

HB 247
WRITTEN
TESTIMONY
FOR HOUSE
RESOURCES,
FEBRUARY -
MARCH 2016
(FILE 5)

<TARGET><BILL>HB 247</BILL><SUBJECT>HB 247 WRITTEN
TESTIMONY FOR HOUSE RESOURCES, FEBRUARY-MARCH 2016 (FILE
5)</SUBJECT><COMM>HRES29</COMM></TARGET>

Written testimony for House Resources HB 247

Submitted by Sarah Obed
Vice President of External Affairs for Doyon, Limited

February 26, 2016

The Honorable Benjamin Nageak
Co-Chair of House Resources
Alaska State Capitol, Room 126
Juneau, Alaska 99811-1182

My name is Sarah Obed, and I am the Vice President of External Affairs for Doyon, Limited (“Doyon”). Doyon is the state chartered Alaska Native Claims Settlement Act Regional Corporation for Interior Alaska. Doyon has over 19,300 shareholders, most of whom reside within the State of Alaska. Doyon is the largest private land owner in the State, and one of our highest priorities is the continued exploration for oil and gas resources on State owned lands in the Minto Flats/Nenana Basin, as well as on Doyon-owned lands near Steven’s Village.

HB 247: An Inequitable Result for Middle Earth Exploration and Development

The structure of the Alaska oil and gas production tax is vital to the exploration and development of areas of the state sometimes referred to as “Middle Earth,” which encompasses all areas of the state south of the North Slope and outside of Cook Inlet. These areas are uniquely situated and the opportunities and challenges for economic development and oil and gas exploration and development are dramatically different than the opportunities and challenges on the North Slope and in Cook Inlet.¹

HB 247/SB 130 (“the Bill”) leaves intact certain elements of the oil and gas production tax that are very important for Middle Earth exploration and development, in recognition of the lack of commercial discoveries and infrastructure. For instance, Middle Earth production will benefit from a ceiling tax rate of 4% of the gross value at the point of production for 7 years after the start of commercial production. This ceiling was clearly intended to help “jump-start” Middle Earth production. The Bill also does not change the alternative credit for exploration under AS 43.55.025, which benefits seismic exploration and exploration drilling, and sunsets January 1, 2022 for Middle Earth projects (July 1, 2016 everywhere else). The Bill has left these provisions untouched and thus available for future use for Middle Earth projects.

However, the Bill would result in inequitable treatment of Middle Earth projects. The Bill would repeal the tax credits that have been vital to exploration and development in Middle Earth and Cook Inlet, specifically: the 20% qualified capital expenditure credit under AS 43.55.023(a) (QCE) and the 40% well lease expenditure credit under AS 43.55.023(l) (WLE). Further, this repeal would be effective July 1, 2016 — in the middle of Doyon’s planned drilling season. Doyon decided to drill a well this summer based on the reasonable expectation of receiving these credits,

¹ A summary of Middle Earth exploration and development has been included as an appendix.

and a repeal at that time would catch the project in mid-stride. The repeal of these credits, which are based upon capital expenditures, will also hamper Middle Earth development and production. In addition, assuming that production commences and continues after the 7-year sunset date of the Middle Earth tax ceiling, oil production will bear the 35% tax rate, yet Middle Earth only has a 25% loss credit under AS 43.55.023(b) (Loss Credit), compared to the North Slope where the tax rate and Loss Credit are both 35%.

It is also important to recognize that Middle Earth has not benefitted from certain tax credits and other incentives that have benefitted other areas of the state. Because Middle Earth development is still in its early stages and has not yet reached production, Middle Earth has not availed of credits that can only be applied against production tax liability and that are due to sunset. For example, Middle Earth projects will never be able to use the small producer credit due to the 2016 sunset date. Certain other incentives have never been available to Middle Earth projects, such as the \$5/bbl credit and gross value reduction on the North Slope, and the favorable tax treatment for Cook Inlet production and gas produced and used in the state.

The following table demonstrates: i) what Middle Earth would lose under the Bill; (ii) what opportunities Middle Earth is losing due to sunset dates and the early stages of exploration and development; (iii) what Middle Earth never had compared to other areas; and (iv) what would remain if the Bill passes.

Name	Statute	Description	Status
Qualified capital expenditure credit	AS 43.55.023(a)	20% credit for qualified capital costs	Would be repealed for Middle Earth and Cook Inlet by the Bill
Well lease expenditure credit	AS 43.55.023(l)	40% credit for seismic in a unit and intangible drilling and development costs	Would be repealed for Middle Earth and Cook Inlet by the Bill
Small producer credit	AS 43.55.024(c)	Up to \$12 million credit against tax liability	Sunsets in 2016 - no Middle Earth production, so never used
Middle Earth (a.k.a "new area") development credit	AS 43.55.024(a)	\$6 million credit against tax liability for Middle Earth production	Sunsets in 2016 - no Middle Earth production, so never used
Middle Earth "frontier basin" credits	AS 43.55.025(a)(6) and (7)	Lesser of 80% or \$25 million for four wells and lesser of \$7.5 million or 75 percent for four seismic projects	Sunsets July 1, 2016 - very limited use
Gross value reductions	AS 43.55.160(f), AS 43.55.160(g)	20% - 30% reduction in gross value	Not available to Middle Earth

\$5/bbl credit	AS 43.55.024(i)	\$5/bbl credit applied against tax liability for new oil production	Not available to Middle Earth
Ceiling tax rates for Cook Inlet oil and gas production	AS 43.55.011(j) and (k)	For new production, oil tax rate is 0% and gas tax is capped at \$.177/Mcf.	Not available to Middle Earth
Ceiling tax rate for gas produced and used in the state	AS 43.55.011(o)	Tax on gas used in state is capped at \$.177/Mcf	Not available to Middle Earth due to 2022 sunset - gas under Middle Earth ceiling rate is ineligible
Ceiling tax rates for Middle Earth oil and gas production	AS 43.55.011(p)	4% of gross value for first 7 years of oil and gas production	Available, but sunsets 7 years after start of production
Carried-forward annual loss credit	AS 43.55.023(b)	25% credit for expenditures that were not deductible due to insufficient revenue	Available, but at 25% rate (compared to 35% for North Slope)
Alternative credit for exploration	AS 43.55.025(a)(1)-(4)	30%-40% credit for exploration wells, 40% for seismic outside a unit	Available, but sunsets January 1, 2022

In sum, the Bill would repeal the most valuable credits for Middle Earth exploration and development and would result in inequitable taxation of Middle Earth projects due to the lack of mitigating measures available in other areas of the state. Repealing the QCE and WLE credits and leaving the Loss Credit at 25% not only impacts exploration, but also development activities that are essential for bringing fields into production; the alternative credit for exploration does not cover development activities and in any event sunsets in 2022. This would put Middle Earth on unequal footing for development and production — after 7 years of production, oil will be taxed at the 35% tax rate and the only relief would be a 25% Loss Credit. The net result unduly impacts Middle Earth projects.

There are several potential solutions that would help level the playing field for Middle Earth projects. These solutions can stand alone or be combined, and can be tailored to apply only to Middle Earth, or to Middle Earth and other areas of the state. Options include:

- (i) Do not repeal the QCE and WLE credits;
- (ii) Move the effective date of any repeal to at least January 1, 2017, if not later to allow for effective planning;
- (iii) Increase the rate for the Loss Credit to 35%;

- (iv) Extend the sunset date for the small producer credit;
- (v) Extend the sunset date for the Middle Earth (“new area”) development credit - and increase it to \$12 million per year;
- (vi) Allow Middle Earth the North Slope gross value reductions; and
- (vii) Allow Middle Earth the \$5/bbl North Slope tax credit.

We would be happy to provide draft legislation if it would be helpful.

Appendix: Middle Earth Exploration and Development

Middle Earth includes the Nenana Basin and Yukon Flats in central Alaska where Doyon holds oil and gas interests, including over 400,000 acres of state leases. Middle Earth also includes Kotzebue, Copper River, Bristol Bay, and the Aleutians.

There is no oil and gas production in Middle Earth and the prospective basins are unexplored or underexplored, with no commercial discoveries. Federal and state studies indicate that many of the basins in Middle Earth are highly prospective areas for oil and gas. Some areas are near infrastructure and could be quickly developed to bring oil and gas into production in the near future. There are great opportunities for major oil and gas discoveries that could accelerate economic development and provide jobs, local sources of gas to communities, revenues from royalties, lease rentals, and taxes, and also valuable well and seismic data.

There are several Middle Earth projects that are moving forward and production tax rates and credits impact these projects and the appetite for investment in them. Doyon has been drilling wells and shooting seismic in the Nenana Basin and Yukon Flats for the last several years, is currently building a road and pad for one additional well, is currently shooting seismic, and has moved forward with permitting and contracts for services and equipment. Doyon has advanced its projects from unknown to the demonstration of an active hydrocarbon system and has methodically de-risked the Nenana Basin prospect to a 1-in-2 chance of success for gas. These prospects are roughly 40-60 miles from the Trans-Alaska Pipeline and the likely route of a major gas line, and can provide gas to Fairbanks. These projects are already spurring economic development and providing revenue to the state and localities — Doyon pays the state over \$1.2 million in lease rentals annually.

The oil and gas production tax credits are vital to Middle Earth exploration and development, but the amount of credits associated with Middle Earth activity is miniscule compared to the total amount of credits in the state. Total rebates to Doyon for 2005-2016 are estimated to be only \$62-65 million. However, if there is an oil discovery in 2016, a simple royalty calculation for Doyon’s mean production estimate would be: 70 million barrels x \$60/bbl = \$525,000,000 in oil royalties alone. Further, that estimate is for just one of several similar traps identified in Doyon’s most recent 3-D seismic survey, which covered less than 10% of the area Doyon is actively exploring. Success with one of these traps strongly suggests that there will be success with many others. There are also significant opportunities for gas production, estimated to yield enough gas to supply Fairbanks for over 20 years. In addition, over 30 local groups will provide services for Doyon’s 2016 programs and over 150 people will be directly employed. Such opportunities are repeatable throughout the basin.

House Resources HB 247 Testimony

February 29, 2016

J. Patrick Foley
Senior Vice President, Alaska Operations



Caelus Energy Alaska: Key Facts & Information

- ❖ Privately-held E&P company focused exclusively on Alaska's NS
- ❖ \$2Bn capital investment in Alaska since 2002
- ❖ ~\$300MM 2016 capital budget
- ❖ Total Alaska workforce is equivalent to over 600 full-time positions
 - ~70 full-time Alaska employees
 - Nearly 400 contractors on the North Slope today
- ❖ Operational Highlights & Accomplishments:
 - 23MMBO gross cumulative production since 2008
 - 4MMBO gross annual production 2015
 - 2015 best safety record, 0.65 OSHA recordable injury rate
 - Longest Oooguruk well length to date: 23,209'MD (ODS N-7i)
- ❖ Direct Financial Benefits to the State:
 - \$65MM paid in royalties to the State of Alaska
 - \$60MM paid to the State of Alaska / NSB in property taxes
- ❖ Proven & Potential Reserves:
 - ~85 MMBO remaining at ODS
 - ~100 MMBO remaining at Nuna
- ❖ 350,000 undeveloped State of Alaska leases on the North Slope



North Slope Exploration & Development Program

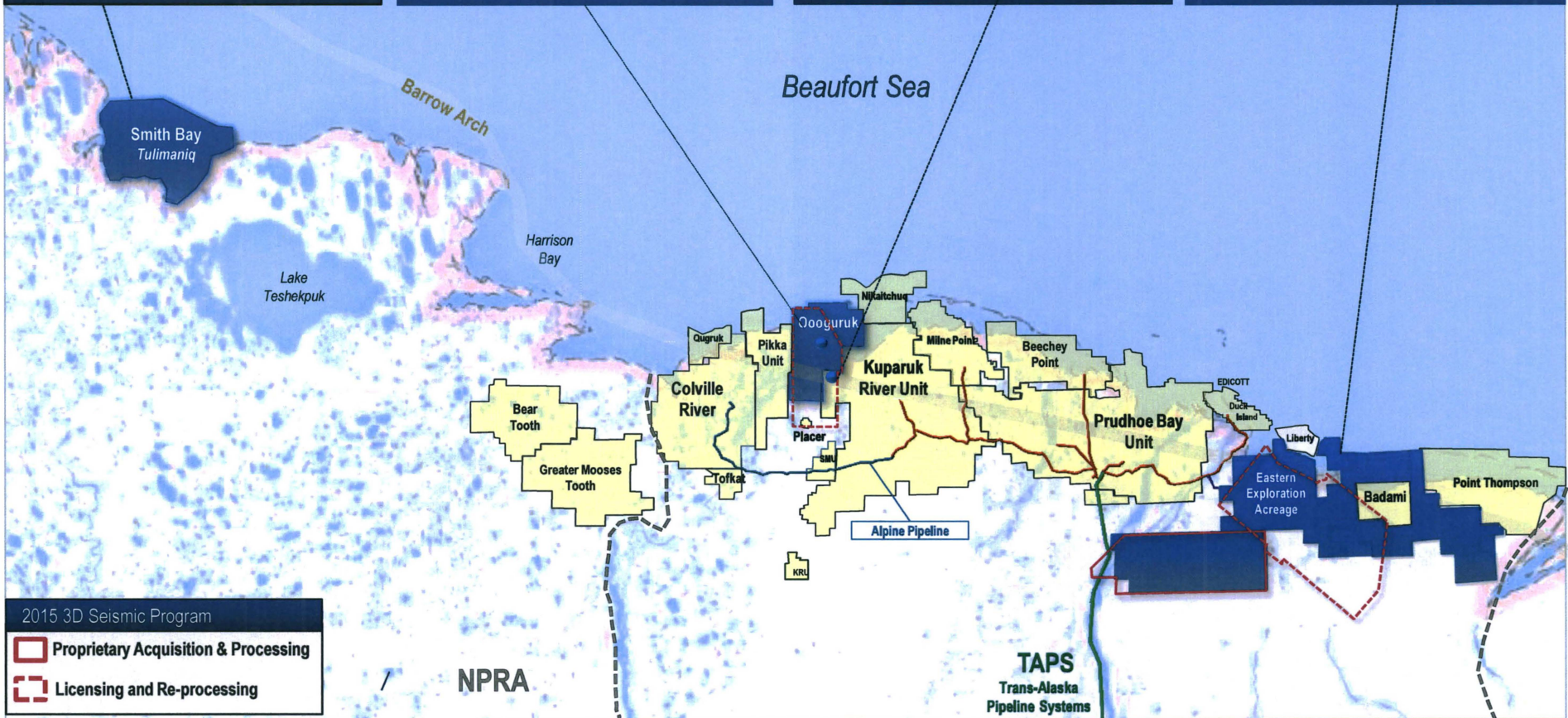


Smith Bay Exploration Tulimaniq

Oooguruk Unit (ODS / OTP)

Nuna Drill Site

Eastern ANS Exploration Acreage



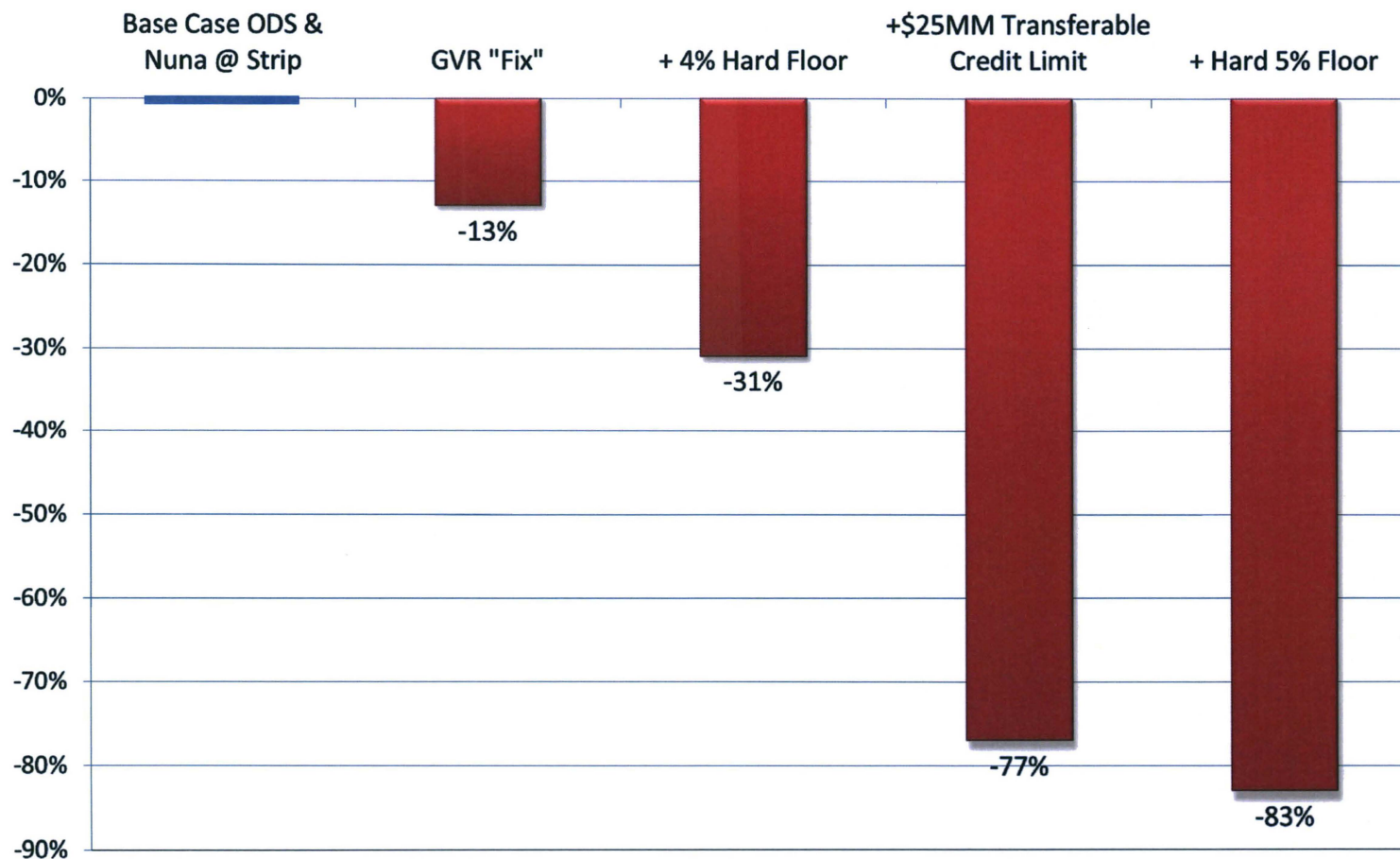
Alaska : An Attractive Investment Opportunity?

World Class Resources?	Yes
Access to Substantial Leasehold of Interest?	Yes
Access to G&G Data and Information	Yes
Expert Contractor Community?	Yes
Hospitable Regulatory Environment?	Yes
Access to Existing Infrastructure?	Yes
Favorable Logistics?	No – remote, harsh conditions, seasonal limitations
Favorable Fiscal Regime?	Yes, under SB21. No, under proposed system changes
Stable Fiscal Regime?	No, 5 significant changes in a decade
Lender & Equity Provider’s Confidence?	Historically low participation & experience Confidence in stability is low Apollo has backed Caelus Other equity providers are “watching” Bank of America committed but spooked by change ING backed out when changes began Wells Fargo disengaged when changes began

Tax Program Changes & Impacts to Caelus

Felt like the rug was pulled from under us when the change conversation began

Percentage Change in Life-Cycle Project Net Present Value



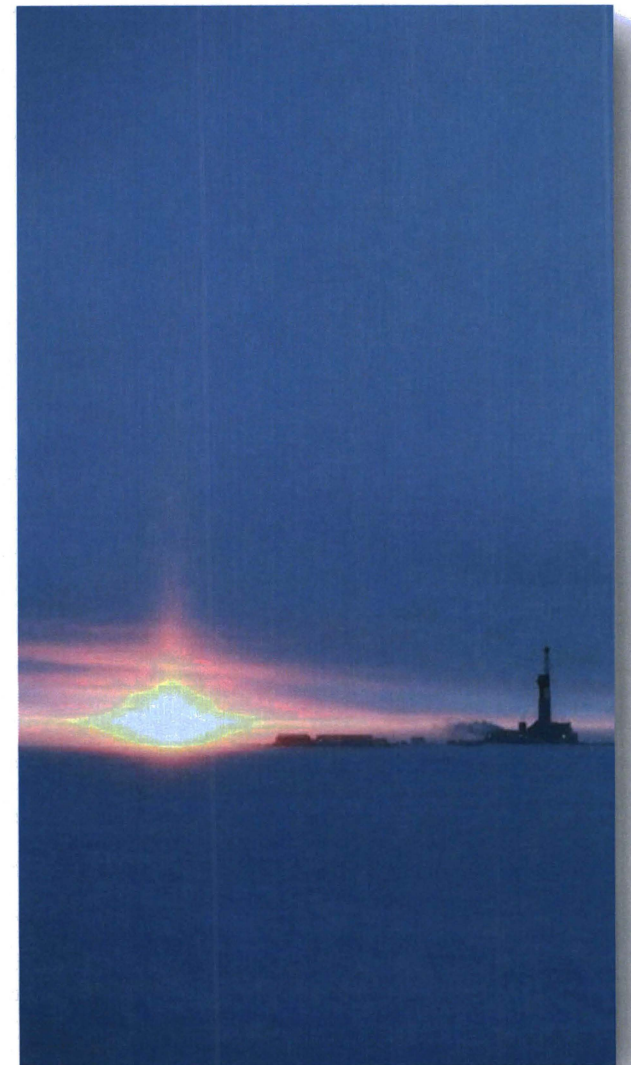
First oil Late 2018 IF Prices recover & confidence in favorable / stable fiscal terms exist

- ❖ Caelus holds 100% interest
- ❖ 100+ MMBO 2P reserves
- ❖ 20,000 to 25,000 BOPD peak production in 2021

Economically Benefits Alaska

- ❖ 300 FTE contractor construction jobs for two years
- ❖ 300 FTE contractor drilling jobs for 4 to 5 years
- ❖ \$1.75 Bn in future payments to the State of Alaska
 - ~ \$900MM in future royalty payments*
 - ~ \$500 MM in future NPSL payments*
 - > \$250 MM in future production tax payments*
 - ~ \$100 MM in future Ad Valorem taxes
- ❖ <\$250MM in future NOL cash payments from the State of Alaska

* Values are undiscounted based upon a Flat \$70/bbl Brent Price Assumption



❖ Alaska has Great Resource Potential

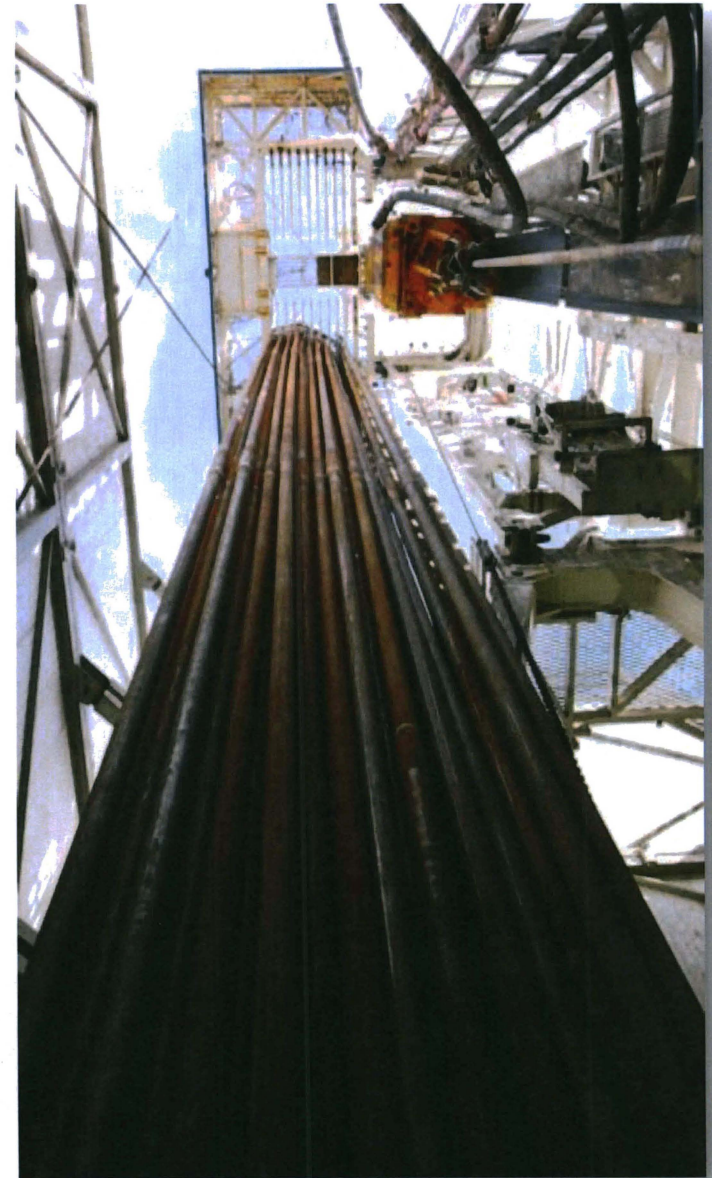
- Alaska needs more exploration & production companies to fully develop its petroleum resources

❖ HB 247 will:

- Significantly increase taxes on industry
- Delay or cancel existing and future projects
- Negatively impact production, jobs & revenue
- Discourage attracting 3rd party capital investments

❖ Recommendations

- Increasing taxes on Alaska's primary industry not the answer to budget problems
- Refundable Loss Carry Forward levels playing field, and should be maintained at current
- Allow for reasonable transition accommodations
- Grandfather projects with near-term developments



Thank you



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House Resources Committee

HB247

Scott Jepsen, VP External Affairs

Paul Rusch, VP Finance

ConocoPhillips Alaska

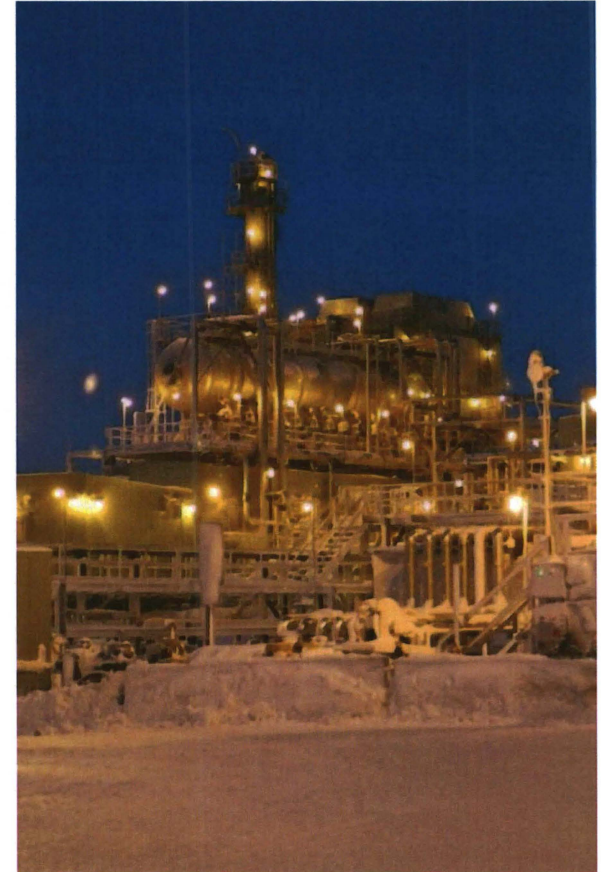
February 29, 2016

Agenda

- Look back since MAPA passed
- Economic Environment
- HB247 Assessment
- Observations

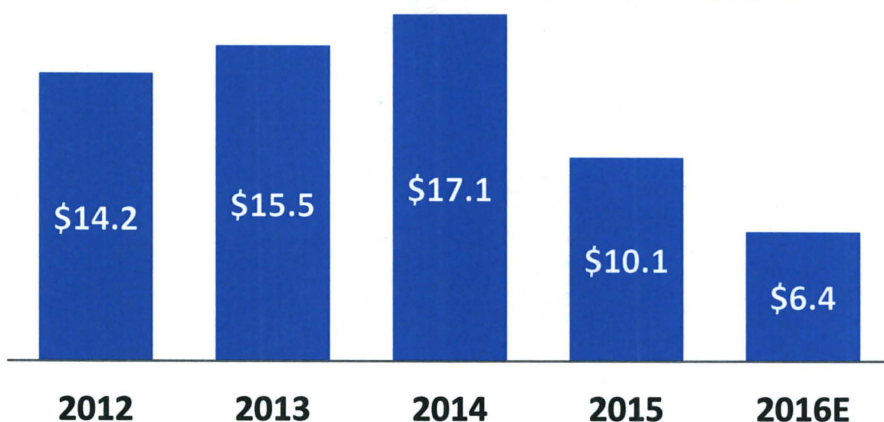
Activities Since Tax reform (MAPA) Passed

- **Added two rigs to the Kuparuk rig fleet**
 - Investment has decreased Kuparuk Unit decline
- **Two new-build rigs are on order – deliver 2016**
- **New Drill site at Kuparuk (DS 2S) – on stream October 12, 2015**
 - Estimated 8,000 BOPD peak production rate
 - About \$500 million gross cost to develop
 - 250+ construction jobs
- **Viscous oil expansion in Kuparuk (1H NEWS)**
 - About 8,000 BOPD gross, 100+ construction jobs
 - About \$450 million gross cost to develop
 - Under construction – first oil 2017
- **New development in NPRA (GMT1)**
 - Final investment decision made late 2015
 - About \$900 million gross cost to develop; peak gross rate ~30,000 BOPD
 - About 600-700 construction jobs
 - First oil 2018
- **Permitting underway for GMT2**
 - \$1+ billion gross investment
 - Will create 600-700 jobs
- **Active Exploration Program**
 - 2 wells drilled in 2014
 - Acquired GMT1 Seismic – 2015
 - Three wells planned for 2016 (NPRA)



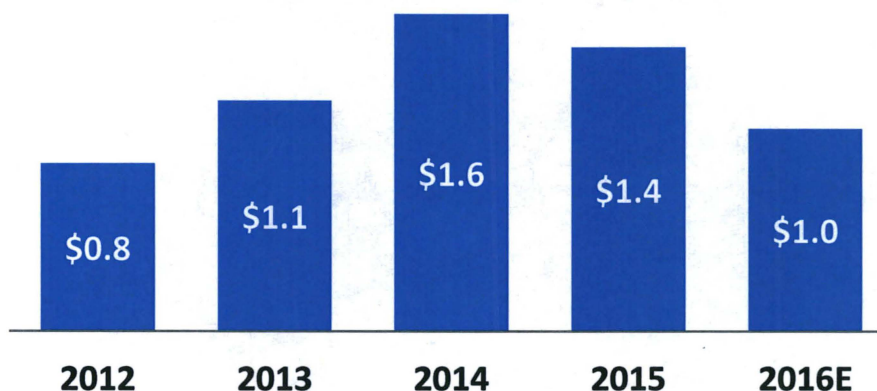
Capital Spending Trends

ConocoPhillips Capital Spend (\$B)



Total Company capital reduced 63% since 2014

ConocoPhillips Alaska Capital Spend (\$B)

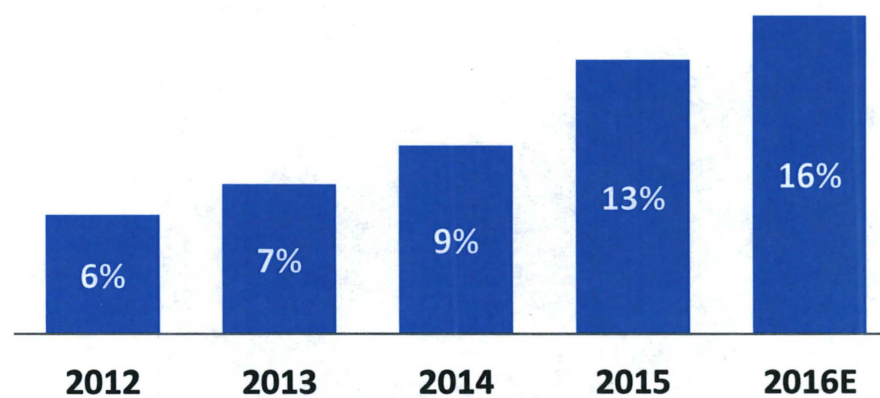


2016E Alaska capex ~ 25% higher than ACES years (~\$0.8 B/yr 2007-2012)

ANS WC Oil Prices (\$/bbl)

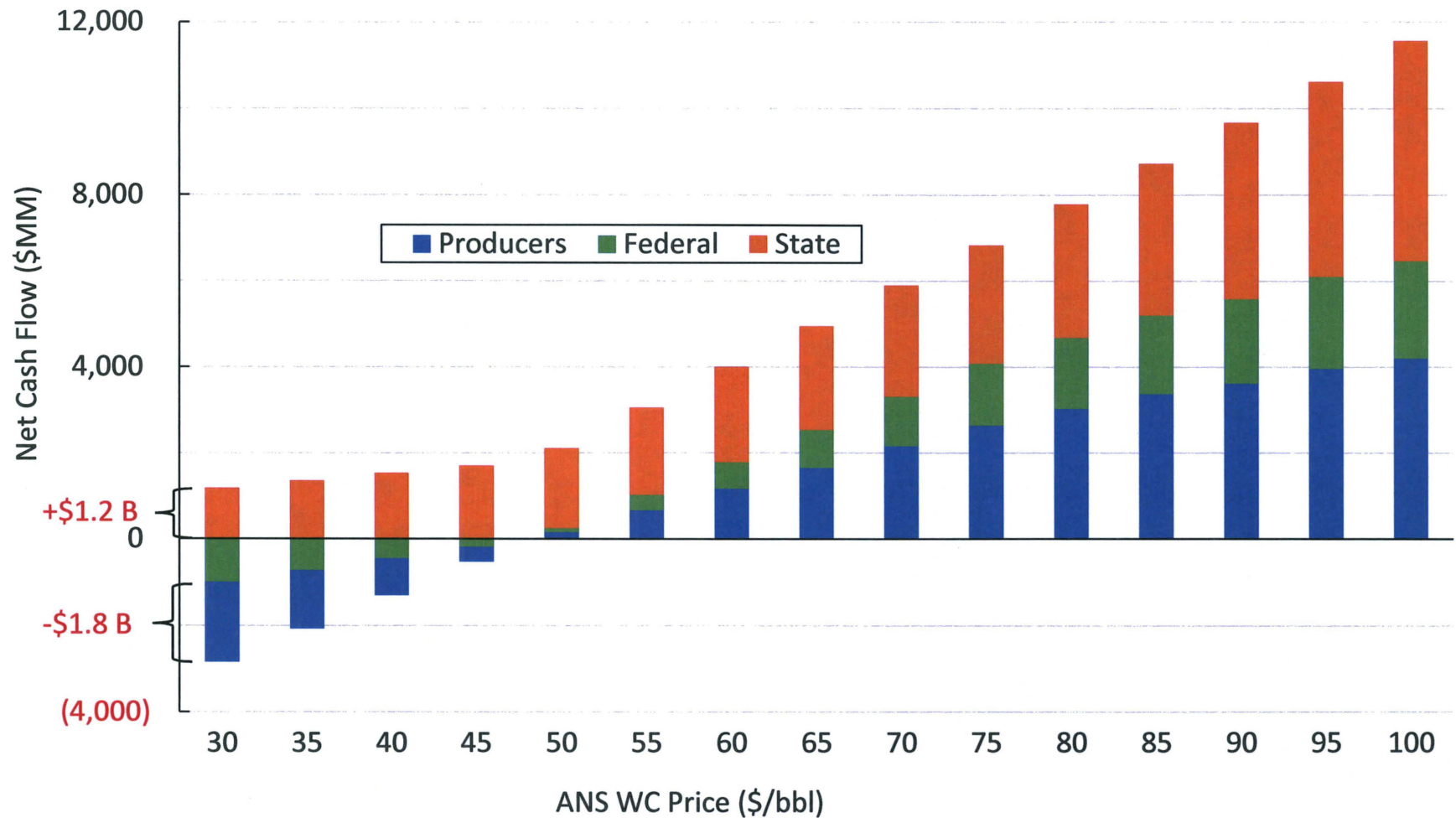


Alaska Capex as % of COP Total (%)



Alaska Producers Negative at Current Pricing

2017 FY Cash Flow - 2015 Fall RSB assumptions



State share shown excludes tax credits other than production tax credits

Key Concerns with HB 247

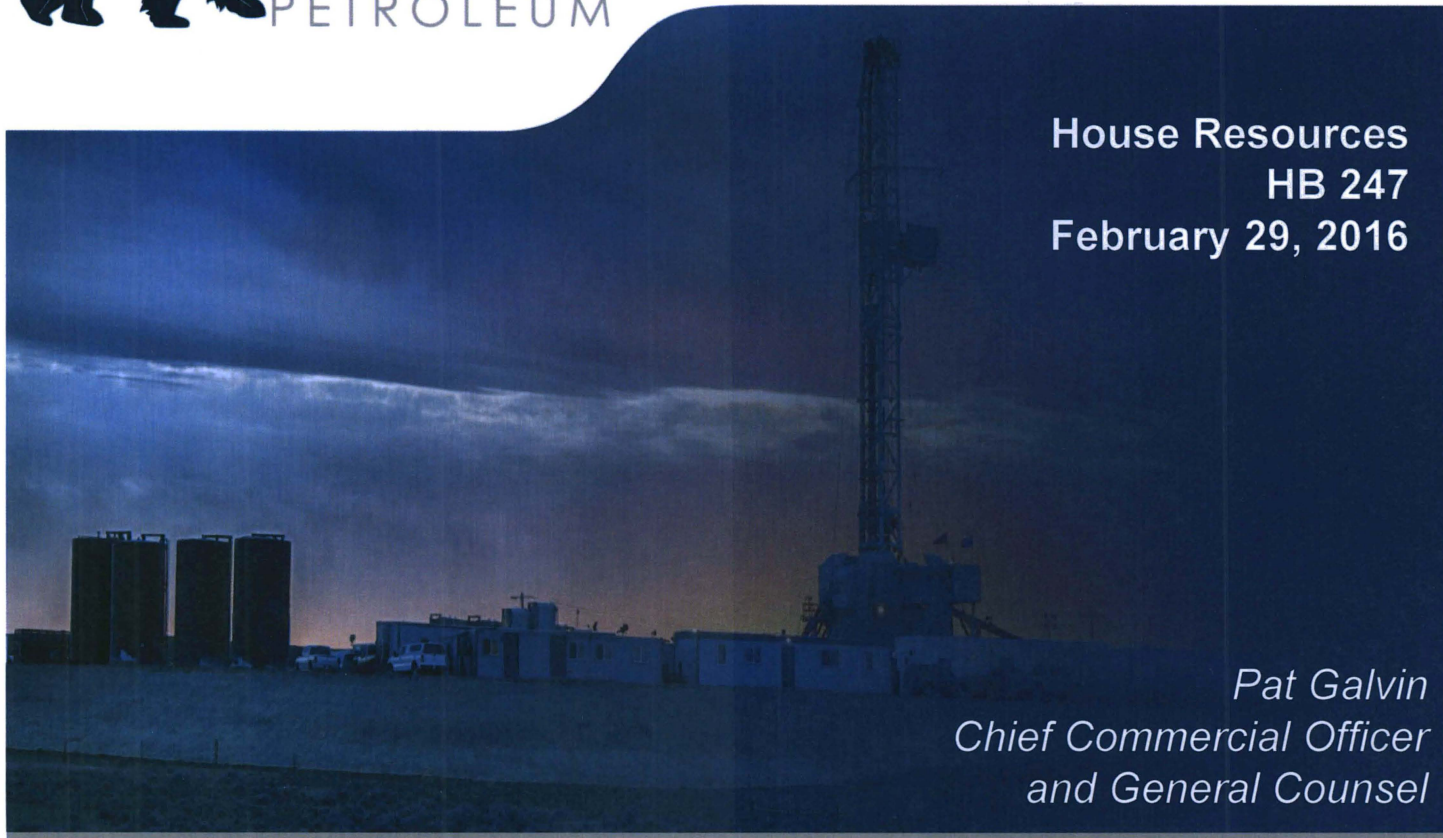
- Increase in minimum tax from 4% to 5%
 - 25% tax increase when industry in negative cash flow position
 - ConocoPhillips in excess of \$100 MM cash flow negative in 2015
- Hard minimum tax floor
 - Represents a potential tax increase when oil prices are low – moving in the wrong direction
- Various changes resulting in a tax increase
 - Increase in interest rate for under/over paid taxes
 - Monthly accounting for production tax credits vs current yearly approach
 - NOL calculations

Key Concerns with HB 247

- Increase interest rate on taxes due
 - Applies a punitive interest rate when payments are made in good faith and on-time
 - Current tax system leads to uncertainty on final tax amount due until audits have been completed
 - Pace of completing audits and appeals (6+ years) leads to excessive interest charges
- Restricting use of per barrel credits to the month earned moves towards a monthly tax - intent was full year basis
- Other Changes
 - Limiting deductions for calculating NOLs
 - Confidentiality

Observations

- Significant changes in tax law would validate concerns regarding State's ability to implement a stable oil and gas fiscal policy
 - Only 18 months since SB21 ratified by voters
 - Long-term investment requires durable, reasonable fiscal framework
- Increased tax burden will adversely impact ConocoPhillips current year and future investments
- HB-247 sends a negative message to investors



House Resources
HB 247
February 29, 2016

*Pat Galvin
Chief Commercial Officer
and General Counsel*

PRESENTATION TOPICS

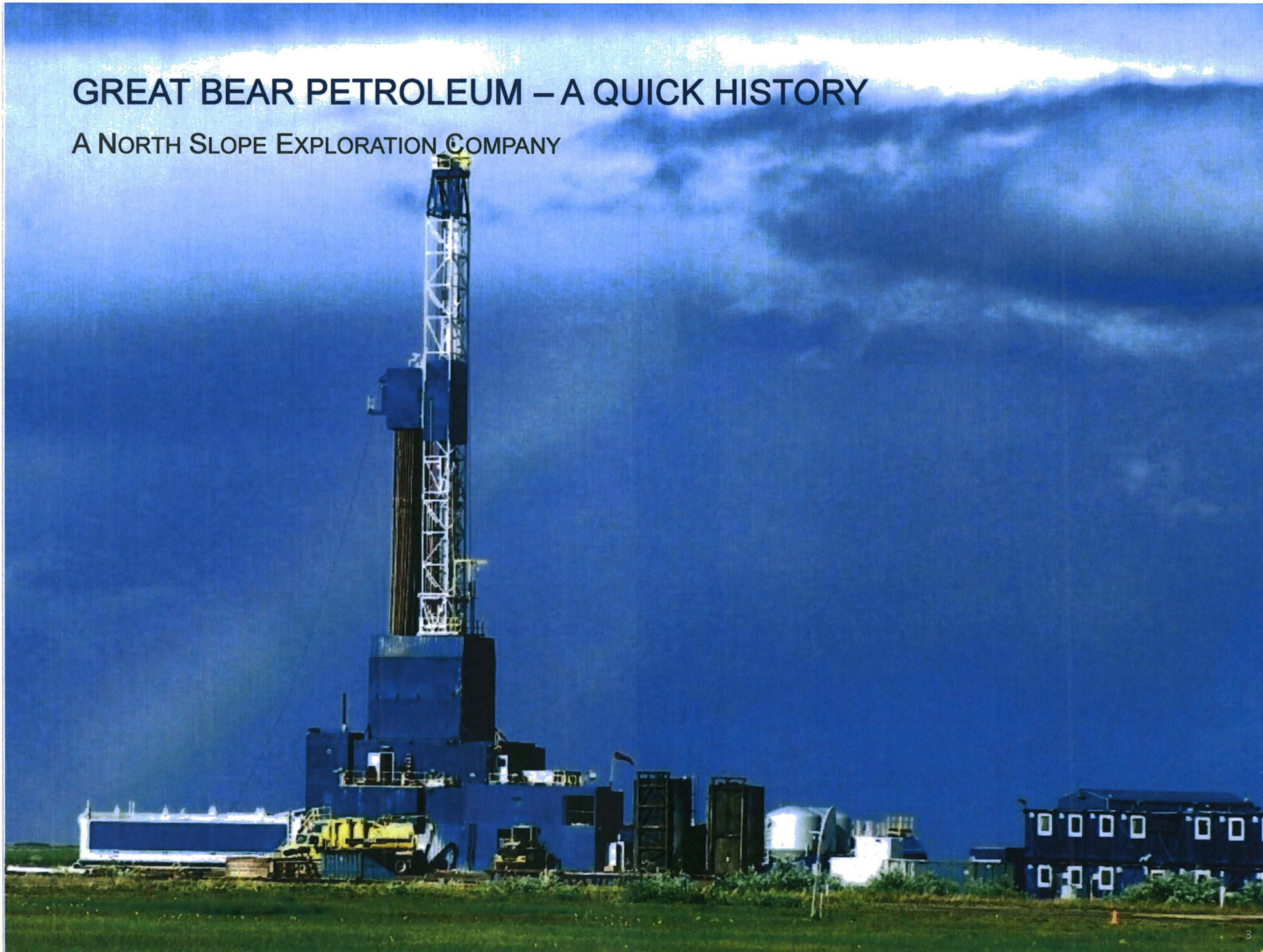
RELATING TO PRODUCTION TAX CREDITS & HB 247

- Overview of Great Bear Petroleum
- Review of Great Bear's Exploration Activities
- North Slope Challenges for Explorers
- Great Bear's Forward Looking Plans
- The Role of Tax Credits In Great Bear's Activities
- Reasons to Extend Exploration Incentive Credits for the North Slope (currently set to expire 6/30/16)



GREAT BEAR PETROLEUM – A QUICK HISTORY

A NORTH SLOPE EXPLORATION COMPANY



GREAT BEAR PETROLEUM – A QUICK HISTORY

A NORTH SLOPE EXPLORATION COMPANY

- Founded in 2010
- Focused exclusively on Alaska's North Slope
- Office and employees all in Anchorage
- Holder of 499,000 acres, Operator of 590,000 acres
- Acquired 500 square miles of 3D seismic
- Currently acquiring another 450 square miles
- Drilled 3 exploration wells



GREAT BEAR PETROLEUM – A QUICK HISTORY

FROM UNCONVENTIONAL TO CONVENTIONAL

- Original Target -> North Slope Shale Play (aka “source rock play”, aka “unconventional play”)
- Soon Faced an “Alaska Shale Play Catch-22”
 - Not economic without cost reductions
 - Costs reduction requires a critical mass of drilling activity, such as that generated by a shale play
- Re-directed focus to extensive conventional prospectivity
- Still believe a North Slope unconventional play can be economic following a conventional play build-out

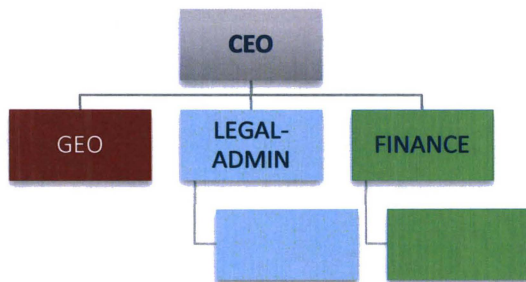


STRATEGIC EXPANSION OF CAPABILITIES

PARTICULAR FOCUS ON GEOSCIENCE & OPERATIONS

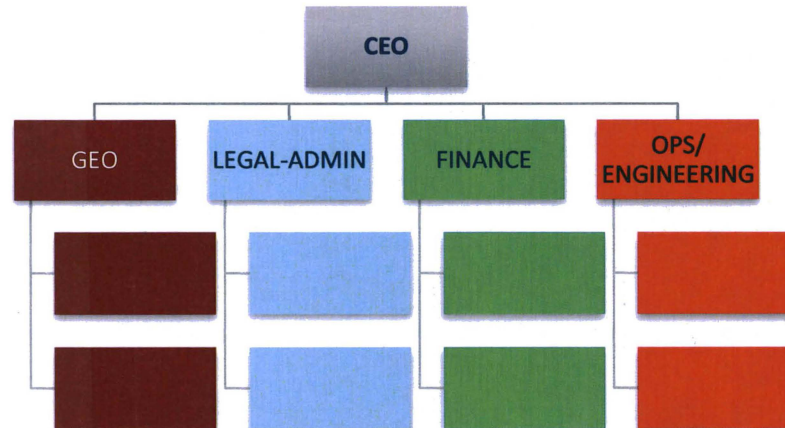
June 2015

5.5 Full Time Employees



Current

13 Full Time Employees



STRATEGIC EXPANSION OF CAPABILITIES

NEW MANAGEMENT TEAM



**Mike
Mason**
President
& CEO



Ryan Moynagh
Chief Financial
Officer



Pat Galvin
Chief Commercial
Officer & General
Counsel



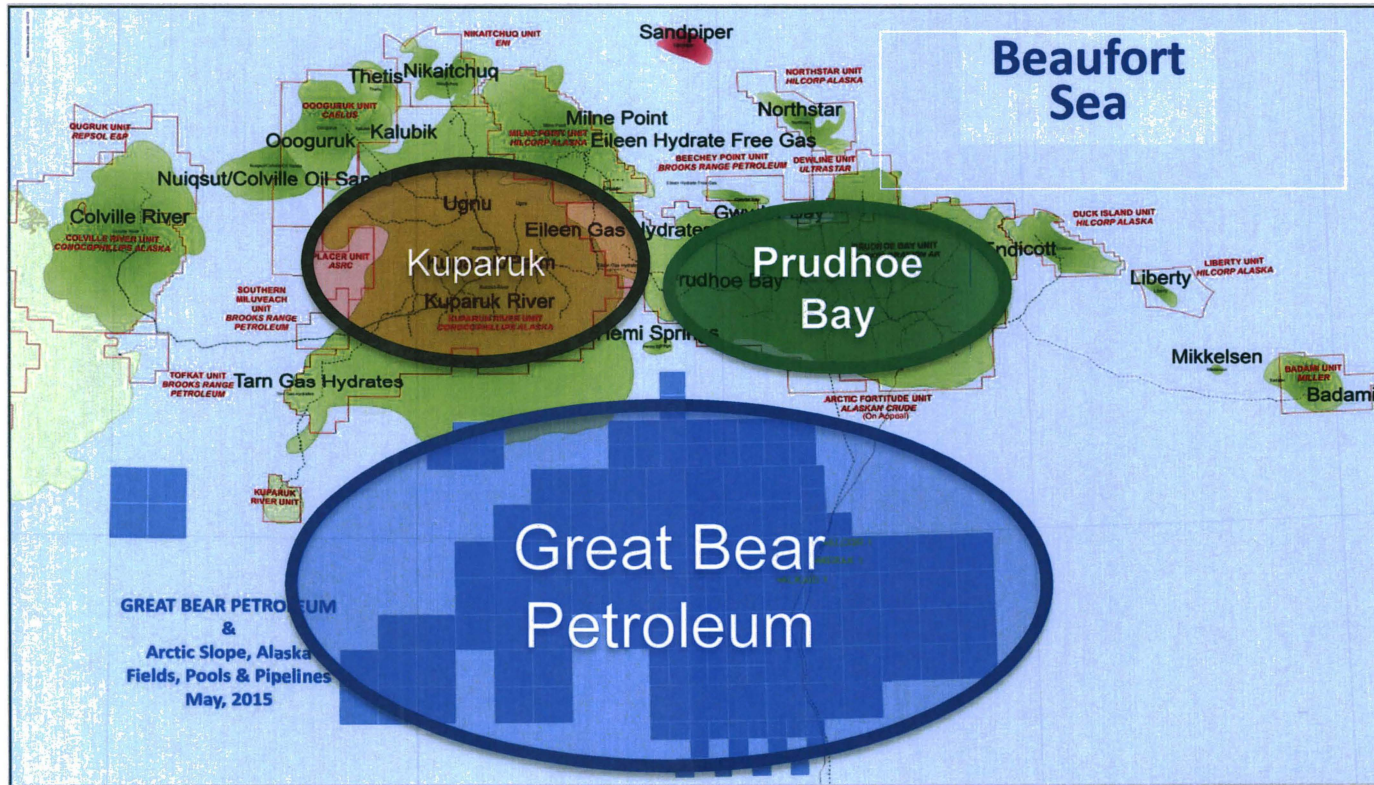
Clark Clement
Chief Operating
Officer



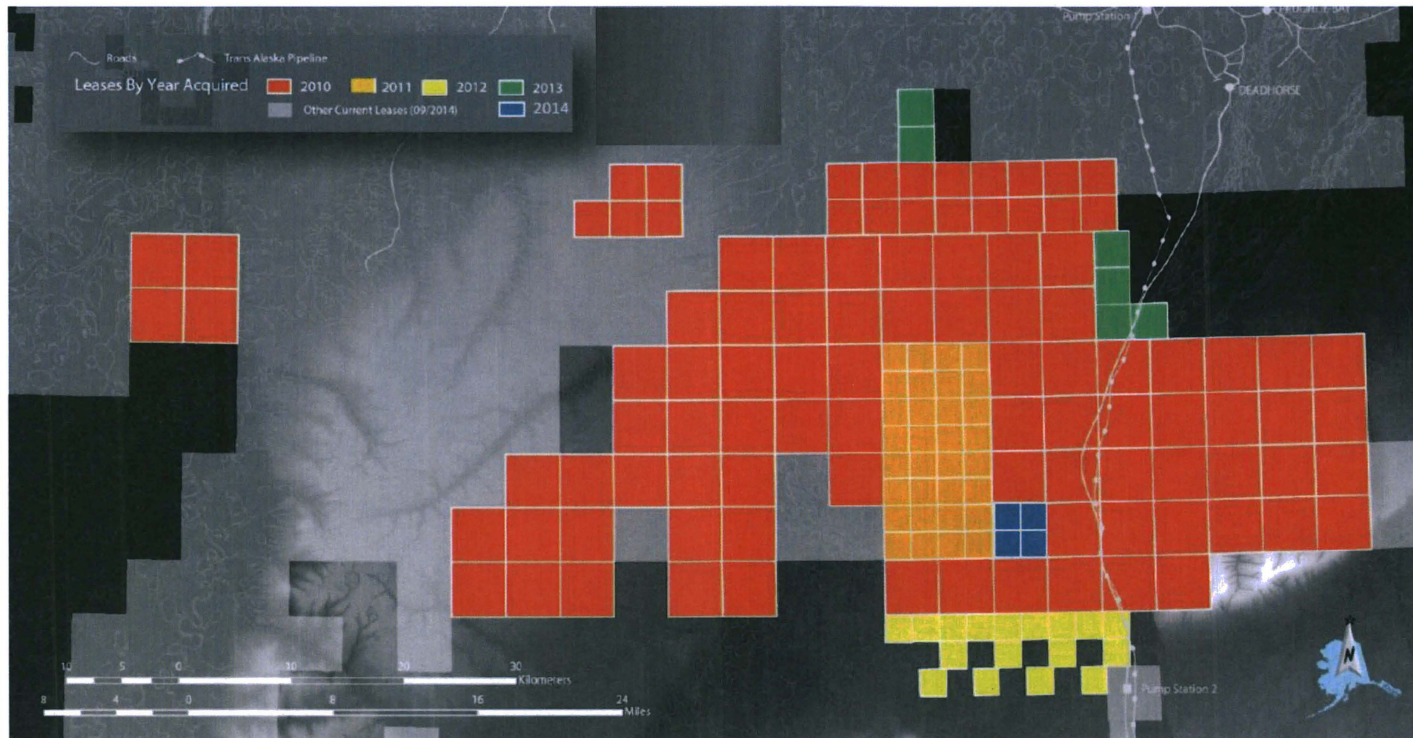
Larry Casarta
VP-Exploration



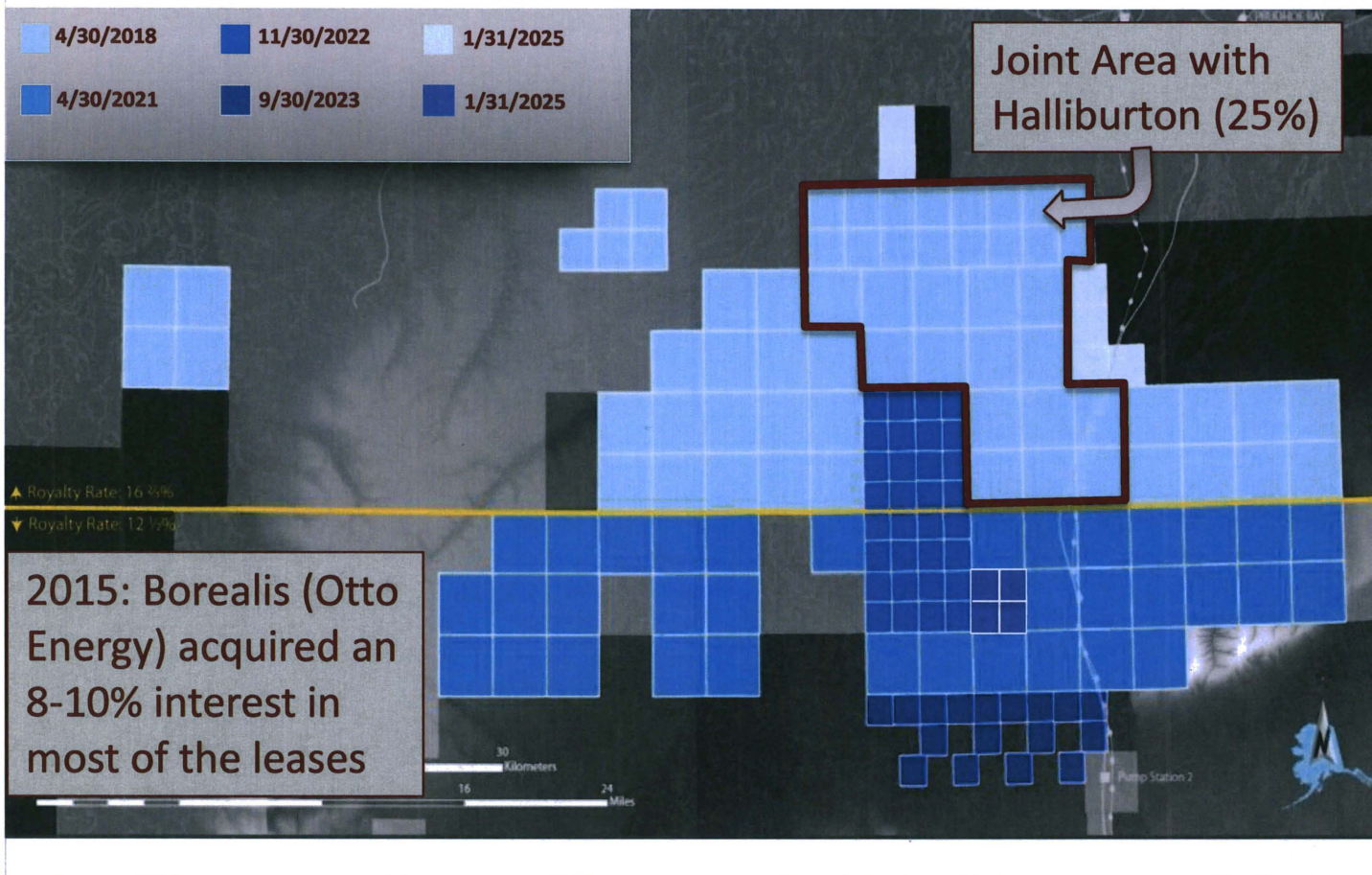
GREAT BEAR – PROJECT AREA



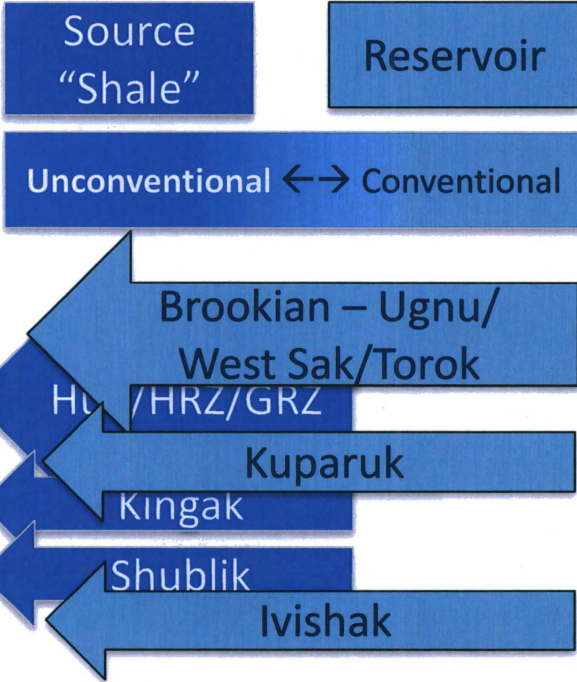
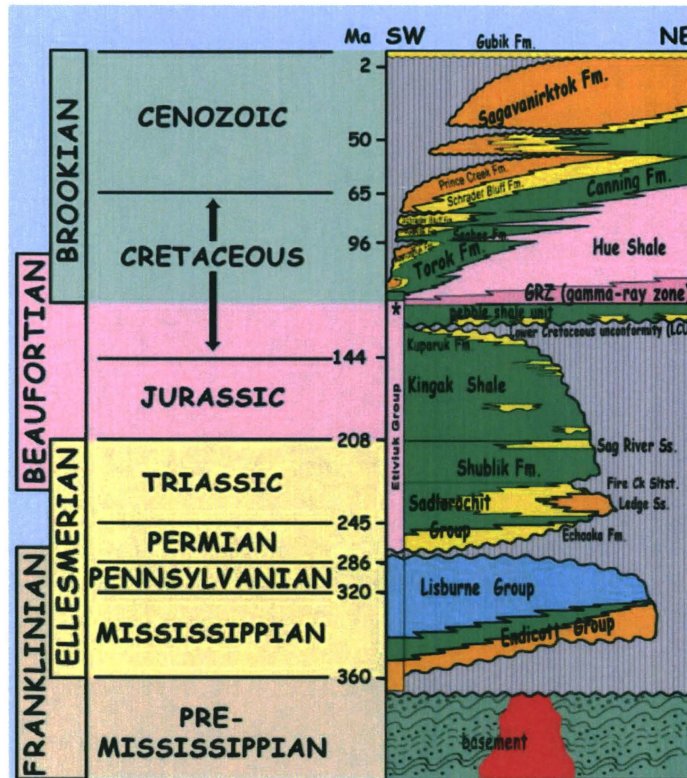
GREAT BEAR – LEASEHOLD POSITION



GREAT BEAR – LEASEHOLD POSITION

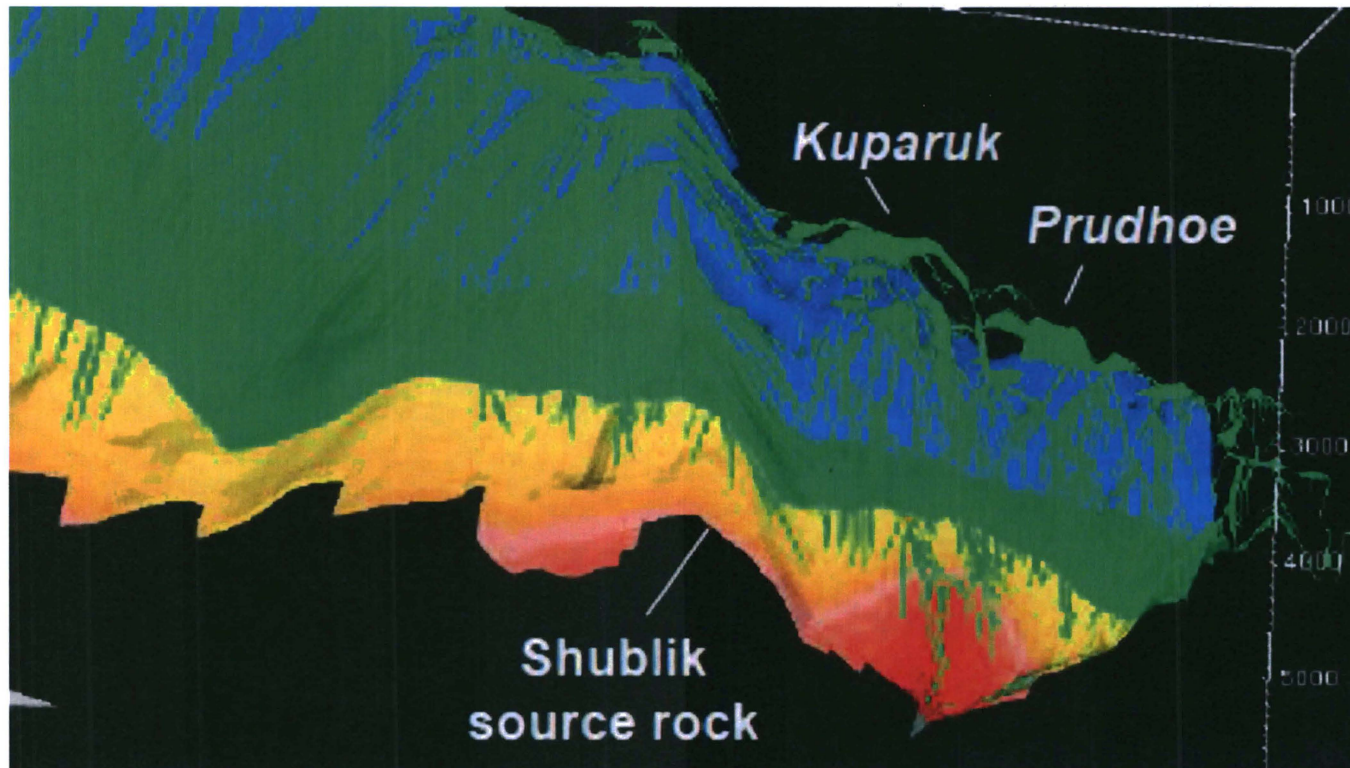


GEOLOGIC TARGETS



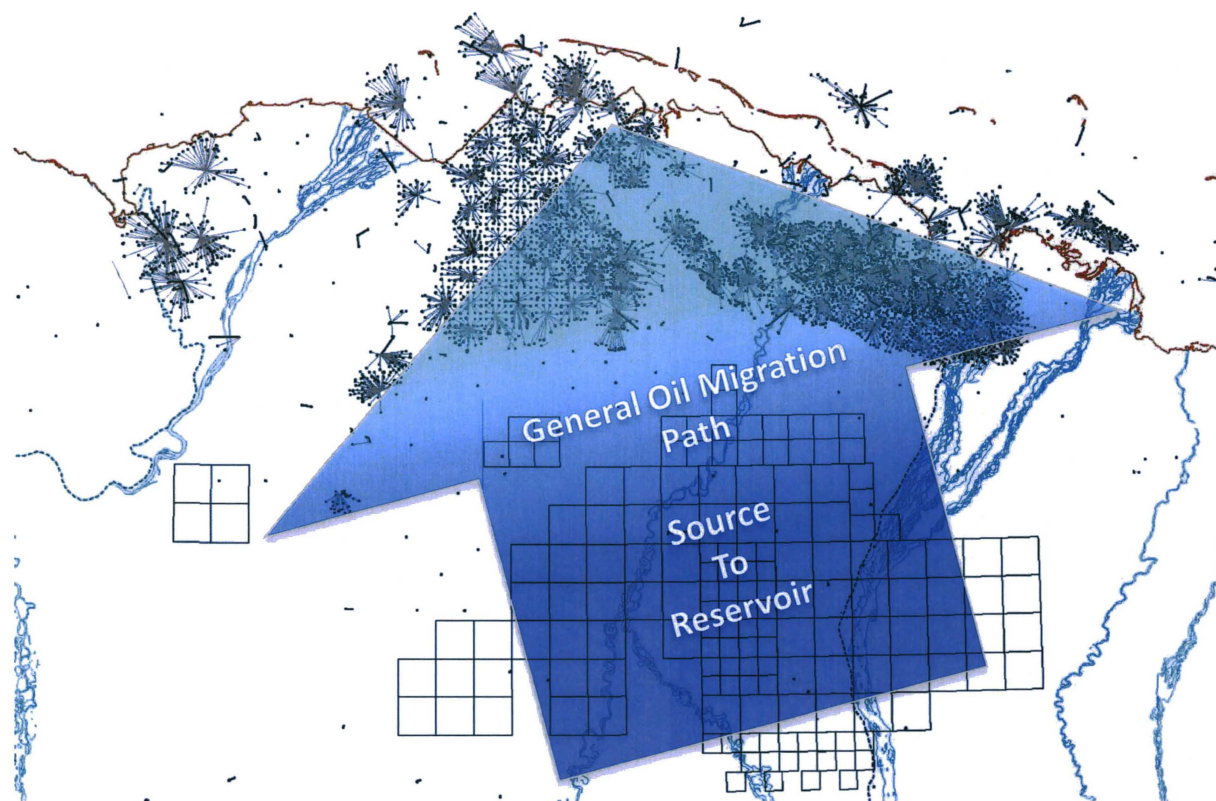
MODEL – MIGRATION OF SHUBLIK OIL

SOURCE: PETROMOD



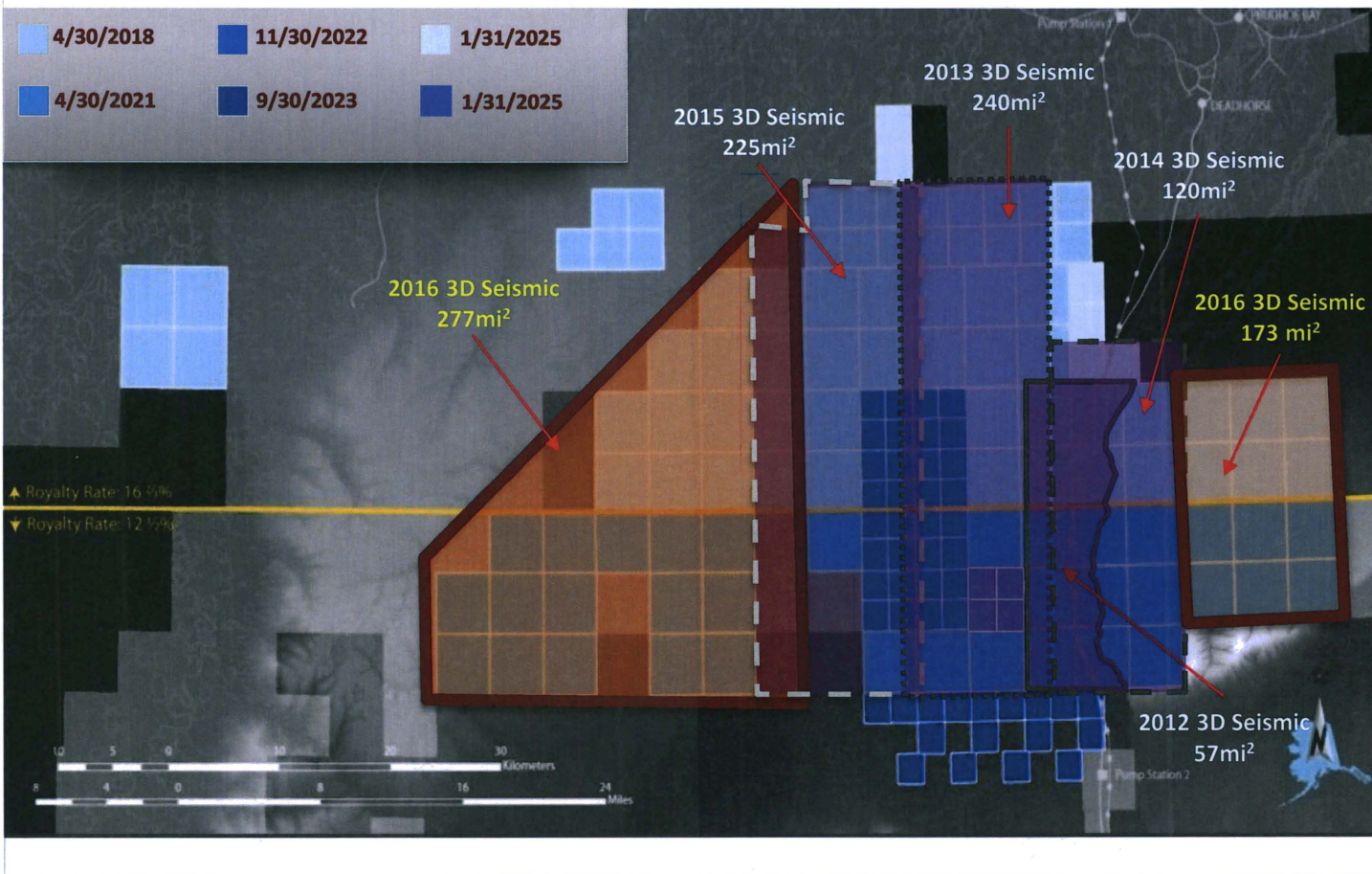
GREAT BEAR'S CONCEPT

FIND AND PRODUCE OIL FROM THE SOURCE OR FROM TRAPS ALONG THE MIGRATION ROUTE



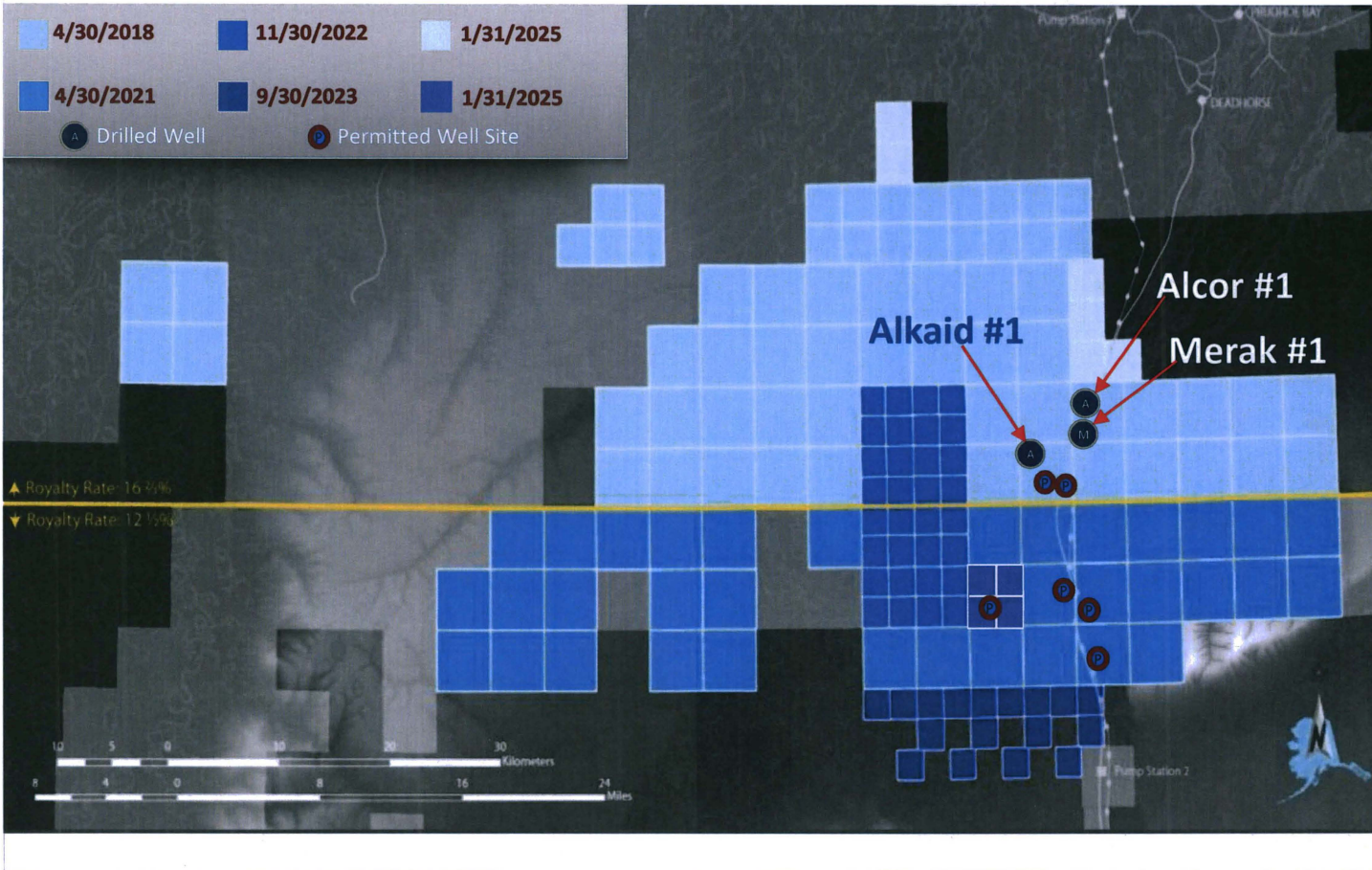
GREAT BEAR – 3D SEISMIC SURVEYS

2012 - PRESENT



GREAT BEAR – EXPLORATION WELLS

2012 - PRESENT



GREAT BEAR PROJECT SPENDING (2010 – PRESENT)

BUSTING THE MYTH THAT EXPLORATION COMPANIES DON'T HAVE "SKIN IN THE GAME"

- Total Gross Spend of Approximately \$220 Million
 - Approximately \$140M has been or will be reimbursed by State of Alaska
 - Net Operating Loss Credits (25% -> 45% -> 35%)
 - 40% Exploration Incentive Credit for Seismic
 - 30% Exploration Incentive Credit for Wells
- Great Bear Petroleum and Partners have spent approximately \$80M that will not be recovered through tax credits
 - As a result, Great Bear has been very prudent and deliberate in what activities we have conducted
- State now has extensive new data about its resources on the Great Bear leases



TAX CREDIT FINANCING

BUSTING THE MYTH THAT EXPLORATION COMPANIES ARE "FINANCED" BY TAX CREDITS

- North Slope exploration company investors pay for employee salaries, oil and gas lease rentals, office rental, and other business expenses
- Some expenditures (geologic work, permitting, etc.) qualify for tax credits (35% - 75% reimbursement rate)
- The explorer can borrow against those expected tax credits, but has to have the remaining equity funding (plus financing costs) in hand to qualify for the loans
- At no time does a North Slope explorer "make money" on tax credits



CHALLENGES UNIQUE TO NORTH SLOPE EXPLORERS

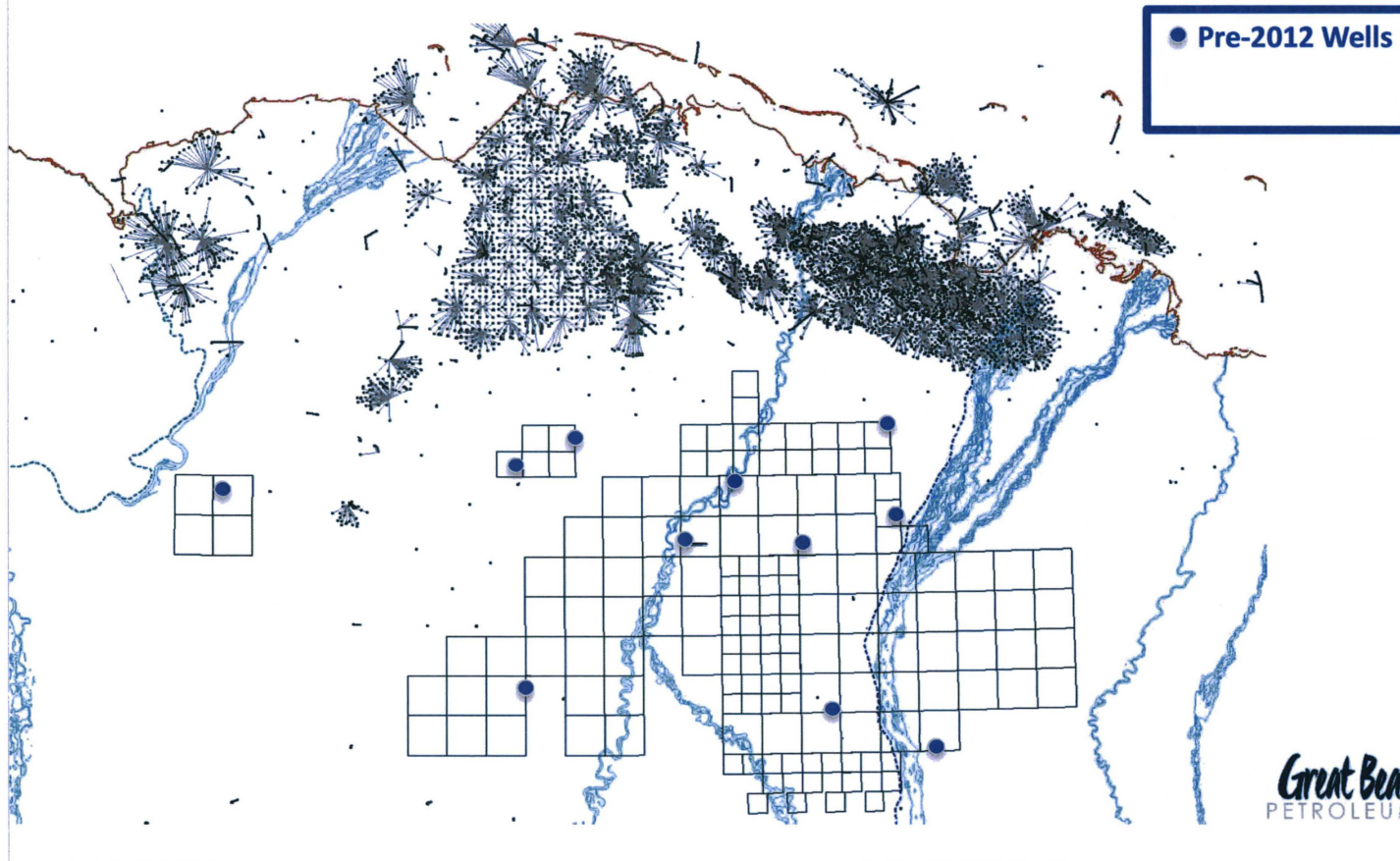
ADDING MORE RISK TO AN ALREADY RISKY INVESTMENT

- Lack of Geologic Data
- Short & Unpredictable Winter Exploration Season
- Permitting Complexity & Delays
- Alaska's High Cost Environment



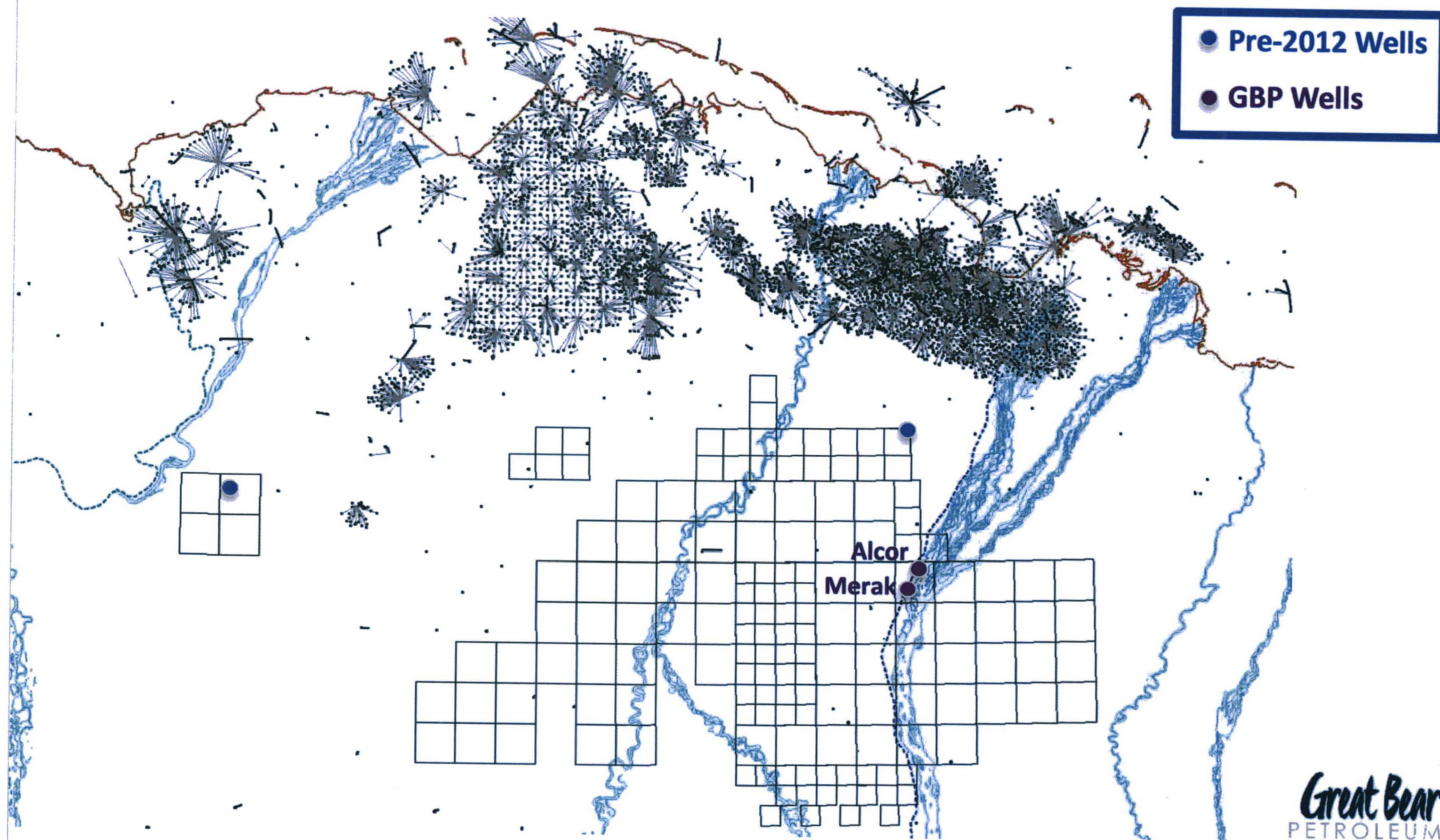
UNIQUE ANS CHALLENGES – LACK OF GEOLOGIC DATA

FEW WELLS IN GREAT BEAR ACREAGE



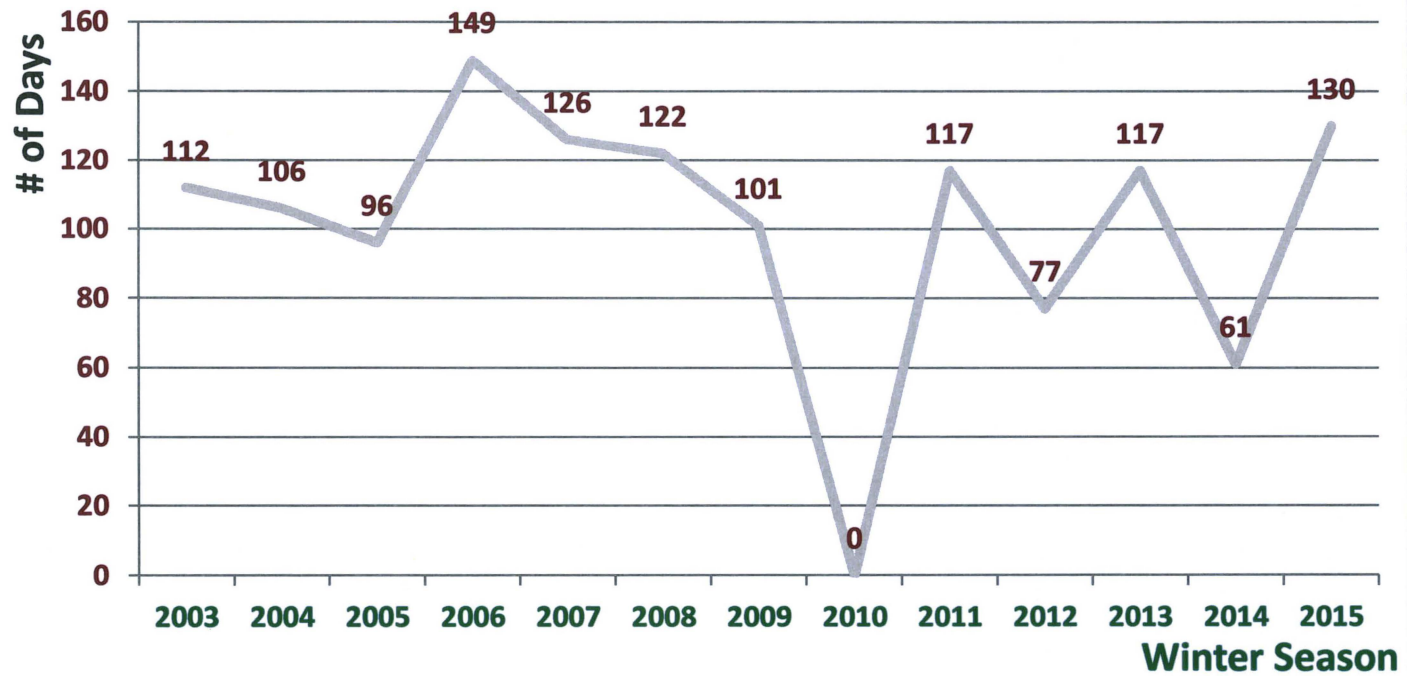
UNIQUE ANS CHALLENGES - LACK OF GEOLOGIC DATA

EVEN FEWER WELLS THAT PENETRATED THE SHUBLIK FORMATION



ANS CHALLENGES— SHORT & UNPREDICTABLE DRILLING SEASON

NUMBER OF DRILLING DAYS PER YEAR THE LOWER FOOTHILLS TUNDRA WAS OPEN TO ACTIVITY



UNIQUE ANS CHALLENGES – COMPLEX PERMITTING

DIFFICULT TO FIGURE OUT – DIFFICULT TO EXECUTE

- Multiple Jurisdictions, Separate Processes
 - Example: Winter Exploration Well Program
 - 19 Different Permits
 - 16 Different Agency Contacts

- North Slope Development Challenge
 - Wetland Permitting – What Mitigation Will Be Required?



UNIQUE ANS CHALLENGES – HIGH COSTS

CHALLENGES THE ECONOMICS OF EXPLORATION AND ANY DISCOVERY

- Causes of the High Cost Environment
 - Lack of Infrastructure
 - Lack of Competition in Service Sector
 - One-Off Exploration Drilling Programs
 - Alaska is Far From Sources of Equipment



GREAT BEAR – IMMEDIATE WORK PLAN

HOW WE WILL REALIZE THE POTENTIAL

1. Complete our seismic program
2. Complete our prospect inventory
3. Execute a multi-year, multi-well exploration program
4. Secure cost-effective services by using the multi-well commitment



GREAT BEAR – IMMEDIATE WORK PLAN

HOW PRODUCTION TAX CREDITS WILL DICTATE LIKELIHOOD OF SUCCESS

Number of Exploration Wells We Will Drill Is Directly Dependent on the Tax Credit Program

- Extension of the Exploration Incentive Credit Program
- “Stackability” of EIC and NOL Credits
- Collateralization of Tax Credit Certificates
- Interest Rate on Tax Credit Financing



HOW TAX CREDITS DICTATE EXPLORATION DRILLING VOLUME

A CONCEPTUAL EXAMPLE

\$100M

Exploration Company Has \$100M In Equity Capital to Spend on Exploration

35% Tax Credit Offered

\$140M
5-7 Wells

Company will spend approximately \$140M in exploration activities

65% Tax Credit Offered

\$260M
10-13 Wells

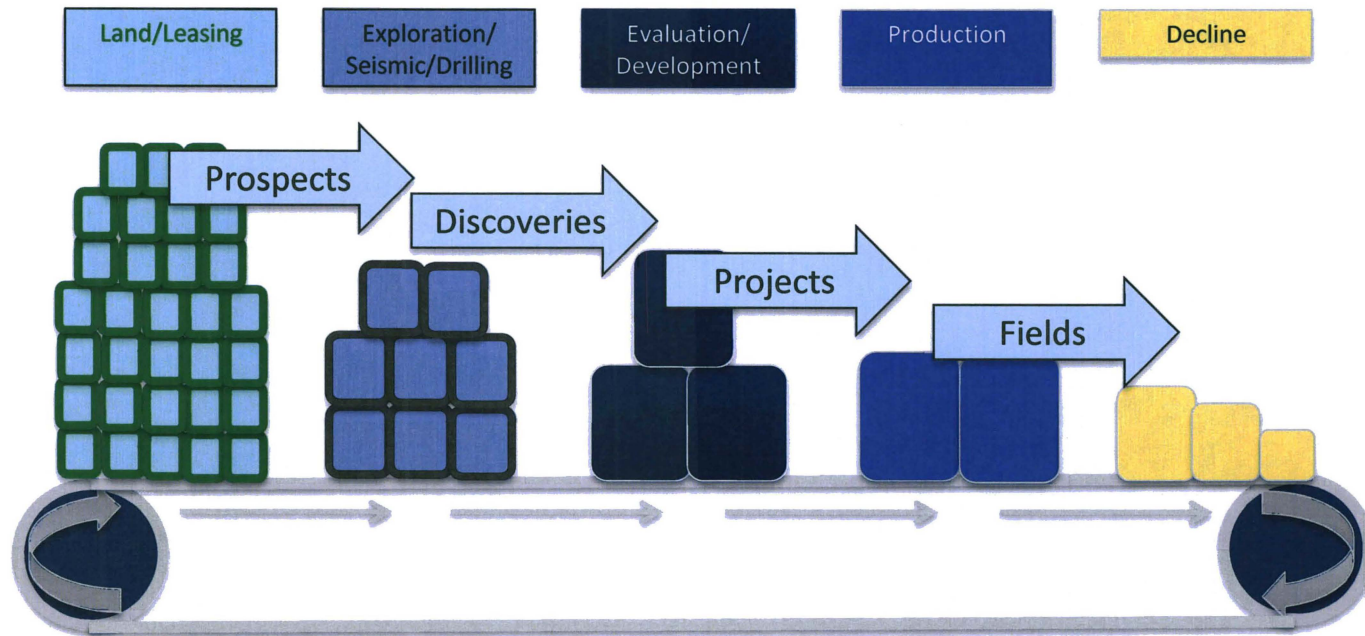
Company will spend approximately \$260M in exploration activities

By offering a higher tax credit, State generates more activity



EXPLORATION'S ROLE IN FUTURE STATE PRODUCTION

AS A RESOURCE OWNER, STATE WANTS TO KEEP EXPLORATION GOING



A Strong Exploration And Production System Must Keep Feeding the System with New Exploration



WHY THE STATE SHOULD EXTEND EXPLORATION INCENTIVE CREDITS

STATE NEEDS NORTH SLOPE EXPLORATION DRILLING

- Successful exploration will result in future production and significant cash flow to the State
- Chance of success is increased by drilling more wells
 - Multiple play types to explore
 - Constantly learning - early wells reduce risk on subsequent wells
 - Success breeds success – one discovery will increase interest in other North Slope exploration
- As resource owner across the North Slope, the State has a greater chance of success than any individual explorer
- The State's risk is reduced, and chance of success is improved, if the number of exploration wells increases
- At a minimum, the State obtains valuable data about its resources to attract future investment



TAX CREDITS – KEEP WHAT IS WORKING

INERTIA/MOMENTUM ARE STRONG FORCES IN THE OIL & GAS INDUSTRY

- Alaska Has Emphasized North Slope Exploration in State Oil and Gas Policy for the Past 15 Years
 - Areawide Leasing Program
 - Exploration Incentive Credit (EIC) Program
 - Net Operating Loss Credits
 - Tax Credit Certificate Payments
 - Collateralization of Tax Credit Certificates
- It Took A While, But That Effort is Now Showing Success
 - Diversified Group of North Slope Explorers
 - Recent Discoveries
 - New Production Coming On-Line
- Elimination/Reduction of Credits Will Be Costly
 - Likely to Slow Down or Stop Exploration
 - Lower Likelihood of New Discoveries
- Getting Momentum Back Will Take A Long Time



SUMMARY

- Great Bear is a highly active North Slope explorer
- Great Bear's investment to date has been substantial and well spent
- Great Bear's pace and volume of future exploration activity will be directly related to tax credit program
- Risk is reduced, and likelihood of success is increased by more exploration
- Reducing exploration risk of Alaska's North Slope resources is a good investment for the State of Alaska
- The Exploration Incentive Program ("025 Credits") should be extended for North Slope exploration activities



Tax Testimony to House Resource Committee

Joe Reese & Diane Colley, BP

February 29, 2016

Co-Chairs, Members of the Committee: For the record my name is Joe Reese and I am Senior Managing Tax Counsel for BP Alaska. I am very pleased to be here along with my colleague Diane Colley, who is BP's Manager of Production Tax and Royalty. BP is a member of AOGA and supports the testimony provided by AOGA earlier today. Diane and I are here to provide BP's views on tax policy and, in particular, HB 247.

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

BP is committed to maintaining a safe and compliant business in Alaska that is sustainable. Over the past two years, there has been a 70% drop in oil price. Under the current market conditions, BP's business in Alaska is spending more cash than it is bringing in, and this is not sustainable. As a result, BP is instituting a reduction in force of ~13% and is evaluating our activity level at PBU in order to adjust expenditures in response to the lower price environment. Improving our cost base is essential to maintaining our activity level at Prudhoe Bay and the long-term viability of an AK LNG Project.

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

that Alaska's production tax is not a tax on "profits"; it is more accurately described as a tax on cash flow because of the way capital expenditures are treated. Currently we are cash flow negative, yet we still pay production tax because certain of our cash costs, like our investment in the AK LNG Project and other specifically excluded costs, are not deductible for production tax purposes.

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

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

Now, we'd like to provide a few comments specifically about HB 247:

1. The Administration has proposed several changes to the Minimum Tax:
 - a. Increase -The Administration's proposal to increase the minimum tax from 4% to 5% would have a chilling effect on additional investment. This would represent a 25% tax increase to BP at a time when BP needs that cash to maintain our activity level.

b. Artificial limitation on Use of Credits Within a Tax Year – The production tax is an annual tax paid in monthly installments reflecting budgeted costs and forecasted prices that evolve during the year, with a final “true-up” to the actual figures on March 31st of the following year. This structure of monthly installments and a final true-up reflects the fact that the producers keep their financial books and records on an annual basis and do not close and balance them on a monthly or quarterly basis. The Administration proposes to limit the amount of a tax credit to the specific amount reflected for it in each monthly installment. This means any increase between that initial credit amount and any greater amount determined for it at true-up would be disallowed, but any reductions at true-up in monthly reported credits would be reflected in the total allowable amount for that credit for the year. This inconsistency is not based on good tax policy, but is simply a significant tax increase. It pretends that annual tax credits can be accurately quantified and reported on a monthly basis, even though it is not possible to have perfect full-year information when the monthly installments are filed.

2. The Administration has proposed a material increase to the interest rate for tax overpayments and underpayments: Currently, the interest is calculated at a rate 3% points above the federal funds discount rate, using simple interest. The proposal would more than double the differential from the fed funds rate, to 7% points above the federal funds discount rate, and have interest compound at the end of each calendar quarter. Such a compound rate would reward the Department

of Revenue for being slow in its audits, because 7.4% interest compounded quarterly would represent, by itself, more than 55¢ for each \$1 of additional tax claimed by the audit. This would seriously increase the unpredictability of Alaska's tax policy.

3. Net Operating Loss Tax Credit Loss: The Administration's proposal would prevent the use of net operating loss tax credits to reduce the minimum tax. In other words, companies that made important investments in the prior year, even when they may have been spending more cash than they were bringing in, would be prevented from recovering part of that investment. NOL tax credits are utilized by a broad range of companies both on the North Slope and in Cook Inlet, and changing their value would be a disincentive for future investment decisions.
4. Confidentiality: Current law allows the Department of Revenue to publicly disclose information about tax credits on an "aggregated" basis for a group of three or more taxpayers, and the Administration proposes to change this to allow disclosure of an individual taxpayer's credit information. Because of taxpayers' privileges and immunities under the U.S. and Alaska constitutions, confidentiality is the cornerstone for the Department of Revenue's legal authority to require taxpayers to report and pay their own taxes without violating those privileges and immunities. But waiving the confidentiality of taxpayer information is basically an all-or-nothing proposition for taxpayers because neither constitution specifically authorizes partial waivers, while not specifically disallowing them either. In other words, a taxpayer can't be statutorily required to waive unconditionally that

confidentiality without the risk that such a statute would itself violate the taxpayer's constitutional privileges and immunities.

Again:

- BP is committed to maintaining a safe and compliant business in Alaska that is sustainable;
- BP is committed to complying with tax laws in a responsible manner and to having open and constructive relationships with tax policy makers; and
- BP supports durable, predictable and administrable oil and gas tax policy and that is why we do not support HB 247.

Given the current economic environment, 2016 looks to be a challenging year for all of us. We at BP, and we as Alaskans, know what it means to face challenges. The best way we have found is to do so together.

Thank you.



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**HILCORP ALASKA, LLC
Testimony on House Bill 247
Resources Committee
March 1, 2016**

For the record my name is Dave Wilkins, I'm the Senior Vice President for Hilcorp Alaska. Mr. Chairman and members thank you for the opportunity to address the committee about HB 247 today. Before I get into my formal testimony, I'm fairly new to Alaska, so I'd like to tell you a little bit about myself. I'm a petroleum engineer and I've been in the industry for more than 30 years. I've had the privilege of working in many areas of the world including Russia, Texas, Oklahoma, Arkansas, Ohio, Pennsylvania, Louisiana, Wyoming and now Alaska. I'm proud to say I moved my family here last summer to lead the Hilcorp team here in Alaska because, one, it's an amazing place to raise my 3 children two, I'm excited about the opportunities available to Hilcorp in Alaska and three, I'm proud to work beside some of the most talented and dedicated people I have seen in 30+ years. I truly look forward to continuing the legacy of responsible development of Alaska's resources so that my children might also have the opportunity to both live and work in such a great state.

For those of you who aren't familiar with our company, Hilcorp is the largest privately-held oil and gas company in the United States.

Headquartered in Houston, TX, Hilcorp has operations in areas that include the Gulf Coast of Texas and Louisiana, the Northeast United States. Then in 2012 we entered into Alaska's Cook Inlet and in 2014 the North Slope.

Hilcorp was founded 1989 and has more than 1350 full-time employees.

Just over 500 of those employees support our operations here in Alaska and I'm proud to say that nearly 90% are Alaskan residents.

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

Hilcorp's assets are primarily (although not exclusively) older fields with extensive production histories, steady and predictable performance that carry incredible opportunity for getting more oil and gas out of the ground safely and responsibly while extending production life through efficiency and thousands of smaller scale projects. We hope the State sees a need to

attract more companies like Hilcorp as fields and infrastructure continue to age.

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

So, we absolutely agree with all of what the Alaska Oil & Gas Association presented on HB 247. The credits in question have resulted in more investments here in Alaska. We stand by our commitment to serve Alaskans' energy needs first.

It's no secret that Hilcorp has been a big part in reviving energy security in Southcentral Alaska. Over the past 4 years, we have invested over \$1 billion in projects and have drilled over 50 wells in the Cook Inlet Area. As a result of this investment and the positive results, we're sending more oil to be refined and used in Alaska and we're currently making gas supply commitments into the year 2023 with local utilities and continue to work to ensure a reliable energy source for Alaska's largest population hub. As you're well aware, prior to Hilcorp's entry into Alaska, there was

widespread concern that utilities would need to import natural gas to meet demand.

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

It's also no secret that Alaska's tax credit system and the Cook Inlet Recovery act were key drivers in bringing Hilcorp to Alaska in our investments to date. Since 2012, Hilcorp has spent approximately \$3.2 Billion dollars in capital and acquisition costs here in the State of Alaska. Those investments were aimed at one primary goal – increasing oil & gas production. Since 2012, we have increased overall organic (non-acquisition) production by approximately 40% in Cook Inlet. A lot of people like to ask us how we do it, and the answer is simple. First, we have a talented and

dedicated workforce here in Alaska and second, we have and continue to make significant investments; investments that were encouraged by the State's tax credit program and investment that did just what the credits were meant to do...**Increase energy supply for Alaskans.**

I would argue that our success has been meaningful to many, including the State. Increased production levels of oil and natural gas in the Cook Inlet basin has resulted in increased royalty rates, property taxes, jobs and more. One example of this is looking at our Monopod offshore platform. In January 2012, right after Hilcorp took over operations, the realized oil price was approximately \$95 per barrel. Production was approximately 600 barrels of oil per day, a marginal rate for an offshore platform that has a high operating costs. As the royalty owner, the State's take from the Monopod at that time was approximately \$90,000 per month...when oil was about \$95 a barrel. Because of this marginal rate and low profitability, the Monopod qualified for royalty relief under HB 185 passed in 2003. The royalty rate was restructured to help maintain profitability for the platform so it would not be shut-in and/or permanently abandoned. Over the past 4 years, Hilcorp has done over 150 projects on the Monopod alone, most of

which were smaller in scope, and they have increased production to a current rate of approximately 3,000 barrels of oil per day. Because of this increase, the state's royalty share is back up to the standard 12-1/2% and even with oil prices at \$35 per barrel; the state's royalty take from the Monopod has increased to approximately a half a million dollars per month. That's over a 10x increase in royalty barrels and a 5X increase in royalty dollars going to the state, despite oil prices declining more than 60%. I would offer, we need more results like this. I will also offer that the industry needs a system in place that incentivizes not jeopardizes continued investments in that type of activity. It's a really good example of the State putting good policy in place and aimed at and achieving a positive result.

I can tell you today that the credits Hilcorp EARNED were absolutely reinvested in Alaska. Our current production rates prove it. We have managed to work our way above the 50K Barrel threshold both through acquisition and A LOT of hard work. Breaking the 50K mark means we can no longer cash in the very credits that HB247 proposes to take away. But other budding companies can, and Hilcorp is a company that always welcomes competition in the market. We want to help promote a healthy

industry throughout the state. An active industry means additional service companies will be attracted to Alaska which creates competition and will help drive down costs.

A lot of the discussion surround HB247 has involved the Cook Inlet basin, primarily because of the notable increase in production and activity that the existing tax structure intended to generate was wildly successful. Our success in Cook Inlet is what fueled Hilcorp's interest in expanding to the North Slope... And we did just that in November of 2014 when we purchased 20% BP's assets on the Slope.

It's been just over a year since we arrived on the North Slope and I am so excited about the amount of opportunity up there. We have a comprehensive list of projects we can invest in...projects that will put more oil in the pipeline and support literally hundreds, if not thousands, of jobs for Alaskans.

BUT, in today's price environment and in the face of an uncertain state fiscal structure, it is difficult to determine what projects move forward and when. We have to be very thoughtful with every penny we spend. We have

to continue to work hard to build efficiencies and cut costs, while ensuring we do it safely and without causing harm to the environment. Cutting COSTS, not corners, is the only way we will survive the current downturn.

I know that we aren't the only ones faced with difficult decisions and realities during this challenging time. I also recognize the members of this committee and the legislature have much to consider about what is best for the state and our future.

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

Thank you.



Written Testimony for House Resources Committee on HB 247

March 2, 2016

Representative Benjamin Nageak
Co-Chair, House Resources
Alaska State Capitol, Room 126
Juneau, AK 99801

Dear Representative Nageak;

My name is Greta Schuerch and I am the Corporate & Public Policy Liaison at NANA Regional Corporation.

As you may recall, I testified during last year's Legislative Session on the issue of the Frontier Basin Tax Credit Program in front of both House and Senate Resource Committees. As you know, this program is extremely important to the communities in NANA region for its potential to offer economic relief to our schools, small businesses, local governments and residents who pay the highest cost of living in Alaska.

At NANA, our mission is to improve the quality of life for our more than 13,900 Iñupiat shareholders by maximizing economic growth, protecting and enhancing our lands, and promoting healthy communities with decisions, and behaviors guided by our Iñupiat Illitquisiat, our traditional value system.

While the development of the Red Dog Mine has resulted in positive economic impact in the region, our communities, families and elders struggle to make ends meet due to the outrageous cost of living and high energy costs.

Residents in Northwest Arctic communities are paying between \$6 and \$11 a gallon for gasoline and heating fuel. We believe that lower energy cost through natural gas will bring sustainable solutions to the economy of Rural Alaska.

Developing natural gas for local use would significantly reduce the cost of doing business in the Arctic, strengthen the economy, thereby strengthening local businesses, communities and families.

Some of NANA's efforts related to local gas exploration include the reprocessing of vintage 2D seismic data from the 1970s and a geological and geophysical review of existing information (including the two wells drilled in the 1970s.) NANA packaged this data for marketing purposes which led to five signed confidentiality agreements in 2014 and 2015, with one company visiting the region twice in 2014 who later deemed the basin as too high of a geological risk to fund exploration in total.

NANA will continue to work at advancing exploration in the Kotzebue Basin and to de-risk the geology through our own work and also by seeking exploration partners. In order to continue on this path the exploration incentives are critical.

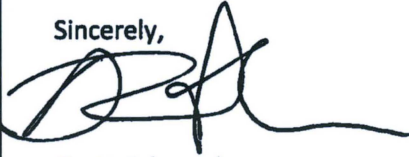
NANA is requesting that the present credits as they relate to the "Middle Earth" areas are maintained with the ability to utilize both credits stipulated under AS 43.55.023 and 025(a) (1-4). However, because we do not currently have active programs, we request the sunset date for credits stipulated under AS 43.55.025 (a) (6) & (7) be extended until 2022. An extension would recognize the logistical challenges in developing a program in Northwest Alaska.

Of the various tax credits made available by the State, the cost of Middle Earth Tax credits is minimal while the potential for positive impact toward energy independence for the rural economies is significant.

Should you have questions or require additional information, please feel free to contact me.

Taikuu, Qu yana.

Sincerely,

A handwritten signature in black ink, appearing to read 'Greta Schuerch', written over the word 'Sincerely,'.

Greta Schuerch



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Opposition of HB 247 • Before House Resources, Juneau Testimony provided by Marleanna Hall • March 2, 2016

Good evening. My name is Marleanna Hall, and I am the executive director of the Resource Development Council, commonly referred to as "RDC."

To introduce myself for those of you who do not know me, I have been with RDC for almost nine years, but this is my first opportunity to testify in front of your committee as executive director. I am originally from Nome, graduated from Chugiak High School, and went on to graduate from the University of Alaska Anchorage. My husband, son and I live in Anchorage and we hope to live and work here in Alaska for the rest of our lives.

While I don't have a presentation today, I think it is very important for me to be here to offer RDC's perspective on HB 247.

RDC is a statewide non-profit business association comprised of individuals and companies from Alaska's oil and gas, mining, forest products, fisheries and tourism industries. RDC's membership of nearly 400 corporate members and hundreds of individual members, includes the 12 land owning Alaska Native corporations, local communities, organized labor and industry-support firms across the entire economy, all of which depend on a healthy oil and gas industry. RDC's purpose is to encourage a strong, diversified private sector in Alaska and expand the state's economic base through the responsible development of our natural resources.

As you can see, RDC members are truly the life-blood of Alaska's economy. We believe the best approach to expand the economy and generate new revenues for the state is to produce more oil, attract more tourists, harvest more fish, and mine more minerals. Increasing taxes on our natural resource industries will not increase production for the Trans Alaska Pipeline System, it will not encourage the development of new mines in Alaska, it will not attract more tourists, and it will not increase investment in the fishing industry. Higher taxes in this low-priced commodity environment will likely deter investment and lead to lower state revenues and a weaker private sector over the long run.

With regard to HB 247, raising taxes on companies that are reporting record losses and are in negative cash flow is not sound fiscal policy.

According to the Energy Information Administration, oil prices today are not only the lowest we've seen in a decade, when adjusted for inflation, they are the lowest since the mid-1980s. In less than two years, oil prices have fallen 70 percent. This obviously has impacted state revenues, but also the industry, which receives 100 percent of its revenue based on the commodity price.

This is clearly not the time to raise taxes on the primary engine of Alaska's economy. The oil industry is struggling with low oil prices and tight capital markets. Companies are cutting budgets and making tough investment decisions. Increasing taxes on the industry at this time will compound a bad situation and jeopardize new investment, further damaging our private sector economy and shrinking the economic pie for everyone.

The oil industry is truly the foundation of Alaska's economy and keeping it strong is the key to sustaining the private sector, Alaskan jobs, state government, and the overall economy. A healthy and strong oil and gas industry is also vital to progressing the Alaska LNG mega project. To sustain our economy, Alaska needs to encourage new investment, jobs and production by maintaining a stable, competitive tax structure.

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When you incentivize something, you get more of it. Look at the current tax policy. It has brought new exploration, jobs, and continued investment to the state. It has stabilized North Slope production and has somewhat shielded Alaska from the massive cut backs that have occurred elsewhere. Following the enactment of the new tax law in 2013, Alaska saw \$5 billion in new investment across the state from legacy companies to new companies that have made big investments in good faith under the current regime. The sudden and dramatic drop in oil prices have slowed progress as companies struggle with low cash flows, but Alaska is in a much better position because of those investments. The tax policy has done what it was supposed to do: increase investment.

Conversely, HB 247 moves us in the wrong direction. It represents the sixth major tax change in Alaska in the last 11 years. Raising taxes when prices go up, and then raising them again when prices are down, creates instability and fails to provide investors with any fiscal certainty. HB 247 will make Alaska less competitive for global investment and risks future projects that would put more oil in TAPS, which should be our number one goal. Alaska needs a plan that grows the pie bigger for everyone.

RDC's members are not only the oil companies that will be directly impacted by HB 247, but also companies in the support industries and native corporation ventures. Alaska's Native Corporations (ANCs) are, and will continue to be economic engines in Alaska. A large part of the ANC success we see today is a result of purchases or joint ventures of oil and gas support industry companies in Alaska.

These investments not only create jobs for Alaska native shareholders, but often result in job training, education, and opportunities where few others exist. In addition to these benefits, oil production on native-owned land directly benefits the shareholders of all 12 land owning ANCs and some 220 village corporations.

Other RDC member companies, some of whom you have heard from already or will hear from today, will further explain to you the negative impacts of HB 247 on their companies. These companies, both big and small, rely on a healthy and stable oil and gas industry.

Another major concern that we have with HB 247 is that the administration has not conducted a risk analysis on the bill's impact on the oil industry. The effect of this tax proposal must be fully reviewed and unintended consequences, including potential impacts on future investment and production, considered.

Our members are not asking for a tax decrease during this time of low commodity prices like other states and countries are considering, but we do request that as the state considers changes to tax policy, it do no harm to the state's largest industry, an industry facing significant economic hardship. Otherwise, we may soon learn that the more Alaska taxes companies, the less likely a company will invest here – and the more likely its limited capital will go to jurisdictions that do encourage investment.

We are deeply concerned HB 247, if enacted, will force industry to reduce investments, which will lead to reduced oil and gas production and ultimately result in less revenue for the state, exacerbating the revenue crisis.

In closing, it is important for Alaskans to remember that the oil industry is a major revenue producer for the State of Alaska, and is the largest producer of revenue for the North Slope Borough, the City of Valdez, and the Kenai Peninsula Borough.

Co-chair Nageak, co-chair Talerico, and members of the House Resources Committee, I thank you for the opportunity to offer RDC's perspective on HB 247 today.

**Testimony by Jim Jansen
House Resources-March 2, 2016**

Chairman Nageak (Chairman Talerico) and members of the House Resources Committee, my name is Jim Jansen, Chairman of Lynden and Co-Chair of the Keep Alaska Competitive Coalition.

Thank you for the opportunity to testify this evening.

By way of introduction, Lynden is an Alaska, truck, marine and air Transportation Company who operates throughout the state with about 1,000 Alaska employees and hundreds of service partners.

The KEEP Alaska Competitive Coalition was founded as the Make Alaska Competitive Coalition in 2011 to advocate for change in Alaska's oil tax policy to encourage investment in Alaska. As you may recall, production declined by more than 200,000 barrels a day under the uncompetitive tax policy called ACES.

KEEP is a broad-based group of approximately 8,000 Alaskans, Alaska businesses, Native corporations, individuals and organized labor. We received no funding from the oil industry. After the defeat of the SB 21 referendum, we thought we could retire our coalition but here we are, facing another proposed change, which will send Alaska backward in oil tax policy.

I came to Alaska as a truck driver in 1967, and other than my military service, have lived in Alaska ever since. Alaska was my home before North Slope oil. I operated a trucking business thru the post-pipeline construction recession, and led Lynden since the recession of the 1980s.

Vicki and I have lived the dream in this great state, both from a business and personal perspective, fueled by a strong economy, driven by our resource industries. Personal and business opportunities over the past 49 years make us feel like the luckiest people on earth. I am now nearing the end of my working career, and have focused much of my energy on the future of the next generation of Alaskan's.

I am here today, because I am afraid that Alaska may revert to the economy I faced in 1967. An economy, without the North Slope would be devastating for Alaska, and Lynden. At Lynden, we would be facing massive layoffs of our outstanding Alaska employees – as our state speeded towards economic ruin. I don't scare easily, but I can tell you that I fear for our State and Lynden's people, if the legislature tries to solve Alaska's fiscal problems by imposing unreasonable taxes on our resource industries.

How we deal with our fiscal challenge will determine if we retain the Alaska we have enjoyed since the development of Prudhoe Bay. Alaska needs to adjust, to live within

our means, but we cannot do it on the backs of our resource industries. We may have to sacrifice a portion of our PFD and we may need to pay taxes, too.

To put my testimony in perspective, first let's acknowledge the situation we find ourselves in with \$30/bbl. oil prices. We all know the size of our current deficit and we all know we need to deal with it sooner rather than later.

Our state is facing a massive fiscal crisis unseen in more than 30 years. We thank the Legislators and the Governor who are willing to put Alaska's long-term economic future ahead of short-term politics. There is nothing more important for our state than to solve our budget deficit and build a sustainable economic future for our State, but, we can't do it on the backs of an ailing industry that already pays most of Alaska's bills.

I agree conceptually with much of the Governor's plan: use of the permanent fund earnings, reduction of our dividend program, reducing the operating budget, and instituting some new taxes. One part of the Governor's plan that does concern me, however, is the proposal for yet another change to our oil tax policy.

I have three main points that I wish to make this evening:

1. Increasing oil taxes and reducing credits at a time when the industry is losing money on Alaska production sends the wrong message to an industry that has responded well to our desire to see more investment and more production – even at a time when oil prices have plunged.
2. Maintaining a healthy oil/gas industry in Alaska is vital to our future if we want to keep oil flowing through the pipeline and keep alive any serious prospect for a gas line.
3. As we deal with the painful economic transition caused by low prices, we need to be mindful to protect the viability of all of our resource industries as they continue to be a major source of employment and income to Alaskans – not to mention important taxpayers.

While passage of SB 21 does a better job of protecting revenues at low oil prices than the prior tax structure, HB247 raises the tax from 4 to 5%, and eliminates loss credits, adding a new tax burden to the petroleum industry at a time it is losing approximately \$22 for each barrel of North Slope oil produced. Changing the credits is effectively a tax increase. As a state, we wanted the industry to produce oil that we know is more expensive to get out of the ground – and we promised them an incentive to do so. They did just that.

Despite these sobering times, the industry has upheld the commitment it made when the Legislature passed SB 21, the More Alaska Production Act. It pledged to increase

investment – and it did, to the tune of \$5 billion. That investment has led to more production and a leveling off of the production decline through the pipeline.

Industry is still investing substantially more in Alaska, than other regions because SB21 encourages investment. Compare Alaska to North Dakota, Texas, Canada – and most other oil provinces, and we can be extremely thankful we are living and working in Alaska today.

An increased tax on the petroleum industry today, would send a terrible message, namely, that Alaska is a high-risk tax environment and that we are an unreliable partner who does not live up to its commitments. A natural response from the industry would be to curtail their investments here and move them to a more stable and profitable oil province. We would have made it very easy for them to cease investment here.

What do you think would happen today, if Lynden told an oil company today, that we will be raising your freight rates by 25 percent? Obviously, they would shift their business to our competitors. Alaska, like Lynden, competes for investment, and this is the wrong time to increase rates.

HB247 would mark the sixth major tax change in 11 years. Attracting investment requires a fair and stable tax structure. Tax credit policy should not be a whip-saw for filling the budget deficit; it should be a thoughtful approach to a stable and growing economy.

Our oil production peaked at over 2 million barrels per day and is now approximately 500,000 per day. To keep a minimum flow in the pipeline and to obtain the value of what oil remains in our state, we need the industry to continue drilling, continue investing, and to have enough faith in us as predictable and reliable partners to invest \$50 to \$60 billion in a gas line. Continually changing our tax structure makes us predictable in the wrong sense.

The oil and gas industry, like the mining and fishing industries, provides a major source of good-paying jobs in our economy and hopefully will continue to do so well into the future. The tough choices that we have to make to reduce our deficit need to be done in a way that minimizes the shock to our economy in the next several years and are mindful of the economic base that we need for our future.

We are fortunate to have almost \$60 billion in savings to help us with the transition towards an investment-based budget. Let's start using the earnings of those savings as suggested by the Governor, Senator McGuire, Representative Millett and Representative Hawker, along with a reduced budget and carefully considered taxes and user fees to close the gap.

We all know that taxes on our resource industries are politically easier than taxes on our residents. But our resource industries are the last place we should look for quick tax revenue. They are the backbone of our economy, and in the case of oil and gas, they are swimming in an ocean of red ink. Raising taxes on the resource industries are the surest way to drive away investment, which is the only way to grow the economy.

Fortunately we have the financial resources to not only survive – but prosper. What we need now is the courage to responsibly continue to drive down the cost of state government and utilize the permanent fund as intended, to fund state services. We will need to pay taxes ourselves; however, the last place we should look for new revenue is to unfairly tax the very industries that drive our economic future. If we push them away, our economic future will be hopeless.

This is a time for Alaskans to support responsible fiscal policy.

Thank you.

Amidst Low Prices, North Dakota Scrambles To Change Oil Tax Rate

By: **EMILY GUERIN** | April 30, 2015

Distributed by
Representative Kurt Olson



(<http://1m5rjm4bgenp2600za1100pvl3h.wpengine.netdna-cdn.com/files/2015/04/pumpjacks-cropped.jpg>)

Flickr user Geof Wilson

Pumpjacks outside Tioga, North Dakota.

The oil and gas industry pays a ton of money in severance taxes to energy producing states like Colorado, Wyoming and especially North Dakota. When oil prices were high, North Dakota took in about \$10.5 million a day. But as prices have fallen, so has revenue. In the midst of this, North Dakota lawmakers have passed a bill to stabilize and lower the state's oil and gas tax rate.

Very few people in the state capitol of Bismarck support the state's current tax system. Representative Al Carlson, the House Majority Leader, put it this way:

"It was once explained to me that our tax policy is kinda like being on the wheel of fortune," he said. "Because sometimes you can hit the big trip to Hawaii and the next spot can be bankruptcy."

In North Dakota the oil and gas tax rate is pegged to the price of oil. When prices are high, companies pay about 11.5 percent on the value of oil produced. When prices are low for an extended period of time, they pay 5 percent. So in April, Carlson introduced House Bill 1476, which was designed to get rid of that volatility.

"We thought it would be beneficial to have a stable tax system both for the state of North Dakota and for the industry," he explained.

Here's how it will work: The enormous tax cut that lowers the rate to 5 percent disappears forever towards the end of this year. On January 1, 2016, the overall rate drops from 11.5 to 10 percent. And there's a new trigger, one that *raises* the rate back up to 11 percent if the price of oil stays above \$90 for three months in a row.

Severance taxes vary wildly from state to state. (<http://headwaterseconomics.org/interactive/oil-gas-local-governments-production-tax-revenue>) There are places like Alaska, where oil companies can pay over 20 percent of what they produce to the state. Then there are <http://insideenergy.org/2015/04/30/amidst-low-prices-north-dakota-scrambles-to-change-oil-tax-rate/>

states like [Oklahoma](https://stateimpact.npr.org/oklahoma/2013/08/27/study-oklahomas-drilling-incentives-reduce-modest-oil-and-gas-tax-rates/) where companies pay about three percent. There are also a million different exemptions and tax holidays that mean companies can pay different tax rates on new wells, old wells, wells that don't produce much or wells outside a developed oilfield. All that makes it very hard to get an apples-to-apples comparison of severance taxes.

Still, there are some conclusions we can make. Barry Rabe, professor of public and environmental policy at University of Michigan, studies oil and gas taxes. He has found that states that were earlier players in oil and gas tend to have the highest rates.

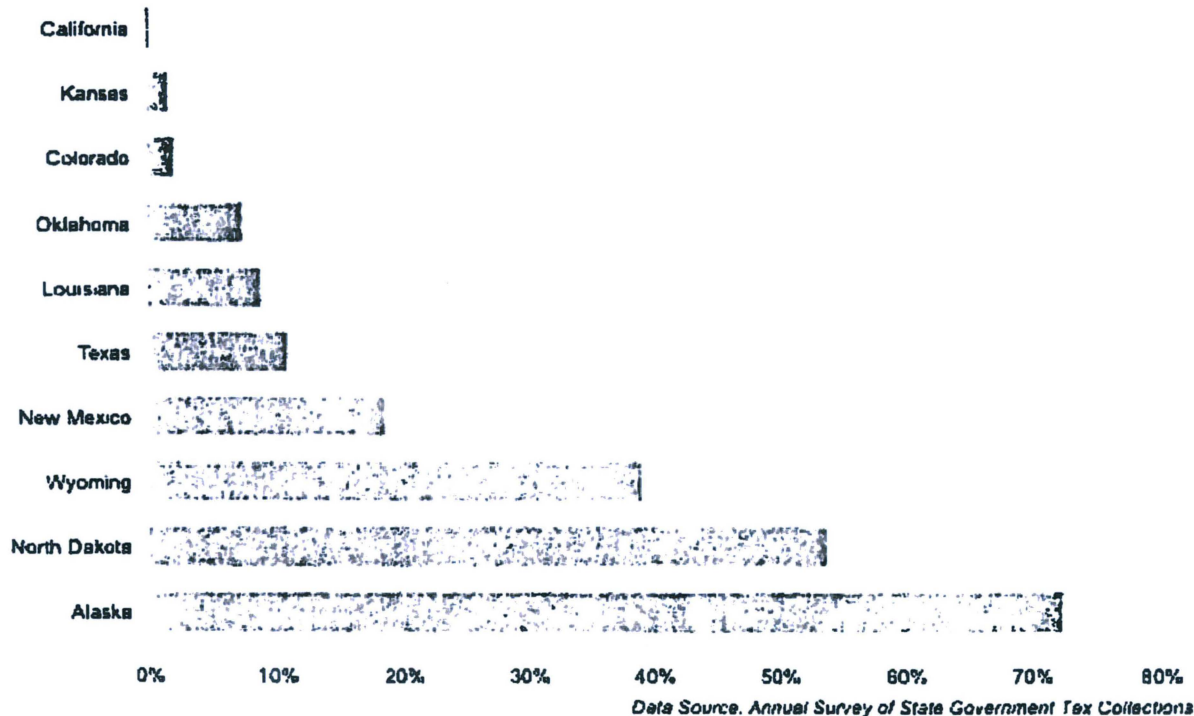
Take Wyoming, where oil was discovered in the 19th century. Companies there pay one of the highest tax rates in the lower 48 — just under 12 percent. That means if oil sells for \$100 a barrel, Wyoming collects about \$12 per barrel. Compare that to newer energy states like Ohio, which collects only 20 cents per barrel of oil they extract, no matter the price.

Ironically, states we tend to think of as most hostile toward taxation tend to set the highest rates, Rabe says.

Mark Haggerty, a researcher with [Headwaters Economics](http://headwaterseconomics.org/), a nonpartisan research group in Montana, says there is a reason for this. He says Wyoming has made a conscious decision to use its natural resources to fund state government and lower the tax burden on its citizens. As such, it needs to tax the industry heavily. Severance taxes make up 40 percent of total tax collections in Wyoming compared to only two percent in Colorado (<http://www.census.gov/govs/statetax/>), a state with a much more diverse economy that is much less dependent on natural resources.

States like Wyoming and North Dakota are, "very dependent on the industry, they need the industry, but they're also willing to be more aggressive in taxing the industry than their neighbors," according to Haggerty.

Which States Rely On Severance Tax Revenue The Most?
Severance Tax Revenue as a Percentage of Total Tax Collections In the Top Ten Oil Producing States



<http://1m5rim4bgenp2600za110opv13h.wpengine.netdna-cdn.com/files/2015/04/CORRECT-tax-graph.jpg>

Get the data: [CSV](http://rawgit.com/insideenergy/Data-for-stories/master/20150430-oilgas-taxrev/oilgas-taxrev.csv) | [XLS](http://rawgit.com/insideenergy/Data-for-stories/master/20150430-oilgas-taxrev/oilgas-taxrev.xlsx) | [Google Sheets](https://docs.google.com/spreadsheets/d/1kFft8pl1OsTn_qr_Wmom4ROWDb1WvASX_PRO6pdOoDO/edit?usp=sharing)
 Source and notes: [Github](https://github.com/InsideEnergy/Data-for-stories/tree/master/20150430-oilgas-taxrev)

But the shale boom is starting to change that. Now that fracking and horizontal drilling are unlocking reserves in unexpected places like Ohio and Michigan, there's more pressure to try to compete with other states for oil companies' business. North Dakota Senator Rich Wardner, R-Dickinson, made that argument before the House Finance and Taxation Committee while testifying in favor of lowering and stabilizing the tax rate. When the price of oil drops, he said a lower rate will cause companies to "stick around longer and there will be more activity out there."

But many researchers disagree with Wardner's argument.

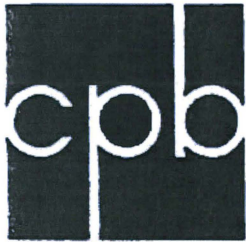
"There's not a lot of evidence, empirically, to suggest that drilling investment follows tax rates, especially when we're talking about a few percentage points," Rabe says. "And yet that still comes up in the minds of a lot of legislators who are thinking about how to best cultivate a resource."

Whether there's evidence for that or not, legislators are grasping for ways to stimulate an industry that's facing a very different future than it was just a few months ago.

What's Next:

- Wanna know how much tax revenue an oil well in the Bakken generates compared to the Eagle Ford, Niobrara or other oil-producing regions? [Headwaters Economics has you covered \(http://headwaterseconomics.org/interactive/oil-gas-local-governments-production-tax-revenue\)](http://headwaterseconomics.org/interactive/oil-gas-local-governments-production-tax-revenue).
- Read [this study \(http://headwaterseconomics.org/energy/state-energy-policies\)](http://headwaterseconomics.org/energy/state-energy-policies) comparing how much tax revenue oil-producing states return to local communities.

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