bonuses
- Regulatory Environment
- Tenure process (fragmentation)
- Well licence approval process (time lines)

- Well density regulations (Pad Drilling)
- Commingling regulations
- Resource management data requirements
- Surface Access
- Municipality Restrictions and Approvals (e.g. Sour Gas, Letters of Credit)
- First Nations Process
- Other Environmental Compliance (e.g., groundwater testing, minimum distances from dwellings, GHG, Air, Land, Water, etc...)
- Impacts / overlap of Federal Regulations

The Investment Competitiveness study will involve key stakeholders including other Government Departments, the Energy Resource Conservation Board, Canadian Association of Petroleum Producers (CAPP) and the Small Explorers and Producers Association of Canada (SEPAC).

For the purposes of this investment competitiveness study:

- Dialogue will be limited to the economic and financial aspects of investment competitiveness, including investors' perceptions.
- While tenure and regulatory issues are being addressed in separate processes, the related economic and financial aspects will be assessed in this study.
- We recognize that there are other stakeholders, however, the purpose of this study is to gather essential information around investment levels and competitiveness

VII. Methodology

Under the guidance of a Project Management Office and the Executive Director of Economics and Markets for the Department of Energy, interviews, focus groups and workshops will be held with stakeholders to identify issues, confirm inputs/methodology, identify work/ information requirements, review, analyze and make recommendations for the preparation of the final deliverable.

Investment competitiveness will be determined on the basis of discounted cash-flow analysis and established and accepted investment criteria for measuring profitability, risk, and fiscal system performance. Measures of Investment Competitiveness include:

- Rate of Return (IROR)
- Net Present Value (NPV)
- Expected Monetary Value (EMV) – Risked NPV
- Profitability Ratio (PFR)
- Risked PFR
- Price / Cost Ratio
- Cost per Unit (Barrel of Oil or Mcf of Natural Gas)
- Payout time (months)
- Resource Owner Share
- Degree of Fiscal Front End Loading
- Incremental Investment Impacts; e.g., Company Taxable Position – full credit vs. stand alone, new entrants)
- Fiscal System Performance: Equity, Efficiency, Neutrality, and Robustness

Cost information to be used in the analysis will be limited to those directly related to the associated reserves. Other measurement criteria and competitiveness indicators will be incorporated as identified through the stakeholder engagement process.

VIII. Critical Success Factors:

The following factors are tantamount to a successful process whereby the project objectives and questions will be debated, deliberated and achieved.

- Industry and other project stakeholders fully understand the process, deliverables and implications of the Investment Competitiveness Study.
- Advisors are brought onto the project early in the process and provide effective support to the industry and DOE teams.
- Project risks and issues are managed proactively.
- Project is managed effectively and key milestones are met.
- Active participation and support from Ministry, Industry Associations and industry senior management in communicating value of study to peers and subordinates.
- Appropriate time is provided to government to fully respond to the report once it is completed.

IX. Key Project Stakeholders

To facilitate the process of stakeholder engagement and ensure that Government, industry and the financial sectors are equitably represented; the following key stakeholder groups have been identified.

Stakeholder Category	Stakeholder Group
Government of Alberta	Executive Level (Premier, Cabinet, Ministers, Deputy Ministers and Special Committees) Department of Energy Department of Finance & Enterprise Treasury Board Alberta Environment Energy Resources Conservation Board
Federal Government	National Energy Board
Pipelines Sector	TransCanada Enbridge
Conventional Oil and Natural Gas Producers	Industry Associations (CAPP, SEPAC) Large CAPS (CEO level) Small Producers/ Juniors and Mid-Caps Working Groups oil and natural gas
Financial Sector	Bankers: Corporate and Investment Banking Investors: Public, Private and Institutional

X. Our Promise

Our promise, based on the aforementioned identified objectives, is to collaborate with our stakeholders. This means that we will look to you for data, information, advice and innovation in formulating solutions and incorporate your advice into our recommendations to the maximum extent possible.

XI. Key Deliverables

Deliverables from the review will include:

- A comprehensive comparison of the economic value of Alberta's natural gas and conventional oil resources by area and resource type, including a comparison of Alberta's competitiveness relative to that of competing jurisdictions.
- A thorough comparison of the characteristics of Alberta's natural gas and conventional oil resources relative to competing jurisdictions, with particular focus on British Columbia, Saskatchewan and on-shore United States; e.g., Texas.
- An identification of the key attributes of oil and gas producers in Alberta going forward.
- An assessment of the regulatory framework to identify potential impacts on investment competitiveness (e.g. impacts on costs and resource recovery) and to identify key enablers and barriers for future natural gas and conventional oil development in Alberta.
- Recommendations for consideration by the Minister of Energy and Executive Council.
- Where appropriate, other recommendations for future studies and / or policy considerations.

XII. Resources Required

The resources required to inform this study, and participate in it include:

1. Financial and economic data provided by the industry including the producers, the financial sectors and other key stakeholders to support their perspectives;
2. Financial and economic data provided by the Department of Energy; and
3. Non-economic factors that influence the study such as human, technology-based and cultural factors.