

HB

247 -

FILE 1

<TARGET><BILL>HB 247</BILL><SUBJECT>HB 247 - FILE
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2d CS FOR HOUSE BILL NO. 247()

IN THE LEGISLATURE OF THE STATE OF ALASKA
TWENTY-NINTH LEGISLATURE - SECOND SESSION

BY

**Offered:
Referred:**

Sponsor(s): HOUSE RULES COMMITTEE BY REQUEST OF THE GOVERNOR

A BILL

FOR AN ACT ENTITLED

1 "An Act relating to the powers and duties of the Alaska Oil and Gas Conservation
2 Commission; relating to exploration incentive credits; relating to confidential
3 information status and public record status of information in the possession of the
4 Department of Revenue; relating to interest applicable to delinquent tax; relating to the
5 oil and gas production tax rate for certain oil exempt from taxation or constituting a
6 landowner's royalty interest; relating to oil and gas production tax credits; relating to
7 tax credit certificates; relating to the calculation of the production tax value of oil and
8 gas; relating to refunds for the gas storage facility tax credit, the liquefied natural gas
9 storage facility tax credit, and the qualified in-state oil refinery infrastructure
10 expenditures tax credit; relating to the purchase of tax credit certificates from the oil
11 and gas tax credit fund; relating to lease expenditures; relating to oil and gas lease
12 expenditures and production tax credits for municipal entities; requiring a bond or cash

1 deposit with a business license application for an oil or gas business; establishing a
2 legislative working group to study the fiscal regime and tax structure and rates for oil
3 and gas produced south of 68 degrees North latitude; and providing for an effective
4 date."

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

6 * **Section 1.** AS 31.05.030 is amended by adding a new subsection to read:

7 (n) Upon request of the commissioner of revenue, the commission shall

8 (1) verify regular production for the purposes of AS 43.55.023(b) and
9 (l); and

10 (2) determine the commencement of regular production from a lease or
11 property for purposes of AS 43.55.160(f) and (g).

12 * **Sec. 2.** AS 38.05.036(a) is amended to read:

13 (a) The department may conduct audits regarding royalty and net profits under
14 oil and gas contracts, agreements, or leases under this chapter and regarding costs
15 related to exploration licenses entered into under AS 38.05.131 - 38.05.134 and
16 exploration incentive credits under this chapter [OR UNDER AS 41.09]. For purposes
17 of an audit under this section,

18 (1) the department may examine the books, papers, records, or
19 memoranda of a person regarding matters related to the audit; and

20 (2) the records and premises where a business is conducted shall be
21 open at all reasonable times for inspection by the department.

22 * **Sec. 3.** AS 38.05.036(b) is amended to read:

23 (b) The Department of Revenue may obtain from the department information
24 relating to royalty and net profits payments and to exploration incentive credits under
25 this chapter [OR UNDER AS 41.09], whether or not that information is confidential.
26 The Department of Revenue may use the information in carrying out its functions and
27 responsibilities under AS 43, and shall hold that information confidential to the extent
28 required by an agreement with the department or by AS 38.05.035(a)(8) [,
29 AS 41.09.010(d),] or AS 43.05.230.

1 * **Sec. 4.** AS 38.05.036(c) is amended to read:

2 (c) The department may obtain from the Department of Revenue all
3 information obtained under AS 43 relating to royalty and net profits and to exploration
4 incentive credits. The department may use the information for purposes of carrying out
5 its responsibilities and functions under this chapter [AND AS 41.09]. Information
6 made available to the department that was obtained under AS 43 is confidential and
7 subject to the provisions of AS 43.05.230.

8 * **Sec. 5.** AS 38.05.036(f) is amended to read:

9 (f) Except as otherwise provided in this section or in connection with official
10 investigations or proceedings of the department, it is unlawful for a current or former
11 officer, employee, or agent of the state to divulge information obtained by the
12 department as a result of an audit under this section that is required by an agreement
13 with the department or by AS 38.05.035(a)(8) [OR AS 41.09.010(d)] to be kept
14 confidential.

15 * **Sec. 6.** AS 38.05.036(g) is amended to read:

16 (g) Nothing in this section prohibits the publication of statistics in a manner
17 that maintains the confidentiality of information to the extent required by an
18 agreement with the department or by AS 38.05.035(a)(8) [OR AS 41.09.010(d)].

19 * **Sec. 7.** AS 40.25.100(a) is amended to read:

20 (a) Information in the possession of the Department of Revenue that discloses
21 the particulars of the business or affairs of a taxpayer or other person, including
22 information under AS 38.05.020(b)(11) that is subject to a confidentiality agreement
23 under AS 38.05.020(b)(12), is not a matter of public record, except as provided in
24 AS 43.05.230(i) - (l) [AS 43.05.230(i) OR (k)] or for purposes of investigation and
25 law enforcement. The information shall be kept confidential except when its
26 production is required in an official investigation, administrative adjudication under
27 AS 43.05.405 - 43.05.499, or court proceeding. These restrictions do not prohibit the
28 publication of statistics presented in a manner that prevents the identification of
29 particular reports and items, prohibit the publication of tax lists showing the names of
30 taxpayers who are delinquent and relevant information that may assist in the collection
31 of delinquent taxes, or prohibit the publication of records, proceedings, and decisions

1 under AS 43.05.405 - 43.05.499.

2 * **Sec. 8.** AS 43.05.225 is amended to read:

3 **Sec. 43.05.225. Interest.** Unless otherwise provided,

4 (1) a delinquent tax under this title,

5 (A) before January 1, 2014, bears interest in each calendar
6 quarter at the rate of five percentage points above the annual rate charged
7 member banks for advances by the 12th Federal Reserve District as of the first
8 day of that calendar quarter, or at the annual rate of 11 percent, whichever is
9 greater, compounded quarterly as of the last day of that quarter; [OR]

10 (B) on and after January 1, 2014, and before January 1, 2017,
11 bears interest in each calendar quarter at the rate of three percentage points
12 above the annual rate charged member banks for advances by the 12th Federal
13 Reserve District as of the first day of that calendar quarter; and

14 (C) on and after January 1, 2017, bears interest in each
15 calendar quarter at the rate of five percentage points above the annual
16 rate charged member banks for advances by the 12th Federal Reserve
17 District as of the first day of that calendar quarter, compounded quarterly
18 as of the last day of that quarter;

19 (2) the interest rate is 12 percent a year for

20 (A) delinquent fees payable under AS 05.15.095(c); and

21 (B) unclaimed property that is not timely paid or delivered, as
22 allowed by AS 34.45.470(a).

23 * **Sec. 9.** AS 43.05.230 is amended by adding a new subsection to read:

24 (l) For tax credit certificates purchased by the department in the preceding
25 calendar year under AS 43.55.028, the department shall make the following
26 information public by April 30 of each year:

27 (1) the name of each person from whom the department purchased a
28 transferable tax credit certificate; and

29 (2) the aggregate amount of the tax credit certificates purchased from
30 the person in the preceding calendar year.

31 * **Sec. 10.** AS 43.20.046(e) is amended to read:

1 (e) The department may [USE AVAILABLE MONEY IN THE OIL AND
2 GAS TAX CREDIT FUND ESTABLISHED IN AS 43.55.028 TO] make the refund
3 applied for under (d) of this section in whole or in part if the department finds that (1)
4 the claimant does not have an outstanding liability to the state [FOR UNPAID
5 DELINQUENT TAXES UNDER THIS TITLE]; and (2) after application of all
6 available tax credits, the claimant's total tax liability under this chapter for the calendar
7 year in which the claim is made is zero. [IN THIS SUBSECTION, "UNPAID
8 DELINQUENT TAX" MEANS AN AMOUNT OF TAX FOR WHICH THE
9 DEPARTMENT HAS ISSUED AN ASSESSMENT THAT HAS NOT BEEN PAID
10 AND, IF CONTESTED, HAS NOT BEEN FINALLY RESOLVED IN THE
11 TAXPAYER'S FAVOR.]

12 * **Sec. 11.** AS 43.20.047(e) is amended to read:

13 (e) The department may [USE MONEY AVAILABLE IN THE OIL AND
14 GAS TAX CREDIT FUND ESTABLISHED IN AS 43.55.028 TO] make a refund or
15 payment under (d) of this section in whole or in part if the department finds that (1)
16 the claimant does not have an outstanding liability to the state [FOR UNPAID
17 DELINQUENT TAXES UNDER THIS TITLE]; and (2) after application of all
18 available tax credits, the claimant's total tax liability under this chapter for the calendar
19 year in which the claim is made is zero. [IN THIS SUBSECTION, "UNPAID
20 DELINQUENT TAX" MEANS AN AMOUNT OF TAX FOR WHICH THE
21 DEPARTMENT HAS ISSUED AN ASSESSMENT THAT HAS NOT BEEN PAID
22 AND, IF CONTESTED, HAS NOT BEEN FINALLY RESOLVED IN THE
23 TAXPAYER'S FAVOR.]

24 * **Sec. 12.** AS 43.20.053(e) is amended to read:

25 (e) The department may [USE MONEY AVAILABLE IN THE OIL AND
26 GAS TAX CREDIT FUND ESTABLISHED IN AS 43.55.028 TO] make a refund or
27 payment under (d) of this section in whole or in part if the department finds that

28 (1) the claimant does not have an outstanding liability to the state
29 [FOR UNPAID DELINQUENT TAXES UNDER THIS TITLE]; and

30 (2) after application of all available tax credits, the claimant's total tax
31 liability under this chapter for the calendar year in which the claim is made is zero.

1 * **Sec. 13.** AS 43.55.011(i) is amended to read:

2 (i) There is levied on the producer of oil or gas a tax for all oil and gas
3 produced each calendar year from each lease or property in the state the ownership or
4 right to which constitutes a landowner's royalty interest, except for oil and gas the
5 ownership or right to which is exempt from taxation. The levy of tax under this
6 subsection may not be less than zero. The provisions of this subsection apply to a
7 landowner's royalty interest as follows:

8 (1) the tax levied for oil is equal to five percent of the gross value at
9 the point of production of the oil;

10 (2) the tax levied for gas is equal to 1.667 percent of the gross value at
11 the point of production of the gas;

12 (3) if the department determines that, for purposes of reducing the
13 producer's tax liability under (1) or (2) of this subsection, the producer has received or
14 will receive consideration from the royalty owner offsetting all or a part of the
15 producer's royalty obligation, other than a deduction under AS 43.55.020 related to a
16 settlement with a royalty owner of the amount of a tax paid, then, notwithstanding (1)
17 and (2) of this subsection, the tax is equal to 25 percent of the gross value at the point
18 of production of the oil and gas.

19 * **Sec. 14.** AS 43.55.011(m) is amended to read:

20 (m) Notwithstanding any contrary provision of [AS 38.05.180(i),
21 AS 41.09.010,] AS 43.55.024 [,] or 43.55.025, the department shall provide by
22 regulation a method to ensure that, for a calendar year for which a producer's tax
23 liability is limited by (j), (k), or (o) of this section, tax credits based on a lease
24 expenditure incurred before January 1, 2011, that are otherwise available under
25 [AS 38.05.180(i), AS 41.09.010,] AS 43.55.024 [,] or 43.55.025 and allocated to gas
26 subject to the limitations in (j), (k), and (o) of this section are accounted for as though
27 the credits had been applied first against a tax liability calculated without regard to the
28 limitations under (j), (k), and (o) of this section so as to reduce the tax liability to the
29 maximum amount provided for under (j) or (o) of this section for the production of gas
30 or (k) of this section for the production of oil. The regulation must provide for a
31 reasonable method to allocate tax credits to gas subject to (j) and (o) of this section.

1 Only the amount of a tax credit remaining after the accounting provided for under this
2 subsection may be used for a later calendar year, transferred to another person, or
3 applied against a tax levied on the production of oil or gas not subject to (j), (k), or (o)
4 of this section to the extent otherwise allowed.

5 * **Sec. 15.** AS 43.55.023(b) is amended to read:

6 (b) Before January 1, 2014, a producer or explorer may elect to take a tax
7 credit in the amount of 25 percent of a carried-forward annual loss. For lease
8 expenditures incurred on and after January 1, 2014, and before January 1, 2016, to
9 explore for, develop, or produce oil or gas deposits located north of 68 degrees North
10 latitude, a producer or explorer may elect to take a tax credit in the amount of 45
11 percent of a carried-forward annual loss. For lease expenditures incurred on and after
12 January 1, 2016, to explore for, develop, or produce oil or gas deposits located north
13 of 68 degrees North latitude, a producer or explorer may elect to take a tax credit in
14 the amount of 35 percent of a carried-forward annual loss. For lease expenditures
15 incurred on or after January 1, 2014, **and before January 1, 2018,** to explore for,
16 develop, or produce oil or gas deposits located south of 68 degrees North latitude, a
17 producer or explorer may elect to take a tax credit in the amount of 25 percent of a
18 carried-forward annual loss. A credit under this subsection may be applied against a
19 tax levied by AS 43.55.011(e). For purposes of this subsection, a carried-forward
20 annual loss is the amount of a producer's or explorer's adjusted lease expenditures
21 under AS 43.55.165 and 43.55.170 for a previous calendar year that was not
22 deductible in calculating production tax values for that calendar year under
23 AS 43.55.160. **For lease expenditures incurred on or after January 1, 2017, any**
24 **reduction under AS 43.55.160(f) or (g) is added back to the calculation of**
25 **production tax values for that calendar year under AS 43.55.160 for the**
26 **determination of a carried-forward annual loss under this subsection. A credit**
27 **under this subsection may be taken for lease expenditures incurred after**
28 **December 31, 2016,**

29 **(1) in the Cook Inlet sedimentary basin only if, during calendar**
30 **year 2016, the producer or explorer had regular production of oil or gas in the**
31 **Cook Inlet sedimentary basin;**

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(2) north of 68 degrees North latitude only if,

(A) during calendar year 2016, the producer or explorer had regular production of an average of less than 15,000 BTU equivalent barrels a day in the state; or

(B) the lease expenditures were incurred under a unit plan of development or a plan of exploration approved by the commissioner of natural resources consistent with AS 38.05.180.

* **Sec. 16.** AS 43.55.023(d) is amended to read:

(d) A person that is entitled to take a tax credit under this section that wishes to transfer the unused credit to another person or obtain a cash payment under AS 43.55.028 may apply to the department for a transferable tax credit certificate. An application under this subsection must be in a form prescribed by the department and must include supporting information and documentation that the department reasonably requires. The department shall grant or deny an application, or grant an application as to a lesser amount than that claimed and deny it as to the excess, not later than 120 days after the latest of (1) March 31 of the year following the calendar year in which the [QUALIFIED CAPITAL EXPENDITURE OR] carried-forward annual loss for which the credit is claimed was incurred; (2) the date the statement required under AS 43.55.030(a) or (e) was filed for the calendar year in which the [QUALIFIED CAPITAL EXPENDITURE OR] carried-forward annual loss for which the credit is claimed was incurred; or (3) the date the application was received by the department. If, based on the information then available to it, the department is reasonably satisfied that the applicant is entitled to a credit, the department shall issue the applicant a transferable tax credit certificate for the amount of the credit. A certificate issued under this subsection does not expire.

* **Sec. 17.** AS 43.55.023(e) is amended to read:

(e) A person to which a transferable tax credit certificate is issued under (d) of this section may transfer the certificate to another person, and a transferee may further transfer the certificate. Subject to the limitations set out in **former (a) of this section and (b) - (d)** [(a) - (d)] of this section, and notwithstanding any action the department may take with respect to the applicant under (g) of this section, the owner of a

1 certificate may apply the credit or a portion of the credit shown on the certificate only
2 against a tax levied by AS 43.55.011(e). However, a credit shown on a transferable tax
3 credit certificate may not be applied to reduce a transferee's total tax liability under
4 AS 43.55.011(e) for oil and gas produced during a calendar year to less than 80
5 percent of the tax that would otherwise be due without applying that credit. Any
6 portion of a credit not used under this subsection may be applied in a later period.

7 * **Sec. 18.** AS 43.55.023(l) is amended to read:

8 (l) A producer or explorer may apply for a tax credit for a well lease
9 expenditure incurred in the state south of 68 degrees North latitude after June 30,
10 2010, as follows:

11 (1) notwithstanding that a well lease expenditure incurred in the state
12 south of 68 degrees North latitude may be a deductible lease expenditure for purposes
13 of calculating the production tax value of oil and gas under AS 43.55.160(a), unless a
14 credit for that expenditure is taken under [(a) OF THIS SECTION, AS 38.05.180(i),
15 AS 41.09.010,] AS 43.20.043 [,] or AS 43.55.025, a producer or explorer that incurs a
16 well lease expenditure in the state south of 68 degrees North latitude may elect to
17 apply a tax credit against a tax levied by AS 43.55.011(e) in the amount of

18 (A) 40 percent of that expenditure incurred before calendar
19 year 2017;

20 (B) 20 percent of that expenditure incurred in calendar
21 year 2017 or 2018 [A TAX CREDIT UNDER THIS PARAGRAPH MAY BE
22 APPLIED FOR A SINGLE CALENDAR YEAR];

23 (2) a producer or explorer may take a credit for a well lease
24 expenditure incurred

25 (A) in the state south of 68 degrees North latitude in connection
26 with geological or geophysical exploration or in connection with an
27 exploration well only if the producer or explorer

28 (i) [(A)] agrees, in writing, to the applicable provisions
29 of AS 43.55.025(f)(2); and

30 (ii) [(B)] submits to the Department of Natural
31 Resources all data that would be required to be submitted under

1 AS 43.55.025(f)(2);

2 **(B) in the Cook Inlet sedimentary basin only if, during**
3 **calendar year 2016, the producer or explorer had regular production of**
4 **oil or gas in the Cook Inlet sedimentary basin.**

5 * Sec. 19. AS 43.55.023(n) is amended to read:

6 (n) For the purposes of (l) of this section, a well lease expenditure incurred in
7 the state south of 68 degrees North latitude is a lease expenditure that is

8 (1) directly related to an exploration well, a stratigraphic test well, a
9 producing well, or an injection well other than a disposal well, located in the state
10 south of 68 degrees North latitude, if the expenditure is [A QUALIFIED CAPITAL
11 EXPENDITURE AND] an intangible drilling and development cost authorized under
12 26 U.S.C. (Internal Revenue Code), as amended, and 26 C.F.R. 1.612-4, regardless of
13 the elections made under 26 U.S.C. 263(c); in this paragraph, an expenditure directly
14 related to a well includes an expenditure for well sidetracking, well deepening, well
15 completion or recompletion, or well workover, regardless of whether the well is or has
16 been a producing well; or

17 (2) an expense for seismic work conducted within the boundaries of a
18 production or exploration unit.

19 * Sec. 20. AS 43.55.024(i) is amended to read:

20 (i) A producer may apply against the producer's tax liability for the calendar
21 year under AS 43.55.011(e) a tax credit of \$5 for each barrel of oil taxable under
22 AS 43.55.011(e) that **receives a reduction in the gross value at the point of**
23 **production under** [MEETS ONE OR MORE OF THE CRITERIA IN]
24 AS 43.55.160(f) or (g) and that is produced during a calendar year after December 31,
25 2013. A tax credit authorized by this subsection may not reduce a producer's tax
26 liability for a calendar year under AS 43.55.011(e) below zero.

27 * Sec. 21. AS 43.55.024(j) is amended to read:

28 (j) A producer may apply against the producer's tax liability for the calendar
29 year under AS 43.55.011(e) a tax credit in the amount specified in this subsection for
30 each barrel of oil taxable under AS 43.55.011(e) that does not **receive a reduction in**
31 **the gross value at the point of production under** [MEET ANY OF THE CRITERIA

1 IN] AS 43.55.160(f) or (g) and that is produced during a calendar year after
2 December 31, 2013, from leases or properties north of 68 degrees North latitude. A tax
3 credit under this subsection may not reduce a producer's tax liability for a calendar
4 year under AS 43.55.011(e) below the amount calculated under AS 43.55.011(f). The
5 amount of the tax credit for a barrel of taxable oil subject to this subsection produced
6 during a month of the calendar year is

7 (1) \$8 for each barrel of taxable oil if the average gross value at the
8 point of production for the month is less than \$80 a barrel;

9 (2) \$7 for each barrel of taxable oil if the average gross value at the
10 point of production for the month is greater than or equal to \$80 a barrel, but less than
11 \$90 a barrel;

12 (3) \$6 for each barrel of taxable oil if the average gross value at the
13 point of production for the month is greater than or equal to \$90 a barrel, but less than
14 \$100 a barrel;

15 (4) \$5 for each barrel of taxable oil if the average gross value at the
16 point of production for the month is greater than or equal to \$100 a barrel, but less
17 than \$110 a barrel;

18 (5) \$4 for each barrel of taxable oil if the average gross value at the
19 point of production for the month is greater than or equal to \$110 a barrel, but less
20 than \$120 a barrel;

21 (6) \$3 for each barrel of taxable oil if the average gross value at the
22 point of production for the month is greater than or equal to \$120 a barrel, but less
23 than \$130 a barrel;

24 (7) \$2 for each barrel of taxable oil if the average gross value at the
25 point of production for the month is greater than or equal to \$130 a barrel, but less
26 than \$140 a barrel;

27 (8) \$1 for each barrel of taxable oil if the average gross value at the
28 point of production for the month is greater than or equal to \$140 a barrel, but less
29 than \$150 a barrel;

30 (9) zero if the average gross value at the point of production for the
31 month is greater than or equal to \$150 a barrel.

1 * **Sec. 22.** AS 43.55.025(m) is amended to read:

2 (m) The persons that drill the first four exploration wells in the state and
3 within the areas described in (o) of this section on state lands, private lands, or federal
4 onshore lands for the purpose of discovering oil or gas that penetrate and evaluate a
5 prospect in a basin described in (o) of this section are eligible for a credit under (a)(6)
6 of this section. A credit under this subsection may not be taken for more than two
7 exploration wells in a single area described in (o)(1) - (6) of this section. Exploration
8 expenditures eligible for the credit in this subsection **in an area described in (o)(1) -**
9 **(3), (5), or (6) of this section** must be incurred for work performed after June 1, 2012,
10 and before July 1, 2016. **Exploration expenditures eligible for the credit in this**
11 **subsection in the area described in (o)(4) of this section must be for work**
12 **performed after June 1, 2012, and before January 1, 2017, except that**
13 **expenditures to complete an exploration well in an area described in (o)(4) of this**
14 **section that was spudded but not completed before January 1, 2017, are eligible**
15 **for the credit under this subsection.** A person planning to drill an exploration well
16 on private land and to apply for a credit under this subsection shall obtain written
17 consent from the owner of the oil and gas interest for the full public release of all well
18 data after the expiration of the confidentiality period applicable to information
19 collected under (f) of this section. The written consent of the owner of the oil and gas
20 interest must be submitted to the commissioner of natural resources before approval of
21 the proposed exploration well. In addition to the requirements in (c)(1), (c)(2)(A), and
22 (c)(2)(C) of this section and submission of the written consent of the owner of the oil
23 and gas interest, a person planning to drill an exploration well shall obtain approval
24 from the commissioner of natural resources before the well is spudded. The
25 commissioner of natural resources shall make a written determination approving or
26 rejecting an exploration well within 60 days after receiving the request for approval or
27 as soon as is practicable thereafter. Before approving the exploration well, the
28 commissioner of natural resources shall consider the following: the location of the
29 well; the proximity to a community in need of a local energy source; the proximity of
30 existing infrastructure; the experience and safety record of the explorer in conducting
31 operations in remote or roadless areas; the projected cost schedule; whether seismic

1 mapping and seismic data sufficiently identify a particular trap for exploration;
2 whether the targeted and planned depth and range are designed to penetrate and fully
3 evaluate the hydrocarbon potential of the proposed prospect and reach the level below
4 which economic hydrocarbon reservoirs are likely to be found, or reach 12,000 feet or
5 more true vertical depth; and whether the exploration plan provides for a full
6 evaluation of the wellbore below surface casing to the depth of the well. Whether the
7 exploration well for which a credit is requested under this subsection is located within
8 an area and a basin described under (o) of this section shall be determined by the
9 commissioner of natural resources and reported to the commissioner. A taxpayer that
10 obtains a credit under this subsection may not claim a tax credit under AS 43.55.023
11 or another provision in this section for the same exploration expenditure.

12 * **Sec. 23.** AS 43.55.025(m), as amended by sec. 22 of this Act, is amended to read:

13 (m) The persons that drill the first four exploration wells in the state and
14 within the areas described in (o) of this section on state lands, private lands, or federal
15 onshore lands for the purpose of discovering oil or gas that penetrate and evaluate a
16 prospect in a basin described in (o) of this section are eligible for a credit under (a)(6)
17 of this section. A credit under this subsection may not be taken for more than two
18 exploration wells in a single area described in (o)(1) - (6) of this section. Exploration
19 expenditures eligible for the credit in this subsection in an area described in (o)(1) -
20 (3), (5), or (6) of this section must be incurred for work performed after June 1, 2012,
21 and before July 1, 2016. Exploration expenditures eligible for the credit in this
22 subsection in the area described in (o)(4) of this section must be for work performed
23 after June 1, 2012, and before January 1, 2017, except that expenditures to complete
24 an exploration well in an area described in (o)(4) of this section that was spudded but
25 not completed before January 1, 2017, are eligible for the credit under this subsection.
26 A person planning to drill an exploration well on private land and to apply for a credit
27 under this subsection shall obtain written consent from the owner of the oil and gas
28 interest for the full public release of all well data after the expiration of the
29 confidentiality period applicable to information collected under (f) of this section. The
30 written consent of the owner of the oil and gas interest must be submitted to the
31 commissioner of natural resources before approval of the proposed exploration well.

1 In addition to the requirements in (c)(1), (c)(2)(A), and (c)(2)(C) of this section and
2 submission of the written consent of the owner of the oil and gas interest, a person
3 planning to drill an exploration well shall obtain approval from the commissioner of
4 natural resources before the well is spudded. The commissioner of natural resources
5 shall make a written determination approving or rejecting an exploration well within
6 60 days after receiving the request for approval or as soon as is practicable thereafter.
7 Before approving the exploration well, the commissioner of natural resources shall
8 consider the following: the location of the well; the proximity to a community in need
9 of a local energy source; the proximity of existing infrastructure; the experience and
10 safety record of the explorer in conducting operations in remote or roadless areas; the
11 projected cost schedule; whether seismic mapping and seismic data sufficiently
12 identify a particular trap for exploration; whether the targeted and planned depth and
13 range are designed to penetrate and fully evaluate the hydrocarbon potential of the
14 proposed prospect and reach the level below which economic hydrocarbon reservoirs
15 are likely to be found, or reach 12,000 feet or more true vertical depth; and whether
16 the exploration plan provides for a full evaluation of the wellbore below surface casing
17 to the depth of the well. Whether the exploration well for which a credit is requested
18 under this subsection is located within an area and a basin described under (o) of this
19 section shall be determined by the commissioner of natural resources and reported to
20 the commissioner. A taxpayer that obtains a credit under this subsection may not claim
21 a tax credit under [AS 43.55.023 OR] another provision in this section for the same
22 exploration expenditure.

23 * **Sec. 24.** AS 43.55.025(o) is amended to read:

24 (o) The activity that is the basis for a credit claimed under (a)(6) and (m) of
25 this section [OR (a)(7) AND (n) OF THIS SECTION] must be for the exploration of a
26 basin and within the following areas whose central points are determined using the
27 World Geographic System of 1984 datum,

28 (1) 100 miles from 66.896128 degrees North, -162.598187 degrees
29 West;

30 (2) 150 miles from 64.839474 degrees North, -147.72094 degrees
31 West;

- 1 (3) 50 miles from 62.776428 degrees North, -164.495201 degrees
2 West;
- 3 (4) 50 miles from 62.110357 degrees North, -145.530551 degrees
4 West;
- 5 (5) 100 miles from 58.189868 degrees North, -157.371104 degrees
6 West;
- 7 (6) 100 miles from 56.005988 degrees North, -160.56083 degrees
8 West.

9 * **Sec. 25.** AS 43.55.028(a) is amended to read:

10 (a) The oil and gas tax credit fund is established as a separate fund of the state.
11 The purpose of the fund is to purchase transferable tax credit certificates issued under
12 AS 43.55.023 and production tax credit certificates issued under AS 43.55.025 [AND
13 TO PAY REFUNDS AND PAYMENTS CLAIMED UNDER AS 43.20.046,
14 43.20.047, OR 43.20.053].

15 * **Sec. 26.** AS 43.55.028(a), as amended by sec. 25 of this Act, is amended to read:

16 (a) The oil and gas tax credit fund is established as a separate fund of the state.
17 The purpose of the fund is to purchase transferable tax credit certificates issued under
18 **former** AS 43.55.023 and production tax credit certificates issued under
19 AS 43.55.025.

20 * **Sec. 27.** AS 43.55.028(e) is amended to read:

21 (e) The department, on the written application of a person to whom a
22 transferable tax credit certificate has been issued under AS 43.55.023(d) or former
23 AS 43.55.023(m) or to whom a production tax credit certificate has been issued under
24 AS 43.55.025(f), may use available money in the oil and gas tax credit fund to
25 purchase, in whole or in part, the certificate. **The department may not purchase a**
26 **total of more than \$75,000,000 in tax credit certificates from a person in a**
27 **calendar year. The department may purchase a certificate or part of a certificate**
28 **only** if the department finds that

29 (1) the calendar year of the purchase is not earlier than the first
30 calendar year for which the credit shown on the certificate would otherwise be allowed
31 to be applied against a tax;

1 (2) the application is not the result of the division of a single entity
2 into multiple entities that would reasonably be expected to apply as a single entity
3 if the \$75,000,000 limitation in this subsection did not exist [APPLICANT DOES
4 NOT HAVE AN OUTSTANDING LIABILITY TO THE STATE FOR UNPAID
5 DELINQUENT TAXES UNDER THIS TITLE];

6 (3) the applicant's total tax liability under AS 43.55.011(e), after
7 application of all available tax credits, for the calendar year in which the application is
8 made is zero;

9 (4) the applicant's average daily production of oil and gas taxable
10 under AS 43.55.011(e) during the calendar year preceding the calendar year in which
11 the application is made was not more than 50,000 BTU equivalent barrels; and

12 (5) the purchase is consistent with this section and regulations adopted
13 under this section.

14 * **Sec. 28.** AS 43.55.028(e), as amended by sec. 27 of this Act, is amended to read:

15 (e) The department, on the written application of a person to whom a
16 transferable tax credit certificate has been issued under former AS 43.55.023(d) or
17 (m) [FORMER AS 43.55.023(m)] or to whom a production tax credit certificate has
18 been issued under AS 43.55.025(f), may use available money in the oil and gas tax
19 credit fund to purchase, in whole or in part, the certificate. The department may not
20 purchase a total of more than \$75,000,000 in tax credit certificates from a person in a
21 calendar year. The department may purchase a certificate or part of a certificate only if
22 the department finds that

23 (1) the calendar year of the purchase is not earlier than the first
24 calendar year for which the credit shown on the certificate would otherwise be allowed
25 to be applied against a tax;

26 (2) the application is not the result of the division of a single entity into
27 multiple entities that would reasonably be expected to apply as a single entity if the
28 \$75,000,000 limitation in this subsection did not exist;

29 (3) the applicant's total tax liability under AS 43.55.011(e), after
30 application of all available tax credits, for the calendar year in which the application is
31 made is zero;

1 (4) the applicant's average daily production of oil and gas taxable
2 under AS 43.55.011(e) during the calendar year preceding the calendar year in which
3 the application is made was not more than 50,000 BTU equivalent barrels; and

4 (5) the purchase is consistent with this section and regulations adopted
5 under this section.

6 * **Sec. 29.** AS 43.55.028(g) is amended to read:

7 (g) The department **shall** [MAY] adopt regulations to carry out the purposes
8 of this section, including standards and procedures to allocate available money among
9 applications for purchases under this chapter [AND CLAIMS FOR REFUNDS AND
10 PAYMENTS UNDER AS 43.20.046, 43.20.047, OR 43.20.053] when the total
11 amount of the applications for purchase [AND CLAIMS FOR REFUND] exceed the
12 amount of available money in the fund. The regulations adopted by the department
13 **must grant a preference to an applicant if at least 80 percent of the applicant's**
14 **workforce in the state in the previous calendar year was composed of resident**
15 **workers; in this subsection, "resident worker" has the meaning given in**
16 **AS 43.40.092(b)** [MAY NOT, WHEN ALLOCATING AVAILABLE MONEY IN
17 THE FUND UNDER THIS SECTION, DISTINGUISH AN APPLICATION FOR
18 THE PURCHASE OF A CREDIT CERTIFICATE ISSUED UNDER FORMER
19 AS 43.55.023(m) OR A CLAIM FOR A REFUND OR PAYMENT UNDER
20 AS 43.20.046, 43.20.047, OR 43.20.053].

21 * **Sec. 30.** AS 43.55.028 is amended by adding a new subsection to read:

22 (j) If an applicant has an outstanding liability to the state directly related to the
23 applicant's oil or gas exploration, development, or production that has not previously
24 been the basis of a reduction by the department under this subsection, the department
25 may purchase only that portion of a certificate that exceeds the outstanding liability.
26 The department may apply the amount by which the department reduced its purchase
27 of a certificate because of an outstanding liability to satisfy the outstanding liability,
28 except that, if the outstanding liability is contested through an appeal or adjudicatory
29 proceeding already established by law, the department may apply the amount to satisfy
30 the outstanding liability only with the applicant's consent. Satisfaction of an
31 outstanding liability under this subsection does not affect the applicant's ability to

1 contest that liability. The department may enter into contracts or agreements with
2 another department to which the outstanding liability is owed.

3 * **Sec. 31.** AS 43.55.029(a) is amended to read:

4 (a) An explorer or producer that has applied for a production tax credit under
5 AS 43.55.023(b) [AS 43.55.023(a), (b),] or (D), [OR] 43.55.025(a), or former
6 AS 43.55.023(a) may make a present assignment of the production tax credit
7 certificate expected to be issued by the department to a third-party assignee. The
8 assignment may be made either at the time the application is filed with the department
9 or not later than 30 days after the date of filing with the department. Once a notice of
10 assignment in compliance with this section is filed with the department, the
11 assignment is irrevocable and cannot be modified by the explorer or producer without
12 the written consent of the assignee named in the assignment. If a production tax credit
13 certificate is issued to the explorer or producer, the notice of assignment remains
14 effective and shall be filed with the department by the explorer or producer together
15 with any application for the department to purchase the certificate under
16 AS 43.55.028(e).

17 * **Sec. 32.** AS 43.55.029(a), as amended by sec. 31 of this Act, is amended to read:

18 (a) An explorer or producer that has applied for a production tax credit under
19 AS 43.55.023(b) [OR (D)], 43.55.025(a), or former AS 43.55.023(a) or (D) may make a
20 present assignment of the production tax credit certificate expected to be issued by the
21 department to a third-party assignee. The assignment may be made either at the time
22 the application is filed with the department or not later than 30 days after the date of
23 filing with the department. Once a notice of assignment in compliance with this
24 section is filed with the department, the assignment is irrevocable and cannot be
25 modified by the explorer or producer without the written consent of the assignee
26 named in the assignment. If a production tax credit certificate is issued to the explorer
27 or producer, the notice of assignment remains effective and shall be filed with the
28 department by the explorer or producer together with any application for the
29 department to purchase the certificate under AS 43.55.028(e).

30 * **Sec. 33.** AS 43.55.029(a), as amended by secs. 31 and 32 of this Act, is amended to read:

31 (a) An explorer or producer that has applied for a production tax credit under

1 AS 43.55.025(a) [AS 43.55.023(b), 43.55.025(a),] or former AS 43.55.023(a), (b), or
2 (l) may make a present assignment of the production tax credit certificate expected to
3 be issued by the department to a third-party assignee. The assignment may be made
4 either at the time the application is filed with the department or not later than 30 days
5 after the date of filing with the department. Once a notice of assignment in compliance
6 with this section is filed with the department, the assignment is irrevocable and cannot
7 be modified by the explorer or producer without the written consent of the assignee
8 named in the assignment. If a production tax credit certificate is issued to the explorer
9 or producer, the notice of assignment remains effective and shall be filed with the
10 department by the explorer or producer together with any application for the
11 department to purchase the certificate under AS 43.55.028(e).

12 * **Sec. 34.** AS 43.55.030(a) is amended to read:

13 (a) A producer that produces oil or gas from a lease or property in the state
14 during a calendar year, whether or not any tax payment is due under AS 43.55.020(a)
15 for that oil or gas, shall file with the department on March 31 of the following year a
16 statement, under oath, in a form prescribed by the department, giving, with other
17 information required, the following:

18 (1) a description of each lease or property from which oil or gas was
19 produced, by name, legal description, lease number, or accounting codes assigned by
20 the department;

21 (2) the names of the producer and, if different, the person paying the
22 tax, if any;

23 (3) the gross amount of oil and the gross amount of gas produced from
24 each lease or property, separately identifying the gross amount of gas produced from
25 each oil and gas lease to which an effective election under AS 43.55.014(a) applies,
26 the amount of gas delivered to the state under AS 43.55.014(b), and the percentage of
27 the gross amount of oil and gas owned by the producer;

28 (4) the gross value at the point of production of the oil and of the gas
29 produced from each lease or property owned by the producer and the costs of
30 transportation of the oil and gas;

31 (5) the name of the first purchaser and the price received for the oil and

1 for the gas, unless relieved from this requirement in whole or in part by the
2 department;

3 (6) the producer's [QUALIFIED CAPITAL EXPENDITURES, AS
4 DEFINED IN AS 43.55.023, OTHER] lease expenditures under AS 43.55.165 [,] and
5 adjustments or other payments or credits under AS 43.55.170;

6 (7) the production tax values of the oil and gas under AS 43.55.160(a)
7 or of the oil under AS 43.55.160(h), as applicable;

8 (8) any claims for tax credits to be applied; and

9 (9) calculations showing the amounts, if any, that were or are due
10 under AS 43.55.020(a) and interest on any underpayment or overpayment.

11 * **Sec. 35.** AS 43.55.030(e) is amended to read:

12 (e) An explorer or producer that incurs a lease expenditure under
13 AS 43.55.165 or receives a payment or credit under AS 43.55.170 during a calendar
14 year but does not produce oil or gas from a lease or property in the state during the
15 calendar year shall file with the department, on March 31 of the following year, a
16 statement, under oath, in a form prescribed by the department, giving, with other
17 information required, the following:

18 (1) the explorer's or producer's [QUALIFIED CAPITAL
19 EXPENDITURES, AS DEFINED IN AS 43.55.023, OTHER] lease expenditures
20 under AS 43.55.165 [,] and adjustments or other payments or credits under
21 AS 43.55.170; and

22 (2) if the explorer or producer receives a payment or credit under
23 AS 43.55.170, calculations showing whether the explorer or producer is liable for a
24 tax under AS 43.55.160(d) or 43.55.170(b) and, if so, the amount.

25 * **Sec. 36.** AS 43.55.075(b) is amended to read:

26 (b) A decision of a regulatory agency, court, or other body with authority to
27 resolve disputes that results in a retroactive change to a lease expenditure, to an
28 adjustment to a lease expenditure, to costs of transportation, to sale price, to prevailing
29 value, or to consideration of quality differentials relating to the commingling of oils
30 has a corresponding effect, either an increase or decrease, as applicable, on the
31 production tax value of oil or gas or the amount or availability of a tax credit as

1 determined under this chapter. For purposes of this section, a change to a lease
2 expenditure includes a change in the categorization of a lease expenditure as a
3 qualified capital expenditure for the purposes of former AS 43.55.023(a) or as not a
4 qualified capital expenditure for the purposes of former AS 43.55.023(a). The
5 producer shall

6 (1) within 60 days after the change, notify the department in writing;

7 and

8 (2) within 120 days after the change, file amended returns covering all
9 periods affected by the change, unless the department agrees otherwise or a stay is in
10 place that affects the filing or payment, regardless of the pendency of appeals of the
11 decision.

12 * **Sec. 37.** AS 43.55.160(d) is amended to read:

13 (d) Irrespective of whether a producer produces taxable oil or gas during a
14 calendar year or month, the producer is considered to have generated a positive
15 production tax value if a calculation described in (a) of this section yields a positive
16 number because the producer's adjusted lease expenditures for a calendar year under
17 AS 43.55.165 and 43.55.170 are less than zero as a result of the producer's receiving a
18 payment or credit under AS 43.55.170. [AN EXPLORER THAT HAS TAKEN A
19 TAX CREDIT UNDER AS 43.55.023(b) OR THAT HAS OBTAINED A
20 TRANSFERABLE TAX CREDIT CERTIFICATE UNDER AS 43.55.023(d) FOR
21 THE AMOUNT OF A TAX CREDIT UNDER AS 43.55.023(b) IS CONSIDERED A
22 PRODUCER, SUBJECT TO THE TAX LEVIED UNDER AS 43.55.011(e), TO THE
23 EXTENT THAT THE EXPLORER GENERATES A POSITIVE PRODUCTION
24 TAX VALUE AS THE RESULT OF THE EXPLORER'S RECEIVING A
25 PAYMENT OR CREDIT UNDER AS 43.55.170.]

26 * **Sec. 38.** AS 43.55.160(e) is amended to read:

27 (e) Any adjusted lease expenditures under AS 43.55.165 and 43.55.170 that
28 would otherwise be deductible by a producer in a calendar year but whose deduction
29 would cause an annual production tax value calculated under (a)(1) or (h) of this
30 section of taxable oil or gas produced during the calendar year to be less than zero
31 may be used to establish a carried-forward annual loss under AS 43.55.023(b) or

1 **43.55.165(a)(3)**. However, the department shall provide by regulation a method to
2 ensure that, for a period for which a producer's tax liability is limited by
3 AS 43.55.011(j), (k), (o), or (p), any adjusted lease expenditures under AS 43.55.165
4 and 43.55.170 that would otherwise be deductible by a producer for that period but
5 whose deduction would cause a production tax value calculated under (a)(1)(C), (D),
6 (E), or (F), or (h)(3) of this section to be less than zero are accounted for as though the
7 adjusted lease expenditures had first been used as deductions in calculating the
8 production tax values of oil or gas subject to any of the limitations under
9 AS 43.55.011(j), (k), (o), or (p) that have positive production tax values so as to
10 reduce the tax liability calculated without regard to the limitation to the maximum
11 amount provided for under the applicable provision of AS 43.55.011(j), (k), (o), or (p).
12 Only the amount of those adjusted lease expenditures remaining after the accounting
13 provided for under this subsection may be used to establish a carried-forward annual
14 loss under AS 43.55.023(b) **or 43.55.165(a)(3)**. **For lease expenditures incurred on**
15 **or after January 1, 2017, a reduction in gross value at the point of production**
16 **under (f) or (g) of this section shall be added back to the calculation of**
17 **production tax value for the determination of a carried-forward annual loss**. In
18 this subsection, "producer" includes "explorer."

19 * **Sec. 39.** AS 43.55.160(e), as amended by sec. 38 of this Act, is amended to read:

20 (e) Any adjusted lease expenditures under AS 43.55.165 and 43.55.170 that
21 would otherwise be deductible by a producer in a calendar year but whose deduction
22 would cause an annual production tax value calculated under (a)(1) or (h) of this
23 section of taxable oil or gas produced during the calendar year to be less than zero
24 may be used to establish a carried-forward annual loss under **AS 43.55.165(a)(3)**
25 **[AS 43.55.023(b) OR 43.55.165(a)(3)]**. However, the department shall provide by
26 regulation a method to ensure that, for a period for which a producer's tax liability is
27 limited by AS 43.55.011(j), (k), (o), or (p), any adjusted lease expenditures under
28 AS 43.55.165 and 43.55.170 that would otherwise be deductible by a producer for that
29 period but whose deduction would cause a production tax value calculated under
30 (a)(1)(C), (D), (E), or (F), or (h)(3) of this section to be less than zero are accounted
31 for as though the adjusted lease expenditures had first been used as deductions in

1 calculating the production tax values of oil or gas subject to any of the limitations
2 under AS 43.55.011(j), (k), (o), or (p) that have positive production tax values so as to
3 reduce the tax liability calculated without regard to the limitation to the maximum
4 amount provided for under the applicable provision of AS 43.55.011(j), (k), (o), or (p).
5 Only the amount of those adjusted lease expenditures remaining after the accounting
6 provided for under this subsection may be used to establish a carried-forward annual
7 loss under AS 43.55.165(a)(3) [AS 43.55.023(b) OR 43.55.165(a)(3)]. For lease
8 expenditures incurred on or after January 1, 2017, a reduction in gross value at the
9 point of production under (f) or (g) of this section shall be added back to the
10 calculation of production tax value for the determination of a carried-forward annual
11 loss. In this subsection, "producer" includes "explorer."

12 * **Sec. 40.** AS 43.55.160(f) is amended to read:

13 (f) On and after January 1, 2014, in the calculation of an annual production tax
14 value of a producer under (a)(1)(A) or (h)(1) of this section, the gross value at the
15 point of production of oil or gas produced from a lease or property north of 68 degrees
16 North latitude meeting one or more of the following criteria is reduced by 20 percent:
17 (1) the oil or gas is produced from a lease or property that does not contain a lease that
18 was within a unit on January 1, 2003; (2) the oil or gas is produced from a
19 participating area established after December 31, 2011, that is within a unit formed
20 under AS 38.05.180(p) before January 1, 2003, if the participating area does not
21 contain a reservoir that had previously been in a participating area established before
22 December 31, 2011; (3) the oil or gas is produced from acreage that was added to an
23 existing participating area by the Department of Natural Resources on and after
24 January 1, 2014, and the producer demonstrates to the department that the volume of
25 oil or gas produced is from acreage added to an existing participating area. This
26 subsection does not apply to gas produced before 2022 that is used in the state or to
27 gas produced on and after January 1, 2022. For oil or gas first produced after
28 December 31, 2016, a reduction allowed under this subsection applies to oil or gas
29 produced from a lease or property for the first 10 years after the commencement
30 of regular production of oil or gas from that lease or property. For oil or gas first
31 produced before January 1, 2017, a reduction allowed under this subsection for a

1 lease or property expires January 1, 2026. The Alaska Oil and Gas Conservation
2 Commission shall determine the commencement of regular production for
3 purposes of this subsection. A reduction under this subsection may not reduce the
4 gross value at the point of production below zero. In this subsection, "participating
5 area" means a reservoir or portion of a reservoir producing or contributing to
6 production as approved by the Department of Natural Resources.

7 * **Sec. 41.** AS 43.55.160(g) is amended to read:

8 (g) On and after January 1, 2014, in addition to the reduction under (f) of this
9 section, in the calculation of an annual production tax value of a producer under
10 (a)(1)(A) or (h)(1) of this section, the gross value at the point of production of oil or
11 gas produced from a lease or property north of 68 degrees North latitude that does not
12 contain a lease that was within a unit on January 1, 2003, is reduced by 10 percent if
13 the oil or gas is produced from a unit made up solely of leases that have a royalty
14 share of more than 12.5 percent in amount or value of the production removed or sold
15 from the lease as determined under AS 38.05.180(f). This subsection does not apply if
16 the royalty obligation for one or more of the leases in the unit has been reduced to 12.5
17 percent or less under AS 38.05.180(j) for all or part of the calendar year for which the
18 annual production tax value is calculated. This subsection does not apply to gas
19 produced before 2022 that is used in the state or to gas produced on and after
20 January 1, 2022. For oil or gas first produced after December 31, 2016, a
21 reduction allowed under this subsection applies to oil or gas produced from a
22 lease or property for the first 10 years after the commencement of regular
23 production of oil or gas from that lease or property. For oil or gas first produced
24 before January 1, 2017, a reduction allowed under this subsection for a lease or
25 property expires January 1, 2026. The Alaska Oil and Gas Conservation
26 Commission shall determine the commencement of regular production for
27 purposes of this subsection. A reduction under this subsection may not reduce the
28 gross value at the point of production below zero.

29 * **Sec. 42.** AS 43.55.165(a) is amended to read:

30 (a) For the [EXCEPT AS PROVIDED IN (j) AND (k) OF THIS SECTION,
31 FOR] purposes of this chapter, a producer's lease expenditures for a calendar year are

1 (1) costs, other than items listed in (e) of this section, that are

2 (A) incurred by the producer during the calendar year after
3 March 31, 2006, to explore for, develop, or produce oil or gas deposits located
4 within the producer's leases or properties in the state or, in the case of land in
5 which the producer does not own an operating right, operating interest, or
6 working interest, to explore for oil or gas deposits within other land in the
7 state; and

8 (B) allowed by the department by regulation, based on the
9 department's determination that the costs satisfy the following three
10 requirements:

11 (i) the costs must be incurred upstream of the point of
12 production of oil and gas;

13 (ii) the costs must be ordinary and necessary costs of
14 exploring for, developing, or producing, as applicable, oil or gas
15 deposits; and

16 (iii) the costs must be direct costs of exploring for,
17 developing, or producing, as applicable, oil or gas deposits; [AND]

18 (2) a reasonable allowance for that calendar year, as determined under
19 regulations adopted by the department, for overhead expenses that are directly related
20 to exploring for, developing, or producing, as applicable, the oil or gas deposits; **and**

21 **(3) lease expenditures incurred in a previous year that**

22 **(A) met the requirements of AS 43.55.160(e) in the year in**
23 **which the lease expenditures were incurred;**

24 **(B) have not been deducted in the determination of the**
25 **production tax value of oil and gas under AS 43.55.160(a) in a previous**
26 **calendar year;**

27 **(C) were not the basis of a credit under this title; and**

28 **(D) were incurred to explore for, develop, or produce oil or**
29 **gas deposits located north of 68 degrees North latitude.**

30 * **Sec. 43.** AS 43.55.165(f) is amended to read:

31 (f) For purposes of **AS 43.55.023(b)** [AS 43.55.023(a) AND (b)] and only as

1 to expenditures incurred to explore for an oil or gas deposit located within land in
2 which an explorer does not own a working interest, the term "producer" in this section
3 includes "explorer."

4 * **Sec. 44.** AS 43.55.170(c) is amended to read:

5 (c) For purposes of AS 43.55.023(b) [AS 43.55.023(a) AND (b)] and only as
6 to expenditures incurred to explore for an oil or gas deposit located within land in
7 which an explorer does not own a working interest, the term "producer" in this section
8 includes "explorer."

9 * **Sec. 45.** AS 43.55.180(a) is amended to read:

10 (a) The department shall study

11 (1) the effects of the provisions of this chapter on oil and gas
12 exploration, development, and production in the state, on investment expenditures for
13 oil and gas exploration, development, and production in the state, on the entry of new
14 producers into the oil and gas industry in the state, on state revenue, and on tax
15 administration and compliance, giving particular attention to the tax rates provided
16 under AS 43.55.011, the tax credits provided under AS 43.55.024, 43.55.025, and
17 former AS 43.55.023 [AS 43.55.023 - 43.55.025], and the deductions for and
18 adjustments to lease expenditures provided under AS 43.55.160 - 43.55.170; and

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

22 * **Sec. 46.** AS 43.55.895(b) is amended to read:

23 (b) A municipal entity subject to taxation because of this section

24 (1) is eligible for [ALL] tax credits proportionate to its production
25 taxable under AS 43.55.011(e); and

26 (2) shall allocate its lease expenditures in proportion to its
27 production taxable under AS 43.55.011(e) [UNDER THIS CHAPTER TO THE
28 SAME EXTENT AS ANY OTHER PRODUCER].

29 * **Sec. 47.** AS 43.55.900 is amended by adding a new paragraph to read:

30 (26) "regular production" has the meaning given in AS 31.05.170.

31 * **Sec. 48.** AS 43.70 is amended by adding new sections to read:

1 **Sec. 43.70.025. Bond or cash deposit required for an oil or gas business. (a)**

2 At the time of applying for a license under this chapter, an applicant engaged in the
3 business of oil or gas exploration, development, or production shall file a surety bond
4 in the amount of \$250,000 running to the state, conditioned upon the applicant's
5 promise to pay

6 (1) taxes and contributions due the state and political subdivisions;

7 (2) persons furnishing labor or material or renting or supplying
8 equipment to the applicant; and

9 (3) costs of repairs to public facilities.

10 (b) In lieu of the surety bond required under this section, the applicant may
11 file with the commissioner a cash deposit or other negotiable security acceptable to the
12 commissioner in the amount of \$250,000.

13 (c) The bond required by this section remains in effect until cancelled by
14 action of the surety, the principal, or, if the commissioner finds that the business is
15 producing oil or gas in commercial quantities, by the commissioner.

16 **Sec. 43.70.028. Claims against an oil or gas business. (a)** A person having a
17 claim against a person required to file a surety bond under AS 43.70.025 because of
18 the failure to pay a liability described in AS 43.70.025(a) may bring suit upon the
19 bond. A copy of the complaint shall be served by registered or certified mail on the
20 commissioner at the time suit is filed, and the commissioner shall maintain a record,
21 available for public inspection, of all suits commenced. This service on the
22 commissioner shall constitute service on the surety, and the commissioner shall
23 transmit the complaint or a copy of it to the surety within 72 hours after it is received.
24 The surety on the bond is not liable in an aggregate amount in excess of that named in
25 the bond, but, if claims pending at any one time exceed the amount of the bond, the
26 claims shall be satisfied from the bond in the following order:

27 (1) material, equipment, and supplies delivered in the state;

28 (2) labor, including employee benefits;

29 (3) taxes and other amounts due to the city and borough, in that order;

30 (4) repair of public facilities;

31 (5) taxes and other amounts due to the state.

1 (b) If a judgment is entered against a cash deposit, the commissioner, upon
2 receipt of a certified copy of a final judgment, shall pay the judgment from the amount
3 of the deposit in accordance with the priorities set out in (a) of this section.

4 (c) An action described in (a) of this section may not be commenced on the
5 bond more than three years after the bond's cancellation.

6 * **Sec. 49.** AS 43.99.950 is amended by adding a new paragraph to read:

7 (3) "outstanding liability to the state" means an amount of tax, interest,
8 penalty, fee, rental, royalty, or other charge for which the state has issued a demand
9 for payment that has not been paid when due and, if contested, has not been finally
10 resolved against the state.

11 * **Sec. 50.** AS 38.05.180(i); AS 41.09.010, 41.09.020, 41.09.030, 41.09.090;
12 AS 43.20.053(j)(4); AS 43.55.023(a), 43.55.023(o), 43.55.025(a)(5), 43.55.025(a)(7),
13 43.55.025(l), 43.55.025(n), 43.55.028(i), 43.55.075(d)(1), 43.55.165(e)(18), 43.55.165(j),
14 43.55.165(k), and 43.55.890(6) are repealed January 1, 2017.

15 * **Sec. 51.** AS 43.55.023(l) and 43.55.023(n) are repealed January 1, 2019.

16 * **Sec. 52.** AS 43.55.023, 43.55.165(f), and 43.55.170(c) are repealed January 1, 2020.

17 * **Sec. 53.** The uncodified law of the State of Alaska is amended by adding a new section to
18 read:

19 LEGISLATIVE WORKING GROUP. (a) A legislative working group is established
20 to analyze the Cook Inlet fiscal regime for oil and gas, review the state's tax structure and
21 rates on oil and gas produced south of 68 degrees North latitude, recommend changes to the
22 legislature for consideration during the First Regular Session of the Thirtieth Alaska State
23 Legislature, and develop terms for a comprehensive fiscal regime to take effect January 1,
24 2019, including,

25 (1) a tax structure that accounts for the unique circumstances for each oil and
26 gas producing area south of 68 degrees North latitude;

27 (2) incentives other than direct monetary support from the state for the
28 exploration, development, and production of oil and gas south of 68 degrees North latitude;

29 (3) consideration of the competitiveness of the area south of 68 degrees North
30 latitude to attract new oil and gas development;

31 (4) consideration of the unique market considerations of the Cook Inlet

1 sedimentary basin and the need to support energy supply security for communities in
2 Southcentral Alaska;

3 (5) alternative means of state support for the exploration, development, and
4 production of oil and gas in the Cook Inlet sedimentary basin, including loan guarantees or
5 other financial support through the Alaska Industrial Development and Export Authority or
6 other state corporation or entity.

7 (b) The working group consists of

8 (1) two co-chairs, one of whom is a member of the house of representatives
9 appointed by the speaker of the house of representatives, and one of whom is a member of the
10 senate appointed by the president of the senate; and

11 (2) members appointed by the co-chairs; members must be legislators and
12 must include members of the majority and minority caucuses.

13 (c) The co-chairs of the working group may form an advisory group to the working
14 group, composed of members who are not legislators and who have expertise and skills to
15 assist in the review and development of a new plan for the tax structure and rates on oil and
16 gas produced south of 68 degrees North latitude. The members of an advisory group may
17 include commissioners or employees of state departments, members of the oil and gas
18 industry or trade associations, and economists.

19 (d) The working group may be supported by legislative consultants under contract
20 through the Legislative Budget and Audit Committee.

21 * **Sec. 54.** The uncodified law of the State of Alaska is amended by adding a new section to
22 read:

23 **APPLICABILITY.** (a) AS 43.55.028(e), as amended by sec. 27 of this Act,
24 AS 43.55.028(j), added by sec. 30 of this Act, and regulations related to a tax credit certificate
25 purchase preference for applicants with a workforce of resident workers, adopted under
26 AS 43.55.028(g), as amended by sec. 29 of this Act, apply to a purchase applied for on or
27 after the effective date of secs. 27, 29, and 30 of this Act.

28 (b) AS 43.55.165(a), as amended by sec. 42 of this Act, applies to lease expenditures
29 calculated for a calendar year after December 31, 2016.

30 * **Sec. 55.** The uncodified law of the State of Alaska is amended by adding a new section to
31 read:

1 TRANSITION: QUALIFIED CAPITAL EXPENDITURES. (a) Notwithstanding the
2 repeal of AS 43.55.023(a) and (o) by sec. 50 of this Act, and the amendments to
3 AS 45.55.023(d) by sec. 16 of this Act, AS 43.55.023(n) by sec. 19 of this Act,
4 AS 43.55.029(a) by sec. 31 of this Act, AS 43.55.030(a) and (e) by secs. 34 and 35 of this
5 Act, AS 43.55.075(b) by sec. 36 of this Act, AS 43.55.165(f) by sec. 43 of this Act, and
6 AS 43.55.170(c) by sec. 44 of this Act, a taxpayer who incurs a qualified capital expenditure
7 before the repeal of AS 43.55.023(a) and (o) by sec. 50 of this Act that qualifies for a
8 qualified capital expenditure credit under AS 43.55.023(a) may apply for a credit or tax credit
9 certificate under AS 43.55.023(d) and, as applicable, assign the tax credit under
10 AS 43.55.029, as those sections read on the day before the repeal of AS 43.55.023(a) by sec.
11 50 of this Act.

12 (b) The Department of Revenue may continue to apply and enforce AS 43.55.023(a)
13 and (o) and 43.55.029, as those sections read on the day before the repeal of AS 43.55.023(a)
14 by sec. 50 of this Act, for qualified capital expenditures incurred before the repeal of
15 AS 43.55.023(a) by sec. 50 of this Act.

16 * **Sec. 56.** The uncodified law of the State of Alaska is amended by adding a new section to
17 read:

18 TRANSITION: WELL LEASE EXPENDITURES. (a) Notwithstanding the repeal of
19 AS 43.55.023(l) and (n) by sec. 51 of this Act, and the amendment of AS 43.55.029(a) by sec.
20 32 of this Act, a taxpayer who incurs a well lease expenditure before the repeal of
21 AS 43.55.023(l) and (n) by sec. 51 of this Act that qualifies for a well lease expenditure credit
22 under AS 43.55.023(l) may apply for a credit or transferable tax credit certificate under
23 AS 43.55.023 and assign the tax credit under AS 43.55.029, as those sections read on the day
24 before the repeal of AS 43.55.023(l) and (n) by sec. 51 of this Act.

25 (b) The Department of Revenue may continue to apply and enforce AS 43.55.023(l),
26 as that subsection read on the day before the repeal of AS 43.55.023(l) by sec. 51 of this Act,
27 for well lease expenditures incurred before the repeal of AS 43.55.023(l) by sec. 51 of this
28 Act.

29 * **Sec. 57.** The uncodified law of the State of Alaska is amended by adding a new section to
30 read:

31 TRANSITION: CARRIED-FORWARD ANNUAL LOSSES. (a) Notwithstanding the

1 repeal of AS 43.55.023, 43.55.165(f), and 43.55.170(c) by sec. 52 of this Act, and the
2 amendments of AS 43.55.029(a) by sec. 33 of this Act, AS 43.55.160(d) by sec. 37 of this
3 Act, and AS 43.55.160(e) by sec. 39 of this Act, a taxpayer who incurs a carried-forward
4 annual loss before the repeal of AS 43.55.023 by sec. 52 of this Act that qualifies for a
5 carried-forward annual loss credit under AS 43.55.023(b) may apply for a credit or tax credit
6 certificate under AS 43.55.023(d) and assign the tax credit under AS 43.55.029, subject to the
7 requirements of AS 43.55.160(d) and (e), as those sections read on the day before the repeal
8 of AS 43.55.023 by sec. 52 of this Act.

9 (b) The Department of Revenue may continue to apply and enforce AS 43.55.023(b),
10 as that section read on the day before the repeal of AS 43.55.023(b) by sec. 52 of this Act, for
11 a carried-forward annual loss incurred before the repeal of AS 43.55.023(b) by sec. 52 of this
12 Act.

13 * **Sec. 58.** The uncodified law of the State of Alaska is amended by adding a new section to
14 read:

15 TRANSITION: AS 43.55.023 CREDITS. Notwithstanding the repeal of
16 AS 43.55.023, 43.55.165(f), and 43.55.170(c) by sec. 52 of this Act, and the amendments to
17 AS 43.55.025(m) by sec. 23 of this Act, AS 43.55.028(a) and (e) by secs. 26 and 28 of this
18 Act, AS 43.55.029(a) by sec. 33 of this Act, AS 43.55.160(d) by sec. 37 of this Act, and
19 AS 43.55.180(a) by sec. 45 of this Act, the Department of Revenue may continue to apply and
20 enforce AS 43.55.023, as that section read on the day before the repeal of AS 43.55.023 by
21 sec. 52 of this Act, for a credit earned before the repeal of AS 43.55.023 by sec. 52 of this
22 Act.

23 * **Sec. 59.** The uncodified law of the State of Alaska is amended by adding a new section to
24 read:

25 TRANSITION: LEASE EXPENDITURES FOR A CALENDAR YEAR AFTER
26 2006 AND BEFORE 2010. Notwithstanding AS 43.55.165(a), as amended by sec. 42 of this
27 Act, and the repeal of AS 43.55.165(j) and (k) by sec. 50 of this Act, AS 43.55.165(j) and (k)
28 apply to a producer's total lease expenditures for a calendar year after 2006 and before 2010
29 under AS 43.55.165, as that section read on the day before the repeal of AS 43.55.165(j) and
30 (k) by sec. 50 of this Act.

31 * **Sec. 60.** The uncodified law of the State of Alaska is amended by adding a new section to

1 read:

2 TRANSITION: EXPLORATION EXPENDITURES AND SEISMIC
3 EXPLORATION EXPENDITURES. (a) Notwithstanding the repeal of AS 43.55.025(a)(5),
4 (a)(7), (l), and (n) by sec. 50 of this Act, a taxpayer who incurs an exploration expenditure or
5 seismic exploration expenditure before the repeal of AS 43.55.025(a)(5), (a)(7), (l), and (n) by
6 sec. 50 of this Act that qualifies for an exploration or seismic exploration expenditure credit
7 under AS 43.55.025(a)(5) or (a)(7) may apply for a credit or production tax credit certificate
8 under AS 43.55.025 and assign the tax credit under AS 43.55.029, as those sections read on
9 the day before the repeal of AS 43.55.025(a)(5), (a)(7), (l), and (n) by sec. 50 of this Act.

10 (b) The Department of Revenue may continue to apply and enforce
11 AS 43.55.025(a)(5), (a)(7), (l), and (n), as those sections read on the day before the repeal of
12 AS 43.55.025(a)(5), (a)(7), (l), and (n) by sec. 50 of this Act, for exploration expenditures and
13 seismic exploration expenditures incurred before the repeal of AS 43.55.025(a)(5), (a)(7), (l),
14 and (n) by sec. 50 of this Act.

15 * **Sec. 61.** The uncodified law of the State of Alaska is amended by adding a new section to
16 read:

17 TRANSITION: REGULATIONS. The Department of Revenue, the Department of
18 Natural Resources, the Department of Commerce, Community, and Economic Development,
19 and the Alaska Oil and Gas Conservation Commission may adopt regulations necessary to
20 implement the changes made by this Act. The regulations take effect under AS 44.62
21 (Administrative Procedure Act), but not before the effective date of the law implemented by
22 the regulation. The Department of Revenue shall adopt regulations governing the use of tax
23 credits under AS 43.55 for a calendar year for which the applicable tax credit provisions of
24 AS 43.55 differ as between parts of the year as a result of this Act.

25 * **Sec. 62.** The uncodified law of the State of Alaska is amended by adding a new section to
26 read:

27 TRANSITION: RETROACTIVITY OF REGULATIONS. Notwithstanding any
28 contrary provision of AS 44.62.240,

29 (1) if the Department of Revenue expressly designates in a regulation that the
30 regulation applies retroactively, a regulation adopted by the Department of Revenue to
31 implement, interpret, make specific, or otherwise carry out this Act may apply retroactively to

1 the effective date of the law implemented by the regulation;

2 (2) if the Department of Natural Resources expressly designates in the
3 regulation that the regulation applies retroactively, a regulation adopted by the Department of
4 Natural Resources to implement, interpret, make specific, or otherwise carry out the statutory
5 amendments in this Act affecting the administration of oil and gas leases issued under
6 AS 38.05.180(f)(3)(B), (D), or (E), to the extent the regulation relates to the treatment of oil
7 and gas production taxes in determining net profits under those leases, may apply
8 retroactively to the effective date of the law implemented by the regulation.

9 * **Sec. 63.** Sections 22, 53, 61, and 62 of this Act take effect immediately under
10 AS 01.10.070(c).

11 * **Sec. 64.** Sections 32, 51, and 56 of this Act take effect January 1, 2019.

12 * **Sec. 65.** Sections 23, 26, 28, 33, 37, 39, 45, 52, 57, and 58 of this Act take effect
13 January 1, 2020.

14 * **Sec. 66.** Except as provided in secs. 63 - 65 of this Act, this Act takes effect January 1,
15 2017.

Fiscal Note

State of Alaska
2016 Legislative Session

Bill Version: HB 247
Fiscal Note Number: _____
() Publish Date: _____

Identifier: HB247CS(RLS)-DOR-TAX-05-10-16
Title: TAX;CREDITS;INTEREST;REFUNDS;O & G
Sponsor: RLS BY REQUEST OF THE GOVERNOR
Requester: House Rules Committee

Department: Department of Revenue
Appropriation: Taxation and Treasury
Allocation: Tax Division
OMB Component Number: 2476

Expenditures/Revenues

Note: Amounts do not include inflation unless otherwise noted below. (Thousands of Dollars)

	FY2017 Appropriation Requested	Included in Governor's FY2017 Request	Out-Year Cost Estimates					
			FY 2017	FY 2018	FY 2019	FY 2020	FY 2021	FY 2022
OPERATING EXPENDITURES								
Personal Services								
Travel								
Services								
Commodities								
Capital Outlay								
Grants & Benefits								
Miscellaneous								
Total Operating	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0

Fund Source (Operating Only)

None								
Total	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0

Positions

Full-time								
Part-time								
Temporary								

Change in Revenues	0.0		2,500.0	7,500.0	82,500.0	82,500.0	105,000.0
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Estimated SUPPLEMENTAL (FY2016) cost: 0.0 *(separate supplemental appropriation required)*
(discuss reasons and fund source(s) in analysis section)

Estimated CAPITAL (FY2017) cost: 1,200.0 *(separate capital appropriation required)*
(discuss reasons and fund source(s) in analysis section)

ASSOCIATED REGULATIONS

Does the bill direct, or will the bill result in, regulation changes adopted by your agency? yes
If yes, by what date are the regulations to be adopted, amended or repealed? 01/01/17

Why this fiscal note differs from previous version:

Revised to conform to changes in the Rules Committee Substitute, version D. This document only includes the revenue raising numbers, with any program expenditure savings being captured in the companion FUNDCAP fiscal note.

Prepared By: Dan Stickel, Assistant Chief Economist
Division: Tax Division
Approved By: Jerry Burnett, Deputy Commissioner
Agency: Department of Revenue

Phone: (907)465-3279
Date: 05/10/2016 04:30 PM
Date: 05/10/16

FISCAL NOTE ANALYSIS

STATE OF ALASKA
2016 LEGISLATIVE SESSION

BILL NO. HB 247

Analysis

Bill Background

This legislation is a comprehensive attempt to reform and reduce the cost of Alaska's current program of providing direct tax credit rebates and other advantages to oil and gas companies. Various credits have been added to statute since 2003, with state repurchase beginning in 2007. Through the end of FY 2016, about \$8 billion in tax credits will be received by companies. This includes both credits used against tax liability and credits repurchased by the state; it also includes activity on both the North Slope and other areas of the state.

A substantial number of companies rely on these credits to support and subsidize their Alaska operations. For work done in 2015, in many cases the state is paying 55%-65% of the cost of a project during the development phase, and up to 85% of exploration costs. These large numbers result from "stacking" multiple credits. With the transition towards a system based mostly on state support through deductible lease expenditures, the state's contribution towards many projects will be reduced by 50% or more.

The Administration identified several themes, or goals, of this legislation as originally introduced. These include: (1) Reduce the state's annual cash outlay; (2) Protect Net Operating Loss credits especially for exploration activity; (3) Limit repurchases to companies who need the support; (4) Strengthen the minimum tax and prevent abuses to the system; (5) Be more open and transparent; and (6) Honor and pay credits earned to date and through any transition period. To address this final point, this legislation envisions a fund capitalization appropriation to cover any tax credits earned through the effective date. Savings due to reductions in future appropriations needed to repurchase tax credits will be captured in the separate fund capitalization fiscal note.

Summary of Fiscal Impact

With the revisions proposed in the Rules Committee substitute, we anticipate additional revenue of up to \$105 million per year over the time period contained in the fiscal note. No additional revenue is expected in FY17, due to the phased implementation of various bill provisions, and the expectation that major producers will be able to apply credits earned prior to the effective date of this bill against tax payments in FY17-19.

Once fully implemented, the majority of the revenue impacts from this bill for the North Slope will be due to the strengthening of the so-called minimum tax "floor," via elimination of the net operating loss credits that can now be applied against a tax liability. Instead, companies would be required to carry forward lease expenditures to a future tax liability. In the Cook Inlet, the revenue impacts from this bill will be due to elimination of the net operating loss, capital expenditure, and well lease expenditure credits; companies in the Cook Inlet will also not be allowed to carry forward lease expenditures.

A small indeterminate amount of additional revenue would come from the restoration of compound interest and an increase in the interest rate for assessed delinquent taxes.

Implementation Cost

The changes anticipated in this bill will require somewhat substantial reprogramming of the Tax Revenue Management System and Revenue Online tax portal. We have received a preliminary estimate from the software developer, which allows us to reduce our one-time cost to about \$1,200,000 to accomplish these changes. We do not anticipate any additional costs to administer the tax program.

There will also be a need for substantial amendments to existing regulations to fully implement the changes.

FISCAL NOTE ANALYSIS

STATE OF ALASKA
2016 LEGISLATIVE SESSION

BILL NO. HB 247

Analysis Continued

Detail of Specific Provisions

1) Repeal of certain credits and closing of loopholes

For areas outside the North Slope (Cook Inlet and Middle Earth), the Rules committee substitute reduces the Well Lease Expenditure credit from 40% to 20% effective 1/1/17, then eliminates the credit effective 1/1/19. The Qualified Capital Expenditure Credit is eliminated effective 1/1/17, as is the "maintenance reduction" that disallows the first 30 cents per barrel of lease expenditures. Additionally, the Carried Forward Annual Loss (or "Net Operating Loss") credit is eliminated effective 1/1/18. The net effect of these changes will be to reduce state contribution for new Cook Inlet projects from the current 45-65% range to zero beginning in 2019. However, this bill creates a legislative working group and envisions crafting a new Cook Inlet tax regime to take effect in 2019.

For the North Slope, the Rules committee substitute eliminates the Carried Forward Annual Loss credit effective 1/1/17 with a 3-year transition period for non-producers undertaking a DNR-approved plan of development or companies with less than 15,000 barrels per day of production. After 1/1/17 (or the 3-year transition period), a company may carry forward any lease expenditures that exceed their Gross Value at Point of Production, and apply those in calculating a subsequent year's tax liability. Unlike the current credits, these carry forward lease expenditures could not be used to reduce a tax payment below the minimum tax; however other credits could still be used to reduce a tax payment below the minimum tax.

Although we are not forecasting changes to behavior in this analysis, it is reasonable to expect that certain companies who are years from production and tax liability may be less inclined to make investments given the state's reduced support for those investments and the reduced ability to monetize what support remains.

The bill also eliminates a provision of current law that enables companies with "new oil" production on the North Slope and a net operating loss to use a Gross Value Reduction to increase the size of a net operating loss credit. It also eliminates another loophole that has been used by municipal utilities who also own oil or gas production. If a portion of that production is sold to an outside party, the proposed change ensures that these entities are only able to deduct or claim a pro-rated portion of their lease expenditures for the purpose of applying for credits.

2) Deferral or loss of eligibility for credit repurchase

Currently any company with less than 50,000 bbl / day of production in Alaska is eligible to have tax credit certificates repurchased by the state without limit, subject to appropriation. This bill adds an additional restriction to repurchase, so that no single company can receive more than \$75 million per year in state cash repurchases. Although this would not have any impact based on currently forecasted activity and other provisions of this bill, it provides an element of protection from large "outlier" projects that could otherwise result in large credit liability.

3) Other changes

In the CS, the "gross value reduction" for new oil only applies for the first ten years of production, and is lost on 1/1/26 for fields currently receiving that reduction. Additionally, the bill restores quarterly compound interest for delinquent taxes, underpayments, and tax assessments. Current statute has included simple interest since 2014, which is believed to be an inadvertent amendment made in SB21. The interest rate is increased from 3% above the federal discount rate to 5% above.

There is a small extension to a Frontier Areas exploration credit to enable wells in the Copper River basin that are in-process by 1/1/17 to be completed under the program before it sunsets. The committee substitute also repeals several older and currently unused exploration incentive credit programs, and authorizes the Department of Revenue to use credit certificates to offset a company's other obligations to the state prior to repurchase. It also establishes a legislative working group to review the state's tax structure for Cook Inlet and other areas outside the North Slope, to provide

Analysis Continued

Fiscal Detail of CSHB247(RLS)\D (Revenue and Budget Impacts)

Revised 5-10-16 by Department of Revenue

CSHB247(RLS)\D

Provisions in CSHB 247 (RLS) and their Estimated Fiscal Impact as compared to Spring 2016 Forecast (\$millions) - FORECAST PRICE¹

Note: this table attempts to value the impact of each of the items independently, except where noted. In some cases, the total value of several impacts will not equal the sum of the individual impact values.

Brief Description of Provision - Includes only provisions anticipated to have a direct fiscal impact	FY 2017	FY 2018	FY 2019	FY 2020	FY 2021	FY 2022	FY 2023	FY 2024	FY 2025
1. Cook Inlet changes: The QCE credit is eliminated 1/1/17. The well lease expenditure credit is reduced to 20% on 1/1/17 but then eliminated on 1/1/19. The net operating loss credit is eliminated effective 1/1/18. The 30 cent per barrel "maintenance reduction" from allowable lease expenditures is eliminated 1/1/17.	\$0	\$0-\$5	\$5-\$10	\$10-\$15	\$10-\$15	\$30-\$40	\$30-\$40	\$30-\$40	\$30-\$40
2. North Slope changes: The net operating loss credit for North Slope is eliminated effective 1/1/17; lease expenditures not used in a calendar year may be carried forward effective 1/1/17; 3-year transition period for refunds at 35% of loss for companies with less than 15,000 barrels per day of production, or with no production but under a DNR approved plan of exploration or development. GVR cannot be used to create or increase a net operating loss; 30 cent per barrel "maintenance reduction" from allowable lease expenditures is eliminated 1/1/17.	\$0	\$0	\$0	\$60-\$80	\$60-\$80	\$60-\$80	\$40-\$60	\$40-\$60	(\$10)-\$0
3. GVR-eligible production qualifies for the GVR for a period of 10 years or until 1/1/26.	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0
4. The interest rate on delinquent taxes is changed to 5% above the Fed Res Discount rate, compounded quarterly	Indeterminate								
5. A tax exempt entity may earn credits applicable to only those lease expenditures subject to tax	Indeterminate								
Total Revenue Impact	\$0	\$0 to \$5	\$5 to \$10	\$70 to \$95	\$70 to \$95	\$90 to \$120	\$70 to \$100	\$70 to \$100	\$20 to \$40
A. Budget impact of change in net operating loss credits, and QCE/WLE credits for Cook Inlet (provision 1 above)	\$0-\$10	\$25-\$35	\$40-\$50	\$40-\$50	\$100-\$125	\$100-\$125	\$75-\$100	\$75-\$100	\$75-\$100
B. Budget impact of change in net operating loss credits, lease expenditures applicability, and GVR calculation for North Slope (provision 2 above)	\$0	\$10-\$20	\$25-\$35	\$40-\$50	\$100-\$125	\$100-\$125	\$125-\$150	\$125-\$150	\$125-\$150
C. Budget impact of exploration credit extension in Copper River Basin for well spudded by 1/1/17.	(\$5)-\$0	(\$5)-\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0
D. Budget impact of GVR applying to fields for a period of 10 years (provision 3 above)	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0
E. Budget impact of limiting refunds to \$75 million per company per year (only shifts timing of refunds - impact is after all other provisions of bill)	No impact under forecast when combined with other provisions of bill.								
Total Budget Impact	(\$5) to \$10	\$30 to \$55	\$65 to \$85	\$80 to \$100	\$200 to \$250	\$200 to \$250	\$200 to \$250	\$200 to \$250	\$200 to \$250
Total Fiscal Impact - does not include revenue impacts from potential changes in investment²	(\$5) to \$10	\$30 to \$60	\$70 to \$95	\$150 to \$195	\$270 to \$345	\$290 to \$370	\$270 to \$350	\$270 to \$350	\$220 to \$290
Non-refundable carry-forward credits balance at fiscal year end - current law ³	\$618	\$751	\$732	\$585	\$265	\$136	\$59	\$0	\$0
Non-refundable carry-forward credits balance (or equivalent) at fiscal year end - proposed ³	\$610	\$720	\$660	\$685	\$635	\$630	\$640	\$665	\$715
Change in year-end balance due to bill	-\$8	-\$31	-\$72	\$100	\$370	\$494	\$581	\$665	\$715

¹The impacts listed are based on production and prices and company investment as forecasted in DOR's Spring 2016 revenue forecast. The forecasted oil prices are between \$38.89 and \$65.90.

²NOTE: "Total Fiscal Impact" includes best estimates of both revenue and operating budget impacts.

³These rows include estimates of carried-forward credits, and carried-forward lease expenditures, for previous calendar years, plus estimates of credits and carried-forward lease expenditures that will be earned on activity through June 30 of the fiscal year. For carried-forward lease expenditures, the balance shown is the credit-equivalent value of those expenditures assuming a 35% tax rate (for example, \$100 million of carried-forward lease expenditures equate to \$35 million of credits).

NOTE: The fiscal impact of this bill is an estimate based on the Spring 2016 revenue forecast. Estimates shown here are draft / preliminary based on our interpretation of possible changes. We reserve the right to make modifications to estimates for any forthcoming fiscal notes.

Fiscal Note

State of Alaska
2016 Legislative Session

Bill Version: HB 247
Fiscal Note Number: _____
() Publish Date: _____

Identifier: HB247 (HRLS) Fund Cap 5-10-16
Title: TAX;CREDITS;INTEREST;REFUNDS;O & G
Sponsor: RLS BY REQUEST OF THE GOVERNOR
Requester: House Rules

Department: Fund Capitalization
Appropriation: Fund Capitalization (no approps out)
Allocation: Oil and Gas Tax Credit Fund
OMB Component Number: 2894

Expenditures/Revenues

Note: Amounts do not include inflation unless otherwise noted below. (Thousands of Dollars)

	FY2017	Included in	Out-Year Cost Estimates				
	Appropriation Requested	Governor's FY2017 Request	FY 2018	FY 2019	FY 2020	FY 2021	FY 2022
OPERATING EXPENDITURES	FY 2017	FY 2017					
Personal Services							
Travel							
Services							
Commodities							
Capital Outlay							
Grants & Benefits	1,750,000.0	73,425.0					
Miscellaneous							
Total Operating	1,750,000.0	73,425.0	0.0	0.0	0.0	0.0	0.0

Fund Source (Operating Only)

1001 CBR Fund	1,750,000.0						
1004 Gen Fund		73,425.0					
Total	1,750,000.0	73,425.0	0.0	0.0	0.0	0.0	0.0

Positions

Full-time							
Part-time							
Temporary							

Change in Revenues							
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Estimated SUPPLEMENTAL (FY2016) cost: 0.0 *(separate supplemental appropriation required)*
(discuss reasons and fund source(s) in analysis section)

Estimated CAPITAL (FY2017) cost: 0.0 *(separate capital appropriation required)*
(discuss reasons and fund source(s) in analysis section)

ASSOCIATED REGULATIONS

Does the bill direct, or will the bill result in, regulation changes adopted by your agency?
If yes, by what date are the regulations to be adopted, amended or repealed?

Why this fiscal note differs from previous version:

This fiscal note appropriates \$1.75 billion from the Constitutional Budget Reserve to the Oil & Gas Tax Credit Fund. The amount is intended to pay for tax credit claims through FY25. This appropriation requires a supermajority vote in each body.

Prepared By: Representative Johnson
House Rules Committee

Phone: (907)465-4993
Date: 05/10/2016

FISCAL NOTE ANALYSIS

STATE OF ALASKA
2016 LEGISLATIVE SESSION

BILL NO. HB 247

Analysis

This fiscal note capitalizes the Oil and Gas Tax Credit Fund with \$1.75 billion from the Constitutional Budget Reserve Fund. This appropriation is expected to be sufficient to fully pay out tax credits that have already been earned and that will be earned during the phase-out period of the bill. As shown in the table on the following page, HB 247 is projected to reduce credits from \$3.2 billion to \$1.8 billion through FY25, reducing State payments by \$1.3 billion during that period.

Sections 10-12 of the bill eliminate the ability of DOR to pay three tax credits out of the .028 fund that is used to pay out production tax credits. These three credits (the refinery tax credit, the LNG storage facility credit, and the gas storage facility credit) are against the corporate income tax, not the production tax, but they can currently be refunded like a production tax credit. This change would mean that DOR would need a new appropriation to pay out those credits. The tax credit fund would remain for production tax credits, but this would clearly separate the production tax credits from the corporate income tax credits.

This version of HB 247 eliminates net annual loss (NOL) credits after FY16 and replaces them with the ability to carry forward lease expenditures. That means that taxpayers would still have their FY16 NOL balance (about \$600 million) available to use to reduce their production tax liability to zero in FY17 and a couple of years beyond, but they would not be earning additional NOLs in those years. Instead, they can carry forward their unused lease expenditures. Those lease expenditures could be applied to future tax years to bring them down to the minimum tax. The balance shown at the bottom of DOR's analysis on the fourth page of this fiscal note shows over \$2 billion of those carried forward lease expenditures. However, the potential reduction in taxpayer liability would only be about 35% of those amounts.

Impact of HB 247 on Oil and Gas Tax Credits (\$ millions)									
	FY17	FY18	FY19	FY20	FY21	FY22	FY23	FY24	FY25
Projected Credits--No Action (1)	775	500	375	270	250	250	250	250	250
Cumulative Credits	775	1,275	1,650	1,920	2,170	2,420	2,670	2,920	3,170
Projected Impact of HB 247 (2)									
Low	5	(30)	(65)	(80)	(200)	(200)	(200)	(200)	(200)
High	(10)	(55)	(85)	(100)	(250)	(250)	(250)	(250)	(250)
Average	(3)	(43)	(75)	(90)	(225)	(225)	(225)	(225)	(225)
Net Credit Claims under HB 247									
Net Credit Claims under HB 247	773	458	300	180	25	25	25	25	25
Cumulative Claims	773	1,230	1,530	1,710	1,735	1,760	1,785	1,810	1,835
Change in Costs under HB 247									
Change in Costs under HB 247	(3)	(43)	(75)	(90)	(225)	(225)	(225)	(225)	(225)
Cumulative Change	(3)	(45)	(120)	(210)	(435)	(660)	(885)	(1,110)	(1,335)
(1) Source: DOR Spring 2016 Revenue Sources Book									
(2) Source: DOR analysis included in this fiscal note									

Analysis Continued

Fiscal Detail of CSHB247(RLS)\D (Revenue and Budget Impacts)

Revised 5-10-16 by Department of Revenue

CSHB247(RLS) \D

Provisions in CSHB 247 (RLS) and their Estimated Fiscal Impact as compared to Spring 2016 Forecast (\$millions) - FORECAST PRICE¹

Note: this table attempts to value the impact of each of the items independently, except where noted. In some cases, the total value of several impacts will not equal the sum of the individual impact values.

Brief Description of Provision - Includes only provisions anticipated to have a direct fiscal impact	FY 2017	FY 2018	FY 2019	FY 2020	FY 2021	FY 2022	FY 2023	FY 2024	FY 2025
1. Cook Inlet changes: The QCE credit is eliminated 1/1/17. The well lease expenditure credit is reduced to 20% on 1/1/17 but then eliminated on 1/1/19. The net operating loss credit is eliminated effective 1/1/18. The 30 cent per barrel "maintenance reduction" from allowable lease expenditures is eliminated 1/1/17.	\$0	\$0-\$5	\$5-\$10	\$10-\$15	\$10-\$15	\$30-\$40	\$30-\$40	\$30-\$40	\$30-\$40
2. North Slope changes: The net operating loss credit for North Slope is eliminated effective 1/1/17; lease expenditures not used in a calendar year may be carried forward effective 1/1/17; 3-year transition period for refunds at 35% of loss for companies with less than 15,000 barrels per day of production, or with no production but under a DNR approved plan of exploration or development. GVR cannot be used to create or increase a net operating loss; 30 cent per barrel "maintenance reduction" from allowable lease expenditures is eliminated 1/1/17.	\$0	\$0	\$0	\$60-\$80	\$60-\$80	\$60-\$80	\$40-\$60	\$40-\$60	(\$10)-\$0
3. GVR-eligible production qualifies for the GVR for a period of 10 years or until 1/1/26.	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0
4. The interest rate on delinquent taxes is changed to 5% above the Fed Res Discount rate, compounded quarterly	Indeterminate								
5. A tax exempt entity may earn credits applicable to only those lease expenditures subject to tax	Indeterminate								
Total Revenue Impact	\$0	\$0 to \$5	\$5 to \$10	\$70 to \$95	\$70 to \$95	\$90 to \$120	\$70 to \$100	\$70 to \$100	\$20 to \$40
A. Budget impact of change in net operating loss credits, and QCE/WLE credits for Cook Inlet (provision 1 above)	\$0-\$10	\$25-\$35	\$40-\$50	\$40-\$50	\$100-\$125	\$100-\$125	\$75-\$100	\$75-\$100	\$75-\$100
B. Budget impact of change in net operating loss credits, lease expenditures applicability, and GVR calculation for North Slope (provision 2 above)	\$0	\$10-\$20	\$25-\$35	\$40-\$50	\$100-\$125	\$100-\$125	\$125-\$150	\$125-\$150	\$125-\$150
C. Budget impact of exploration credit extension in Copper River Basin for well spudded by 1/1/17.	(\$5)-\$0	(\$5)-\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0
D. Budget impact of GVR applying to fields for a period of 10 years (provision 3 above)	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0
E. Budget impact of limiting refunds to \$75 million per company per year (only shifts timing of refunds - impact is after all other provisions of bill)	No impact under forecast when combined with other provisions of bill.								
Total Budget Impact	(\$5) to \$10	\$30 to \$55	\$65 to \$85	\$80 to \$100	\$200 to \$250	\$200 to \$250	\$200 to \$250	\$200 to \$250	\$200 to \$250
Total Fiscal Impact - does not include revenue impacts from potential changes in investment²	(\$5) to \$10	\$30 to \$60	\$70 to \$95	\$150 to \$195	\$270 to \$345	\$290 to \$370	\$270 to \$350	\$270 to \$350	\$220 to \$290
Non-refundable carry-forward credits balance at fiscal year end - current law ³	\$618	\$751	\$732	\$585	\$265	\$136	\$59	\$0	\$0
Non-refundable carry-forward credits balance (or equivalent) at fiscal year end - proposed ³	\$610	\$720	\$660	\$685	\$635	\$630	\$640	\$665	\$715
Change in year-end balance due to bill	-\$8	-\$31	-\$72	\$100	\$370	\$494	\$581	\$665	\$715

¹The impacts listed are based on production and prices and company investment as forecasted in DOR's Spring 2016 revenue forecast. The forecasted oil prices are between \$38.89 and \$65.90.

²NOTE: "Total Fiscal Impact" includes best estimates of both revenue and operating budget impacts.

³These rows include estimates of carried-forward credits, and carried-forward lease expenditures, for previous calendar years, plus estimates of credits and carried-forward lease expenditures that will be earned on activity through June 30 of the fiscal year. For carried-forward lease expenditures, the balance shown is the credit-equivalent value of those expenditures assuming a 35% tax rate (for example, \$100 million of carried-forward lease expenditures equate to \$35 million of credits).

NOTE: The fiscal impact of this bill is an estimate based on the Spring 2016 revenue forecast. Estimates shown here are draft / preliminary based on our interpretation of possible changes. We reserve the right to make modifications to estimates for any forthcoming fiscal notes.



ALASKA STATE LEGISLATURE HOUSE RULES COMMITTEE

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Summary of \D version

The D version work draft closes out the state's tax credit program between Jan. 1, 2017, and Jan. 1, 2020, except for the Middle Earth 40% exploration credit that sunsets Jan.1, 2022. In phasing out the net operating loss carry-forward credit on the North Slope, the bill implements a system of carrying forward lease expenditures that a business is unable to deduct in the current year. This transition has the effect of hardening the gross minimum tax floor against losses.

Statewide:

- No more than \$75 million per company in credits cashed back, per year.
- Refunds are prioritized to companies with at least 80% Alaska hire.
- Disclosure of some information to the public: the Department of Revenue will make public, annually, the name of a company receiving refunds for credits, as well as the total dollars refunded to the company for the year.
- Outstanding liability – providing a liability is not contested through an official process, DOR can apply a withheld credit against a liability without the taxpayer's consent.
- Includes requirement for a \$250,000 surety bond and provisions for prioritizing claims.
- Municipal producers must allocate lease expenditure to taxable production, so credits are not received/earned for nontaxable production.
- The income tax credits for the instate refinery and LNG storage facilities remain in statute, but as those are not oil and gas production tax-related credits, they are no longer refundable from the Oil and Gas Tax Credit Fund. They are refundable by the Department of Revenue generally (through annual appropriation).
- Interest rates increase from 3 points above the federal discount rate in current statute, simple interest, to five points above, compounding quarterly.
- The gross tax assessed on royalties paid to private landowners may never be less than zero.

Specific to Cook Inlet and Middle Earth:

Cook Inlet and Middle Earth credits terminate Jan. 1, 2019. Middle Earth retains an exploration credit through 2021. A new fiscal regime will be developed for Cook Inlet and Middle Earth.

- For 2016, all credits currently in statute continue: 20% QCE, 40% WLE, 25% NOL
- In order to receive any credits for Cook Inlet work from Jan. 1, 2017, forward, a company must have oil or gas production in Cook Inlet in calendar year 2016.

- For 2017, the 20% QCE credit is repealed. Companies are eligible for a 20% well lease expenditure credit, and for a 25% NOL credit; the 25% NOL credit terminates at the end of 2017.
- For 2018, companies are eligible for a 20% well lease expenditure credit only; this credit terminates at the end of 2018.
- Legislative working group with tighter language, being explicit that the new fiscal regime to be developed would take effect with the expiration of credits, in Jan. 1, 2019.
- There is an additional benefit for Middle Earth; this is the extension of the .025(a)(6) credit in the Copper River Basin only; the credit applies to work done before Jan. 1, 2017, except that a well spudded but not yet completed by Jan. 1, 2017, is eligible.
- And, for Middle Earth, this bill does not change the Jan. 1, 2022 sunset of the Middle Earth exploration credit.

Specific to the North Slope:

North Slope credits terminate Jan. 1, 2017; but, as a transition measure, for three years the state will continue offering a 35% net operating loss carry-forward refundable credit, up to \$75 million per year, for small producers with less than 15,000 barrels per day average production in 2016; or, for producers who are operating in a unit with an approved plan of development or plan of exploration. The net profits system defining principle of allowing a company to recover its losses is retained by transitioning to a carry-forward of lease expenditures that a company was unable to deduct in the current year. This transition also hardens the 4% gross minimum floor against losses.

- The 35% NOL credit terminates at the end of 2016 for companies producing more than 15,000 barrels per day. Companies producing oil or gas on the North Slope in calendar year 2016, up to 15,000 barrels per day, and companies without production but working under a unit with an approved plan of development or plan of exploration, continue to receive the 35% refundable NOL through 2019.
- Except for those smallest producers and new developers, the NOL no longer applies. Instead, companies with more than 15,000 barrels per day production will be able to carry forward lease expenditures they were unable to deduct in the current year. Changing the NOL from a credit to carry-forward lease expenditure deductions hardens the 4% gross minimum floor; unlike credits, deductions cannot reduce production tax value below the gross minimum tax.
- The GVR reduction for new oil goes from a timeless benefit under current statute, to a 10-year benefit once regular production starts. The new oil per-barrel-credit also applies only while the new oil is receiving the GVR. Once new oil 'graduates' into normal oil after 10 years, and no longer receives the new-oil benefits, it is taxed as any other normal oil and is eligible for the sliding scale per-barrel reduction, like all normal oil.
- Previous bill versions have all included a provision to prevent the use of the GVR from increasing the amount of a loss. This bill retains that provision.



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2d CS for House Bill 247 () Version \D

- Section 1 Adds a new subsection to AS 31.05.030, Alaska Oil and Gas Conservation Act. Requires the Alaska Oil and Gas Conservation Commission to verify the start of regular production of new oil. Effective Jan. 1, 2017.
- Secs. 2-6 Amend AS 38.05.036 (a), (b), (c), (f) and (g), Alaska Land Act, Audit of royalty and net profit payments and costs. Conforming to the Section 50 repeal of AS 41.09, an old Department of Natural Resources exploration credit program. Effective Jan. 1, 2017.
- Section 7 Amends AS 40.25.100(a), Public Record Disclosures, Disposition of tax information. Conforming to Section 9, which requires the Department of Revenue to make public some taxpayer information. Effective Jan. 1, 2017.
- Section 8 Amends AS 43.05.225, Administration of Revenue Laws, Interest. The interest rate on delinquent taxes is five points above the 12th Federal Reserve District rate, compounded quarterly. Effective Jan. 1, 2017.
- Section 9 Adds a new subsection to AS 43.05.230, Administration of Revenue Laws, Disclosure of tax returns and reports. Requires the Department of Revenue to make public by April 30 of each year, the name of a company from whom the department purchases a tax credit certificate and the total amount of tax credit certificates purchased from each company. Effective Jan. 1, 2017.
- Section 10 Amends AS 43.20.046(e), Alaska Net Income Tax Act, Gas storage facility tax credit. The Department of Revenue will no longer use the Oil and Gas Tax Credit Fund to refund gas storage facility credits. The credits remain refundable by DOR. Also, definition of "unpaid delinquent taxes" is removed, as a new definition for "outstanding liability" applicable to AS Title 43, Revenue and Taxation, is added in Section 49. Effective Jan. 1, 2017.
- Section 11 Amends AS 43.20.047(e), Alaska Net Income Tax Act, Liquefied natural gas storage facility tax credit. The Department of Revenue will no longer use the Oil and Gas Tax Credit Fund to refund LNG storage facility credits. The credits remain refundable by DOR. Also, definition of "unpaid delinquent taxes" is removed, as a new definition for "outstanding liability" applicable to AS Title 43, Revenue and Taxation, is added in Section 49. Effective Jan. 1, 2017.

- Section 12 Amends AS 43.20.053(e), Alaska Net Income Tax Act, Qualified in-state oil refinery infrastructure expenditures tax credit. The Department of Revenue will no longer use the Oil and Gas Tax Credit Fund to refund instate refinery credits. The credits remain refundable by DOR. Also, reference to “unpaid delinquent taxes” is removed, as a new definition for “outstanding liability” applicable to AS Title 43, Revenue and Taxation, is added in Section 49. Effective Jan. 1, 2017.
- Section 13 Amends AS 43.55.011(i), Oil and Gas Production Tax. Ensures the tax assessed on private royalties is not less than zero. Effective Jan. 1, 2017.
- Section 14 Amends AS 43.55.011(m), Oil and Gas Production Tax. Conforming to the Section 50 repeal of the DNR credit programs in AS 38.05.180(i) and AS 41.09. Effective Jan. 1, 2017.
- Section 15 Amends AS 43.55.023(b), Oil and Gas Production Tax, Tax credits for certain losses and expenditures. The 35% net operating loss credit on the North Slope terminates at the end of 2016, except the 35% credit (refundable) is available through 2019 for companies producing less than 15,000 barrels per day in 2016, and for companies without production operating under a unit plan of development or plan of exploration approved by the Department of Natural Resources. The 25% net operating loss credit in areas other than the North Slope remains at 25% in 2017, then terminates. To receive the credit in Cook Inlet, a company must have regular production of oil or gas in Cook Inlet in calendar year 2016. Also, ensures that the application of a gross value reduction for new oil cannot increase the size of a loss. Effective Jan. 1, 2017.
- Section 16 Amends AS 43.55.023(d), Oil and Gas Production Tax, Tax credits for certain losses and expenditures. Conforms to the Section 50 repeal of AS 43.55.023(a), qualified capital expenditure credit. Effective Jan. 1, 2017.
- Section 17 Amends AS 43.55.023(e), Oil and Gas Production Tax, Tax credits for certain losses and expenditures. Conforms to the Section 50 repeal of AS 43.55.023(a), qualified capital expenditure credit. Effective Jan. 1, 2017.
- Section 18 Amends AS 43.55.023(l), Oil and Gas Production Tax, Tax credits for certain losses and expenditures. Reduces the well lease expenditure credit from 40% through 2016, to 20% in calendar years 2017 and 2018. To receive this credit in Cook Inlet, the producer must have regular oil or gas production in Cook Inlet in 2016. Effective Jan. 1, 2017.
- Section 19 Amends AS 43.55.023(n), Oil and Gas Production Tax, Tax credits for certain losses and expenditures. Conforms to the Section 50 repeal of AS 43.55.023(a), qualified capital expenditure credit. Effective Jan. 1, 2017.

- Section 20 Amends AS 43.55.024(i), Oil and Gas Production Tax, Additional nontransferable tax credits. Companies may apply the \$5 per-barrel new oil credit only for oil receiving the 10-year gross value reduction. Effective Jan. 1, 2017.
- Section 21 Amends AS 43.55.024(j), Oil and Gas Production Tax, Additional nontransferable tax credits. Once new oil is no longer eligible for new oil benefits and is being taxed as normal oil, the oil is also eligible for the sliding-scale per-barrel credit. Effective Jan. 1, 2017.
- Section 22 Amends AS 43.55.025(m), Oil and Gas Production Tax, Alternative tax credit for oil and gas exploration. Extends a Middle Earth credit for work in the Copper River Basin only, to Jan. 1, 2017. A company that has spudded but not completed a well by Jan. 1, 2017, is also eligible. The AS 43.55.025(a)(6) credit covers 80% of eligible costs, up to \$25 million. Effective immediately.
- Section 23 Amends AS 43.55.025(m), Oil and Gas Production Tax, Alternative tax credit for oil and gas exploration, as amended by Section 22. Conforming to the Section 52 repeal of AS 43.55.023. Effective Jan. 1, 2020.
- Section 24 Amends AS 43.55.025(o), Oil and Gas Production Tax, Alternative tax credit for oil and gas exploration. Conforms to the Section 50 repeal of AS 43.55.025 (a)(7) and (n). Effective Jan. 1, 2017.
- Section 25 Amends AS 43.55.028(a), Oil and Gas Production Tax, Oil and gas tax credit fund. Removes the authority to use the fund to pay refunds for the income tax credits related to the instate refinery, LNG storage facility, and gas storage facility. Effective Jan. 1, 2017.
- Section 26 Amends AS 43.55.028(a), Oil and Gas Production Tax, Oil and gas tax credit fund, as amended by Sec. 25. Conforming to the Section 52 repeal of AS 43.55.023. Effective Jan. 1, 2020.
- Section 27 Amends AS 43.55.028(e), Oil and Gas Production Tax, Oil and gas tax credit fund. Limits the maximum state repurchase of tax credits to \$75 million per company, per year. Requires the Department of Revenue to, before purchasing credit certificates, find that the applicant is not the result of the division of a single entity into multiple entities that would reasonably have been expected to apply as a single entity. Effective Jan. 1, 2017.
- Section 28 Amends AS 43.55.028(e), Oil and Gas Production Tax, Oil and gas tax credit fund, as amended by Sec. 27. Conforms to the Section 52 repeal of AS 43.55.023. Effective Jan. 1, 2020.
- Section 29 Amends AS 43.55.028(g), Oil and Gas Production Tax, Oil and gas tax credit fund. Requires the Dept. of Revenue to adopt regulations granting preference to companies with at least 80% Alaska hire, in case there is not enough money in the

Oil and Gas Tax Credit Fund to cover all applicants. Also, as credits for LNG storage facilities, gas storage facilities and instate refineries would no longer be refunded through the fund, makes conforming adjustments. Effective Jan. 1, 2017.

- Section 30 Adds a new subsection to AS 43.55.028, Oil and Gas Production Tax, Oil and gas tax credit fund. Ensures an outstanding liability to the state related to oil and gas activity is withheld from the amount of a tax certificate purchased by the Dept. of Revenue using the Oil and Gas Tax Credit Fund. The department may use the withheld amount to satisfy an outstanding liability, providing the liability is not being contested through an appeal or adjudicatory process established in law, without the taxpayer's consent. Satisfying a liability in this manner would not affect the applicant's ability to contest a liability. Effective Jan. 1, 2017.
- Section 31 Amends AS 43.55.029(a), Oil and Gas Production Tax, Assignment of tax credit certificate. Conforming to the Section 50 repeal of the qualified capital expenditure credit in AS 43.55.023(a). Effective Jan. 1, 2017.
- Section 32 Amends AS 43.55.029(a), Oil and Gas Production Tax, Assignment of tax credit certificate, as amended by Sec. 31. Conforms to the Section 51 repeal of the well lease expenditure credit in AS 43.55.023(l). Effective Jan. 1, 2019.
- Section 33 Amends AS 43.55.029(a), Oil and Gas Production Tax, Assignment of tax credit certificate, as amended by Secs. 31 and 32. Conforms to the Sec. 52 repeal of the net operating loss credit in AS 43.55.023(b). Effective Jan. 1, 2020.
- Section 34 Amends AS 43.55.030(a), Oil and Gas Production Tax, Filing of statements. Conforms to the repeal of the qualified capital expenditure credit in Section 50. Effective Jan. 1, 2017.
- Section 35 Amends AS 43.55.030(e), Oil and Gas Production Tax, Filing of statements. Conforms to the Section 50 repeal of the qualified capital expenditure credit, AS 43.55.023(a). Effective Jan. 1, 2017.
- Section 36 Amends AS 43.55.075(b), Oil and Gas Production Tax, Limitation on assessment and amended returns. Conforms to the Section 50 repeal of the qualified capital expenditure credit, AS 43.55.023(a). Effective Jan. 1, 2017.
- Section 37 Amends AS 43.55.160(d), Oil and Gas Production Tax, Determination of production tax value of oil and gas. Conforms to the Section 52 repeal of AS 43.55.023(b). Effective Jan. 1, 2020.
- Section 38 Amends AS 43.55.160(e), Oil and Gas Production Tax, Determination of production tax value of oil and gas. Requires that, for the purposes of calculating a carried-forward annual loss, any reduction due to the Gross Value Reduction for new oil is added back to the tax calculation. This prevents the GVR from

increasing the amount of a loss. Also, conforms to the new lease expenditure provisions in Section 42. Effective Jan. 1, 2017.

- Section 39 Amends AS 43.55.160(e), Oil and Gas Production Tax, Determination of production tax value of oil and gas, as amended by Sec. 38. Conforming to Section 52 repeal of AS 43.55.023(b). Effective Jan. 1, 2020.
- Secs. 40-41 Amend AS 43.55.160(f) and (g), Oil and Gas Production Tax, Determination of production tax value of oil and gas. For the gross value reduction for new oil, reduces the period in which the reduction applies from a lifetime benefit in current statute, to a 10-year benefit, beginning once regular production starts from a lease or property. The Alaska Oil and Gas Conservation Commission will determine when regular production begins. For new oil already receiving the gross value reduction, the benefit terminates Jan. 1, 2026. Effective Jan. 1, 2017.
- Section 42 Amends AS 43.55.165(a), Oil and Gas Production Tax, Lease expenditures. For the North Slope, lease expenditures include lease expenditures incurred in a prior year that have not been previously deducted in determining oil and gas taxes and were not the basis of a credit. This section allows lease expenditures to carry over from a prior year. Also, conforming to the Section 50 repeal of AS 43.55.165(j) and (k). Effective Jan. 1, 2017.
- Section 43 Amends AS 43.55.165(f), Oil and Gas Production Tax, Lease expenditures. Conforming to the Section 50 repeal of the qualified capital expenditure credit, 43.55.023(a). Effective Jan. 1, 2017.
- Section 44 Amends AS 43.55.170(c), Oil and Gas Production Tax, Adjustments to lease expenditures. Conforming to the Section 50 repeal of the qualified capital expenditure credit, AS 43.55.023(a). Effective Jan. 1, 2017.
- Section 45 Amends AS 43.55.180(a), Oil and Gas Production Tax, Required report. Conforms to the Section 52 repeal of 43.55.023. Effective Jan. 1, 2020.
- Section 46 Amends AS 43.55.895(b), Oil and Gas Production Tax, Applicability to municipal entities. Requires allocation of lease expenditures and tax credits between taxable and exempt production for a municipal entity. Effective Jan. 1, 2017.
- Section 47 Adds a new paragraph to AS 43.55.900, Oil and Gas Production Tax, Definitions. Defines “regular production” as defined in AS 31.05.170. Effective Jan. 1, 2017.
- Section 48 Adds new sections to AS 43.70, Alaska Business License Act. Requires a \$250,000 surety bond for oil and gas businesses, allowing the Department of Commerce commissioner to cancel the requirement once a business is producing oil or gas in commercial quantities. Provides a framework for people with claims

- against a business required to post the surety bond; prioritizes satisfaction of types of claims. Effective Jan. 1, 2017.
- Section 49 Adds a new paragraph to AS 43.99.950, Revenue and Taxation, General Provisions, defining “outstanding liability to the state.” Effective Jan. 1, 2017.
- Section 50 On Jan. 1, 2017, repeals multiple sections of statute, including the old DNR exploration credit programs; the qualified capital expenditure credit; and pre-2010 tax statutes. (See attached Summary of Repeals)
- Section 51 On Jan. 1, 2019, repeals the well lease expenditure credit. (See attached Summary of Repeals)
- Section 52 On Jan. 1, 2020, repeals all credits remaining in 43.55.023. (See attached Summary of Repeals)
- Section 53 Adds a new section to uncodified law creating a Legislative Working Group to develop a comprehensive tax regime for oil and gas in Cook Inlet and Middle Earth, to take effect Jan. 1, 2019, once the current credits are phased out. The working group’s proposal is to be presented to the Legislature in the 2017 regular session, and should include evaluation of incentives other than direct monetary support, including loan guarantees. Effective immediately.
- Section 54 Applicability language.
- Section 55 Transition language related to the Jan. 1, 2017, repeal of the qualified capital expenditure credit, AS 43.55.023(a). Effective Jan. 1, 2017.
- Section 56 Transition language related to the repeal of the well lease expenditure credit. AS 43.55.023(l) and (n). Effective Jan. 1, 2019.
- Section 57 Transition language related to the repeal of the carry-forward annual loss credit, AS 43.55.023(b). Effective Jan. 1, 2020.
- Section 58 Transition language related to credits. Effective Jan. 1, 2020.
- Section 59 Transition language related to lease expenditures and the repeal of AS 43.55.165(j) and (k). Effective Jan. 1, 2017.
- Section 60 Transition language related to exploration and seismic expenditures. Effective Jan. 1, 2017.
- Section 61 Transition language authorizing the Department of Revenue, Department of Natural Resources, Department of Commerce, Community and Economic Development, and the Alaska Oil and Gas Conservation Commission to adopt regulations for this act. Effective immediately.

- Section 62 Transition language authorizing the Department of Revenue and Department of Natural Resources to adopt retroactive regulations. Effective immediately.
- Section 63 Immediate effective date for sections 22 (extension of Middle Earth credit for a well spudded but not completed), 53 (Legislative Working Group), 61 (authority to adopt regulations) and 62 (authority to adopt retroactive regulations).
- Section 64 Jan. 1, 2019, effective date for sections 32, 51 and 56.
- Section 65 Jan. 1, 2020, effective date for sections 23, 26, 28, 33, 37, 39, 45, 52, 57 and 58.
- Section 66 Jan. 1, 2017, effective date for all other sections.

CS for HB 247 \D - Summary of Repealers

Jan. 1, 2017 (Section 50)

- AS 38.05.180(i) Repeals an old Department of Natural Resources exploration incentive credit program.
- AS 41.09.010-.030, 090 Repeals a currently un-used exploration incentive credit program.
- AS 43.20.053(j)(4) Repeals the definition of "unpaid delinquent tax" in the instate refinery credit statute. A definition of "unpaid delinquent tax" is added to the income tax statute in Section 13.

(j) In this section,

(4) "unpaid delinquent tax" means an amount of tax for which the department has issued an assessment that has not been paid and, if contested, has not been finally resolved in the taxpayer's favor.

- AS 43.55.023(a) Repeals the qualified capital expenditure credit.

- AS 43.55.023(o) Conforming to the repeal of the qualified capital expenditure credit.

(o) In this section, "qualified capital expenditure"

(1) means, except as otherwise provided in (2) of this subsection, an expenditure that is a lease expenditure under AS 43.55.165 and is

(A) incurred for geological or geophysical exploration or

(B) treated as a capitalized expenditure under 26 U.S.C. (Internal Revenue Code), as amended, regardless of elections made under 26 U.S.C. 263(c) (Internal Revenue Code), as amended, and is

(i) treated as a capitalized expenditure for federal income tax reporting purposes by the person incurring the expenditure; or

(ii) eligible to be deducted as an expense under 26 U.S.C. 263(c) (Internal Revenue Code), as amended;

(2) does not include an expenditure incurred to acquire an asset

(A) the cost of previously acquiring which was a lease expenditure under AS 43.55.165 or would have been a lease expenditure under AS 43.55.165 if it had been incurred after March 31, 2006; for purposes of this subparagraph, "asset" includes geological, geophysical, and well data and interpretations; or (B) that has previously been placed in service

in the state; an expenditure to acquire an asset is not excluded under this paragraph if not more than an immaterial portion of the asset meets a description under this paragraph.

AS 43.55.025(a)(5), (7) Repeals exploration credits that are only good for work done before July 2016. Retains the (a)(6) credit, which is extended for spudded but not completed wells in Middle Earth, in Section 22.

(a) Subject to the terms and conditions of this section, a credit against the production tax levied by AS 43.55.011(e) is allowed for exploration expenditures that qualify under (b) of this section in an amount equal to one of the following:

(5) 80, 90, or 100 percent, or a lesser amount described in (1) of this section, of the total exploration expenditures described in (b)(1) and (2) of this section and not excluded by (b)(3) and (4) of this section that qualify only under (1) of this section;

(7) the lesser of \$7,500,000 or 75 percent of the total seismic exploration expenditures described in (n) of this section and that qualify under (b) of this section.

AS 43.55.025(l) Repeals the jack-up rig credit eligibility criteria, conforming to the repeal of the AS 43.55.025 (a)(5) credit.

AS 43.55.025(n) Repeals eligibility criteria for a seismic exploration credit associated with AS 43.55.025 (a)(7), which is repealed.

AS 43.55.028(i) Conforming to the repeal of the qualified capital expenditure credit.

(i) In this section, "qualified capital expenditure" has the meaning given in AS 43.55.023.

AS 43.55.075(d)(1) Conforming to the repeal of the qualified capital expenditure credit.

(d) In this section,

(1) "qualified capital expenditure" has the meaning given in AS 43.55.023;

AS 43.55.165(e)(18) Conforming to the repeal of the qualified capital expenditure credit.

(e) For purposes of this section, lease expenditures do not include

(18) that portion of expenditures, that would otherwise be qualified capital expenditures, as defined in AS 43.55.023, incurred during a calendar year that are less than the product of \$0.30 multiplied by the total taxable production from each lease or property, in BTU equivalent barrels, during that calendar year, except that, when a portion of a calendar year is subject to this provision, the expenditures and volumes shall be prorated within that calendar year;

AS 43.55.165(j) Repeals the “standard deduction” limitation on lease expenditure inflation that expired in 2010.

AS 43.55.165(k) Repeals the “standard deduction” limitation on lease expenditure inflation that expired in 2010.

AS 43.55.890(6) Conforming to the repeal of the qualified capital expenditure credit.

AS 43.55.890: Notwithstanding any contrary provision of AS 40.25.100, and regardless of whether the information is considered under AS 43.05.230(e) to constitute statistics classified to prevent the identification of particular returns or reports, the department may publish the following information under this chapter, if aggregated among three or more producers or explorers, showing by month or calendar year and by lease or property, unit, or area of the state:

(6) qualified capital expenditures, as defined in AS 43.55.023;

Jan. 1, 2019 (Section 51)

AS 43.55.023(l) Repeals the 40% well lease expenditure credit.

AS 43.55.023(n) Related to the repeal of the well lease expenditure credit.

(n) For the purposes of (l) of this section, a well lease expenditure incurred in the state south of 68 degrees North latitude is a lease expenditure that is

(1) directly related to an exploration well, a stratigraphic test well, a producing well, or an injection well other than a disposal well, located in the state south of 68 degrees North latitude, if the expenditure is a qualified capital expenditure and an intangible drilling and development cost authorized under 26 U.S.C. (Internal Revenue Code), as amended, and 26 C.F.R. 1.612-4, regardless of the elections made under 26 U.S.C. 263(c); in this paragraph, an expenditure directly related to a well includes an expenditure for well sidetracking, well deepening, well completion or recompletion, or well workover, regardless of whether the well is or has been a producing well; or

(2) an expense for seismic work conducted within the boundaries of a production or exploration unit.

Jan. 1, 2020 (Section 52)

AS 43.55.023 Repeals the single remaining AS 43.55.023 credit, (b), for net operating losses on the North Slope

AS 43.55.165(f) Conforming to the repeal of AS 43.55.023.

AS 43.55.165, Oil and Gas Production Tax; Lease expenditures; (f) For purposes of AS 43.55.023(a) and (b) and only as to expenditures incurred to explore for an oil or gas deposit located within land in which an explorer does not own a working interest, the term “producer” in this section includes “explorer.”

AS 43.55.170(c)

Conforming to the repeal of AS 43.55.023.

AS 43.55.170, Oil and Gas Production Tax, Adjustments to lease expenditure; (c) For purposes of AS 43.55.023(a) and (b) and only as to expenditures incurred to explore for an oil or gas deposit located within land in which an explorer does not own a working interest, the term “producer” in this section includes “explorer.”

CS HB 247: KEY ISSUES

**Presentation to House Rules Committee
Juneau, Alaska > Tuesday, May 11, 2016**

(via teleconference) Janak Mayer, Chairman & Chief Technologist > janak.mayer@enalytica.com

<http://enalytica.com>

SUMMARY › NS NEW DEVELOPER IMPACTS

divergent proposed changes › common proposed changes › history of credit payouts › north slope vs. cook inlet credits

Issue	Status Quo	CS HB 247 (FIN)	CS HB 247 (RULES)	Impact
Cook Inlet Tax credits & fiscal system	25% Net Operating Loss credit, 20% Qualified Capital Expenditure credit, 40% Well Lease Expenditure credit; up to 65% gov't support for spending and minimal production tax.	Reduce NOL credit to 10%, QCE to 10%, WLE to 20% by 2018. Restrict eligibility for NOL. Working group on Cook Inlet regime.	2017: QCE repealed, 20% WLE Credit, 25% NOL. 2018: NOL repealed. No credits from 2019 onward. Working group on Cook Inlet regime post-2019 credit expiry. Instate refinery and LNG storage facilities credits removed from Oil and Gas Tax Credit Fund.	Cook Inlet credit regime is clearly unsustainable in current environment. Rules CS provides steady ramp-down to zero with time for current companies to seek to become cash self-sustaining, while ending support entirely from 2019 onward.
North Slope gross minimum tax & NOL Credits	4% rate, binding for legacy output if net value is positive. If net value is negative, NOL can 'pierce' floor. "New," GVR-eligible production can take to zero due to \$5/bbl and small producer credit.	Introduce additional, 'harder' 2% gross floor; no credits can reduce tax liability below this.	Maintain status quo - no further floor hardening against credits. However, NOL credit ends and is replaced with pure expenditure carry-forward, effectively hardening floor against future losses.	Rules CS hardens floor against future losses, while maintaining value of current NOL credits; achieves similar fiscal impact in later years as floor hardening, while avoiding investment impacts of imposing unexpected changes on handling of loss credits already earned.
Refundable credits	Producers with >50 mb/d production must carry NOL forward, others can be reimbursed by the state. Current cash timing problems with refundable credit outflow at time of low revenues. Major new NS development could place significant strain on state cashflow.	\$100mm per company annual limit on reimbursement.	\$75mm per company annual limit on reimbursement. Refundable NOL on North Slope only for companies producing there in 2016 (<15 mb/d) or with approved unit plan of development or plan of exploration, expires at end of 2019. Credits in CI only to companies producing there in 2016 (expiring at end of 2018).	Rules CS lowers limit on reimbursement, then ends refundable credits altogether (from start 2019 in CI, start 2020 on NS). Companies with major, capital-intensive projects will need to use intervening time to find substantially more equity capital or bring in working interest partners if they are to proceed with / complete projects.

SUMMARY OF NEW DEVELOPER IMPACTS

divergent proposed changes > common proposed changes > history of credit payouts > north slope vs. cook inlet credits

Feature	Status Quo	CS HB 247 (FIN)	CS HB 247 (RULES)	Impact
Time limit on gross value reduction	No current time limit on how long new developments benefit from GVR.	Allow GVR benefit only for 5 years from first production (or until 1/1/2021).	Allow GVR benefit only for 10 years from first production (or until 1/1/2026).	Short limit effectively <u>eliminates much of the GVR benefit</u> . Major <u>negative impact</u> on recently sanctioned eligible developments. 10 year limit of Rules CS mitigates this significantly.
'Middle Earth' credits	25% Net Operating Loss credit, 20% Qualified Capital Expenditure credit, 40% Well Lease Expenditure credit.	Maintain NOL at 25%, reduce QCE to 10%, WLE to 30% by 2018. WLE may sunset in 2019??	<u>2017</u> : QCE repealed, 20% WLE Credit, 25% NOL. <u>2018</u> : NOL repealed. No credits from 2019 onward.	Rules CS end Middle Earth credits on same timeline as Cook Inlet credits (but maintains 2022 sunset for Middle Earth exploration credit, and, like Finance CS, 'grandfathers' 025(a)(6) credit (see next page)
Interest due on 'delinquent' taxes	Fed Discount Rate + 3% Simple Interest on delinquent taxes (up to 6-year audit statute of limitations).	Fed + 5% compounded quarterly for 3 yrs, then Fed + 5% simple interest (up to 6-year audit statute of limitations)	Fed + 5% compounded quarterly	Complexity of different types of interest in different years, combined with complexity of transition from current system to new system may be difficult to administer - Rules CS opts for greater simplicity.
Alaska hire	Alaska hire not currently given preferential treatment in tax code (significant constitutional restrictions).	No change	No preferential treatment in amount of refunded credits, but companies with >80% Alaska hire placed higher in queue for refundable credit payments	
Gross tax on private royalties	Tax of 5% of Gross Value at Point of Production (GVPP) for oil, 1.667% of GVPP for gas. GVPP can potentially be negative at very low prices.	No change	Clarifies that gross tax on private royalties may not be less than zero.	

SUMMARY > NS NEW DEVELOPER IMPACTS

divergent proposed changes > **common proposed changes** > history of credit payouts > north slope vs. cook inlet credits

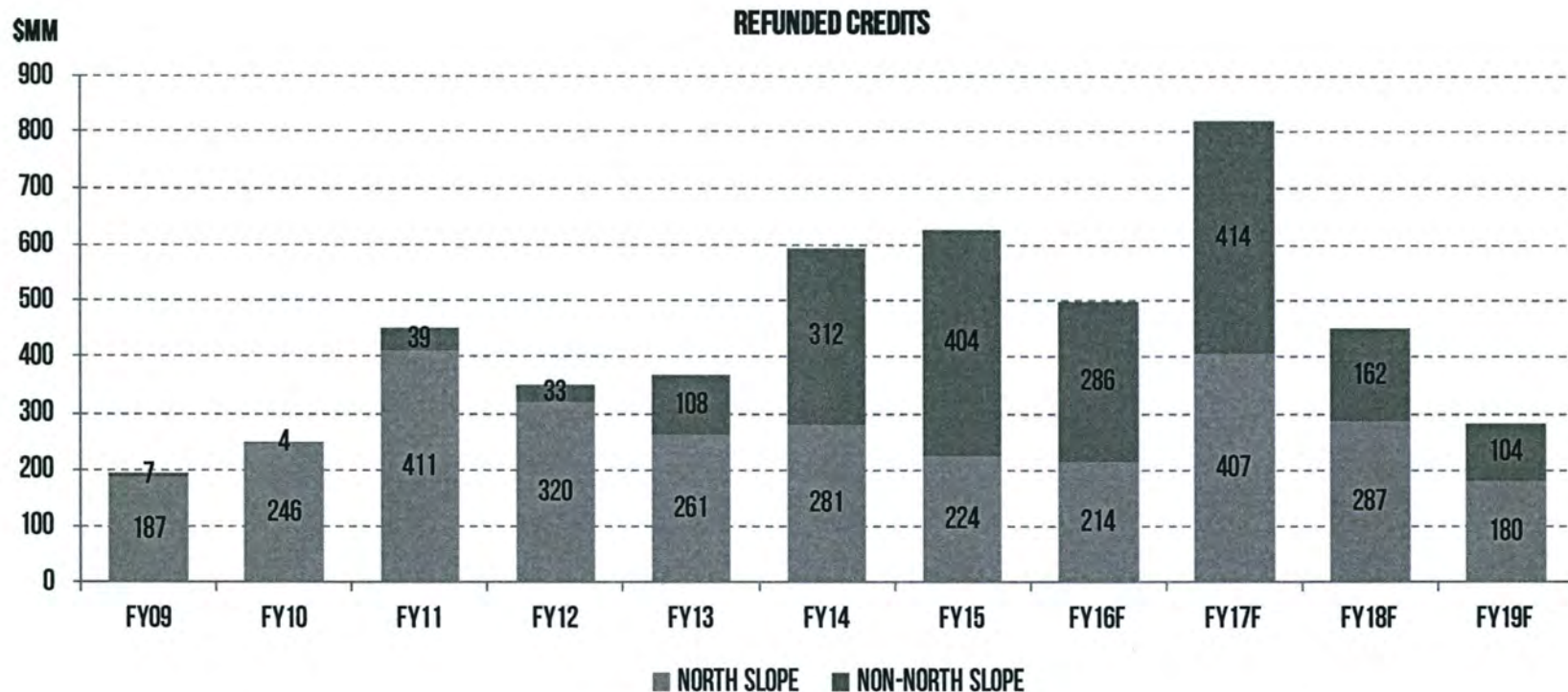
Issue	Status Quo	CS HB 247 (FIN) / CS HB 247 (RULES)	Impact
Refundable credit withholding	Liabilities against production tax withheld from refundable credits, but not other liabilities.	Any exploration/development/production related liabilities to the state can be withheld from refundable credit payments.	Companies in dispute over liabilities will have those amounts withheld. Companies that wish to have withholding used to settle liability may do so. Rules CS clarifies that company must dispute liability in order for withholding not to be used to settle it.
.025 (a)(6) 'Middle Earth' exploration credit	\$25 mm or 80% credit, sunsets July 1 2016.	Extend to allow for completion of wells spudded before July 1 in the Copper River Basin.	
Municipal production expense deduction	Munis that own production and only sell portion can deduct all expenses and claim credits.	Credits and deductions can only be claimed in proportion to taxable production.	
Surety bond	No bond requirement.	Add \$250,000 bond as license requirement.	

REFUNDED CREDITS REACHED NEW HIGH IN FY 2015

Refundable credits in FY 2015 reached \$628 mm, the highest point ever

In both 2014 and 2015, the majority of these credits went to non-North Slope producers

Under DOR's current forecast, credits will exceed \$1.3 billion across FY 2016 and FY 2017



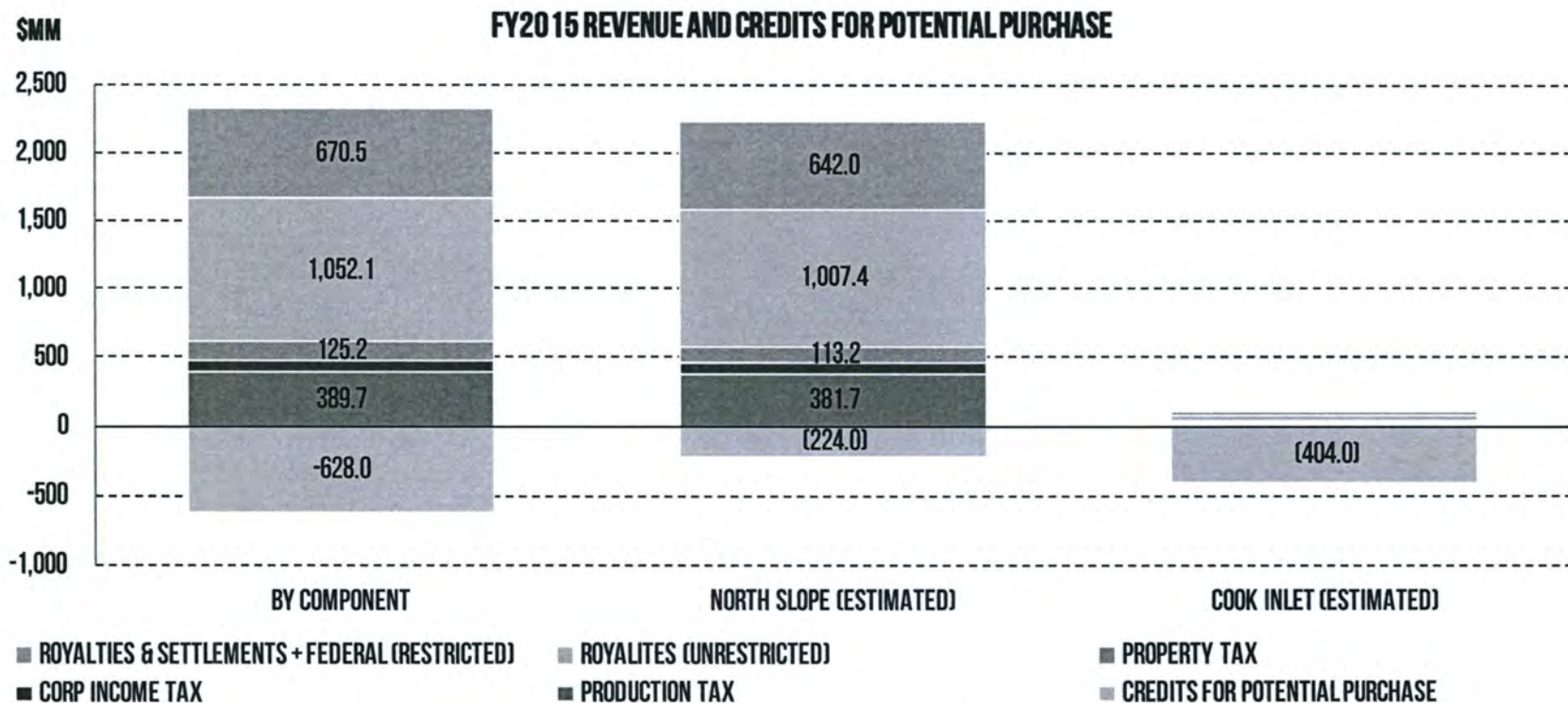
SOURCE: ALASKA DEPARTMENT OF REVENUE, TAX DIVISION

BIG DIFFERENCE BETWEEN NORTH SLOPE AND COOK INLET

The majority of refundable credits go to Cook Inlet producers

Cook Inlet production, however, generates limited direct revenue for the state

Credits on the North Slope are more limited but also a far smaller fraction of total value generated



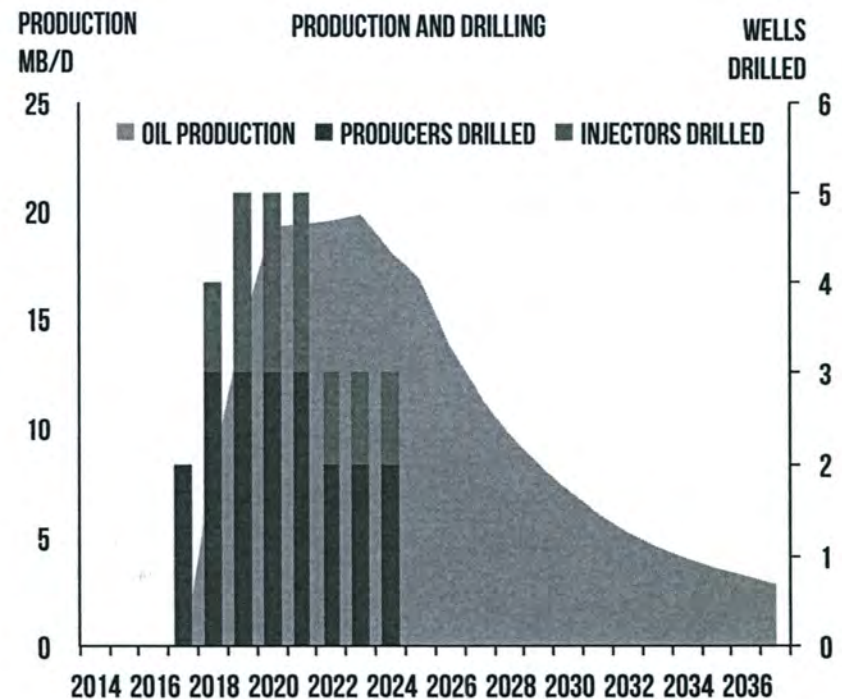
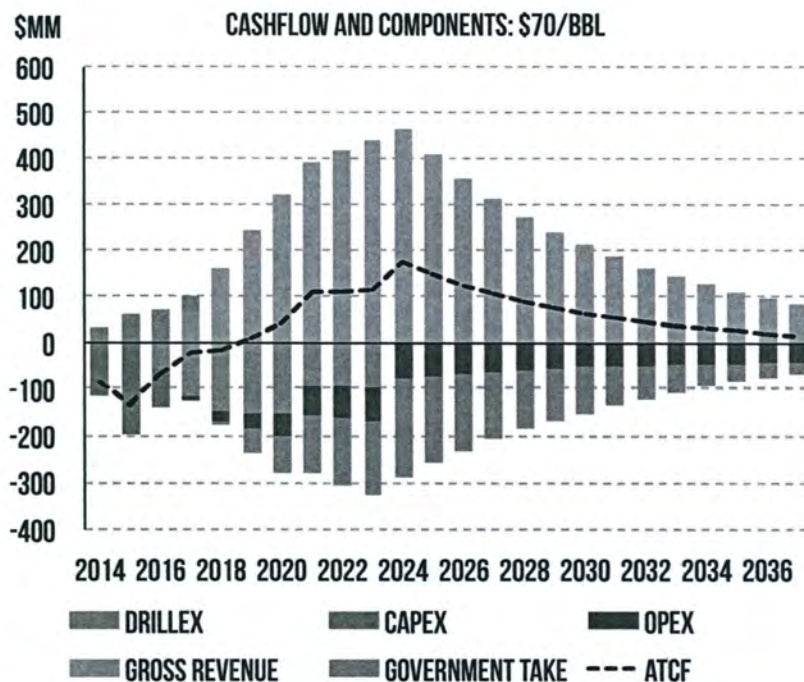
SOURCE: ALASKA DEPARTMENT OF REVENUE, REVENUE SOURCES BOOK; TAX DIVISION; ANALYTICA ESTIMATES

HOW DO CHANGES IMPACT NEW FIELD DEVELOPMENT?

Sample NS investment: Cumulative CAPEX and DRILLEX of \$1.3 bn; average annual OPEX of about \$15/bbl

Peak production of 20 mb/d; 30 wells (production and injection) drilled over 8 years

Ongoing DRILLEX in early years means bulk of tax liability occurs only after several years of production



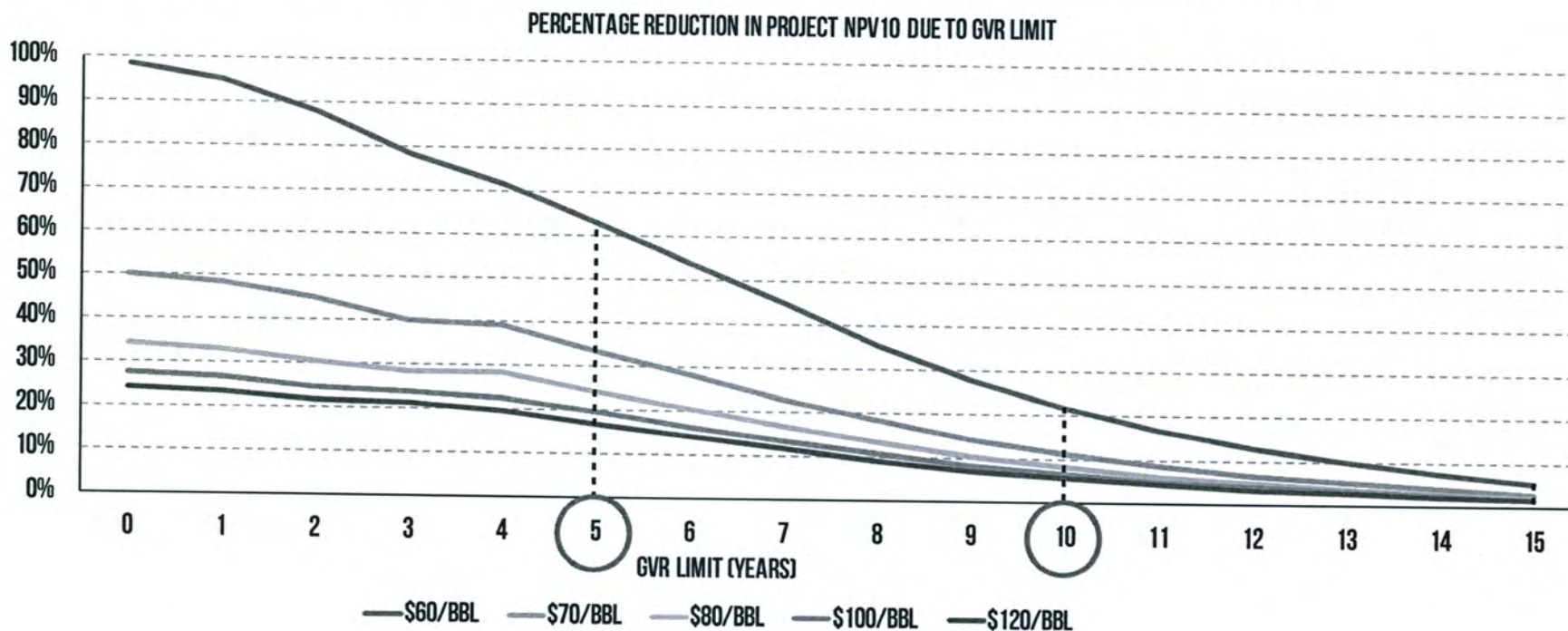
10 YR GVR LIMIT MITIGATES IMPACT ON PROJECT VALUE

Project is marginal at \$60/bbl; elimination of GVR can wipe out all value at that price

Because most tax liability occurs after end of major spending, short GVR limit provides little benefit

5-year GVR limit destroys over 60% of project value at \$60/bbl, relative to status quo

Impact of 10 year limit much lower; 15 year limit preserves almost all of status quo value



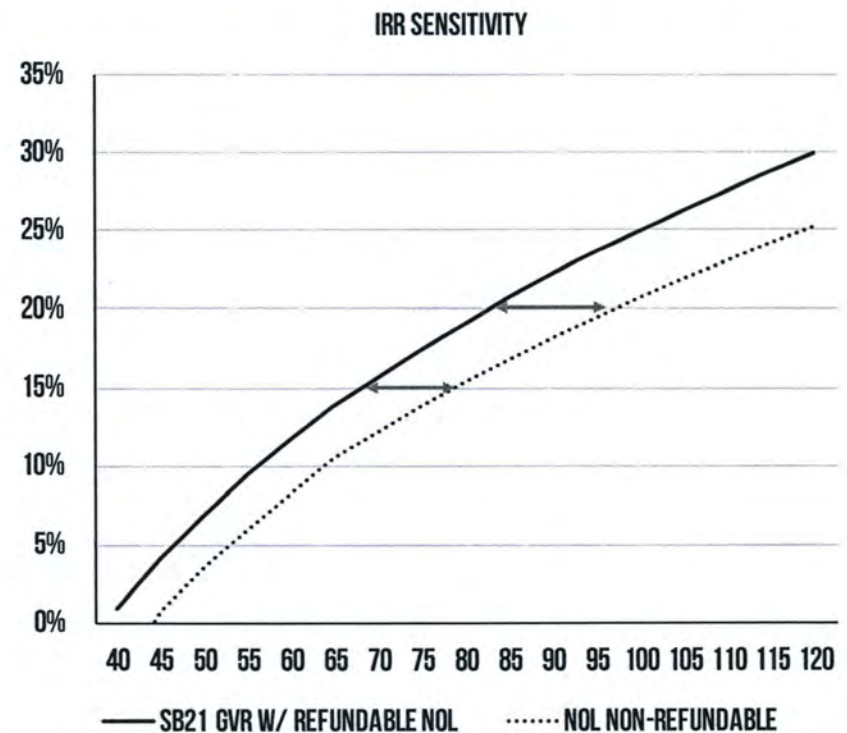
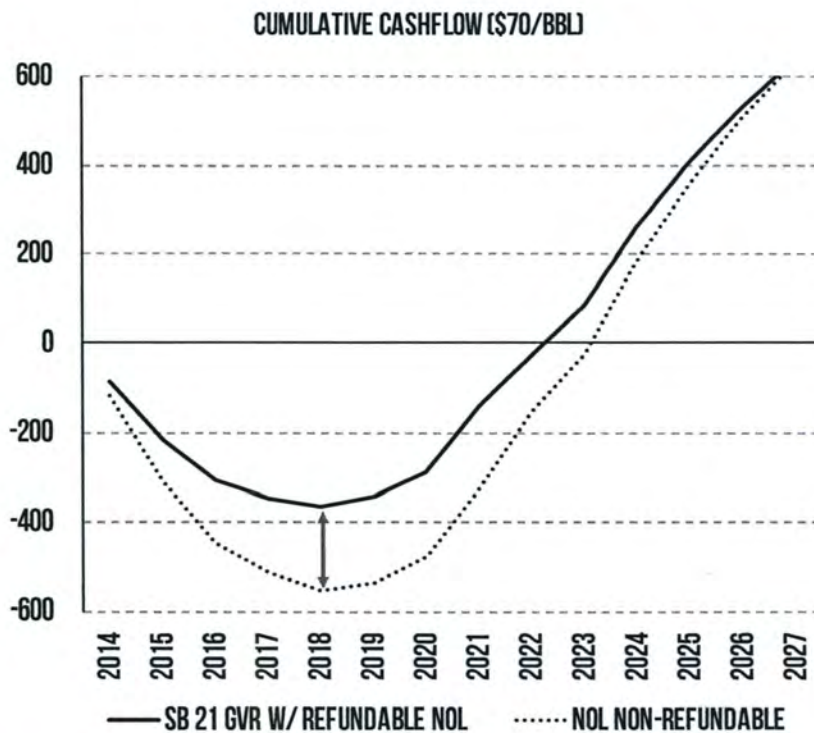
ENDING CREDIT REFUND IMPACTS CAPITAL NEEDS, IRR

Ending refundability would increase capital needs by over 50% (from \$350mm to \$550mm)

At the same time it increases the oil price needed to reach a given IRR by around \$10

New projects currently proposed by smaller companies may not be feasible in their current form

Question: will smaller companies be able to add capital or bring in additional working interest partners?





ALASKA STATE LEGISLATURE HOUSE RULES COMMITTEE

REPRESENTATIVE CRAIG JOHNSON, CHAIRMAN

State Capitol Room 216, Juneau, AK 99801-1182 (907) 465-4993, (907) 465-3872 Fax
716 W. 4th Ave., Ste. 300, Anchorage, AK 99501 (907) 269-0200, (907) 269-0204 Fax

Summary of \M version

The M version work draft closes out the state's tax credit program between Jan. 1, 2017, and Jan. 1, 2020, except for the Middle Earth 30-40% exploration credit that sunsets Jan. 1, 2022. In phasing out the Net Operating Loss carry-forward credit on the North Slope, the bill implements a system of carrying forward lease expenditures that a business is unable to deduct in the current year.

Statewide:

- No more than \$85 million per company in credits cashed back, per year.
- Refunds are prioritized to companies with at least 80% Alaska hire.
- Disclosure of some information to the public: the Department of Revenue will make public, annually, the name of a company receiving refunds for credits, as well as the total dollars refunded to the company for the year.
- Outstanding liability – providing a liability is not contested through an official process, DOR can apply a withheld credit against a liability without the taxpayer's consent.
- Includes requirement for a \$250,000 surety bond and provisions for prioritizing claims.
- Municipal producers must allocate lease expenditure to taxable production, so credits are not received/earned for nontaxable production.
- The income tax credits for the instate refinery and LNG storage facilities remain in statute, but as those are not oil and gas production tax-related credits, they are no longer refundable from the Oil and Gas Tax Credit Fund. They are refundable by the Department of Revenue generally (through annual appropriation).
- Interest rates increase from 3 points above the federal discount rate in current statute, simple interest, to five points above, compounding quarterly.

Specific to Cook Inlet and Middle Earth:

Cook Inlet and Middle Earth credits terminate Jan. 1, 2019. Middle Earth retains an exploration credit through 2021. A new fiscal regime will be developed for Cook Inlet and Middle Earth.

- For 2016, all credits currently in statute continue: 20% QCE, 40% WLE, 25% NOL
- In order to receive any credits for Cook Inlet work from Jan. 1, 2017, forward, a company must have oil or gas production in Cook Inlet in calendar year 2016.
- For 2017, the 40% WLE is repealed. Companies are eligible for a 30% capital credit, and for a 25% NOL credit; the 25% NOL credit terminates at the end of 2017.

- For 2018, companies are eligible for a 20% capital credit only; this credit terminates at the end of 2018.
- Legislative working group with tighter language, being explicit that the new fiscal regime to be developed would take effect with the expiration of credits, in Jan. 1, 2019.
- There is an additional benefit for Middle Earth; this is the extension of the 025(a)(6) credit for a well spudded, but not completed, by July 2016.
- And, for Middle Earth, this bill does not change the Jan. 1, 2022 sunset of the Middle Earth exploration credit.

Specific to the North Slope:

North Slope credits terminate Jan. 1, 2017; but, as a transition measure, for three years the state would continue to offer a 35% net operating loss carry-forward refundable credit, up to \$85 million per year, for very small producers with production by the end of 2016. The net profits system defining principle of allowing a company to recover its losses is retained by transitioning to a carry-forward of lease expenditures that a company was unable to deduct in the current year.

- The 35% NOL credit terminates at the end of 2016 for companies producing more than 20,000 barrels per day and companies with no production. Companies producing oil or gas on the North Slope in calendar year 2016, up to 20,000 barrels per day, continue to receive the 35% refundable NOL through 2019.
- Except for those smallest producers, the NOL no longer applies. Instead, companies in pre-production development or with more than 20,000 barrels per day production will be able to carry forward lease expenditures they were unable to deduct in the current year. Changing the NOL from a credit to carry-forward lease expenditure deductions hardens the 4% gross minimum floor; unlike credits, deductions cannot reduce production tax value below the gross minimum tax.
- The GVR reduction for new oil goes from a timeless benefit under current statute, to a 10-year benefit once regular production starts. The new oil per-barrel-credit also applies only while the new oil is receiving the GVR. Once new oil 'graduates' into normal oil after 10 years, and no longer receives the new-oil benefits, it is taxed as any other normal oil and is eligible for the sliding scale per-barrel reduction, like all normal oil.
- Previous bill versions have all included a provision to prevent the use of the GVR from increasing the amount of a loss. This bill retains that provision.



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2d CS for House Bill 247 () Version \M

- Section 1 Adds a new subsection to AS 31.05.030, Alaska Oil and Gas Conservation Act. Requires the Alaska Oil and Gas Conservation Commission to determine the start of regular production of new oil. Effective Jan. 1, 2017.
- Secs. 2-6 Amend AS 38.05.036 (a), (b), (c), (f) and (g), Alaska Land Act, Audit of royalty and net profit payments and costs. Conforming to the Section 47 repeal of AS 41.09, an old Department of Natural Resources exploration credit program. Effective Jan. 1, 2017.
- Section 7 Amends AS 40.25.100(a), Public Record Disclosures, Disposition of tax information. Conforming to Section 9, which requires the Department of Revenue to make public some taxpayer information. Effective Jan. 1, 2017.
- Section 8 Amends AS 43.05.225, Administration of Revenue Laws, Interest. The interest rate on delinquent taxes is five points above the 12th Federal Reserve District rate, compounded quarterly. Effective Jan. 1, 2017.
- Section 9 Adds a new subsection to AS 43.05.230, Administration of Revenue Laws, Disclosure of tax returns and reports. Requires the Department of Revenue to make public by April 30 of each year, the name of a company from whom the department purchases a tax credit certificate and the total amount of tax credit certificates purchased from each company. Effective Jan. 1, 2017.
- Section 10 Amends AS 43.20.046(e), Alaska Net Income Tax Act, Gas storage facility tax credit. The Department of Revenue will no longer use the Oil and Gas Tax Credit Fund to refund gas storage facility credits. The credits remain refundable by DOR. Also, definition of "unpaid delinquent taxes" is removed, as a new definition for "outstanding liability" applicable to AS Title 43, Revenue and Taxation, is added in Section 46. Effective Jan. 1, 2017.
- Section 11 Amends AS 43.20.047(e), Alaska Net Income Tax Act, Liquefied natural gas storage facility tax credit. The Department of Revenue will no longer use the Oil and Gas Tax Credit Fund to refund LNG storage facility credits. The credits remain refundable by DOR. Also, definition of "unpaid delinquent taxes" is removed, as a new definition for "outstanding liability" applicable to AS Title 43, Revenue and Taxation, is added in Section 46. Effective Jan. 1, 2017.

- Section 12 Amends AS 43.20.053(e), Alaska Net Income Tax Act, Qualified in-state oil refinery infrastructure expenditures tax credit. The Department of Revenue will no longer use the Oil and Gas Tax Credit Fund to refund instate refinery credits. The credits remain refundable by DOR. Also, reference to “unpaid delinquent taxes” is removed, as a new definition for “outstanding liability” applicable to AS Title 43, Revenue and Taxation, is added in Section 46. Effective Jan. 1, 2017.
- Section 13 Amends AS 43.55.011(m), Oil and Gas Production Tax. Conforming to the Section 47 repeal of the DNR credit programs in AS 38.05.180(i) and AS 41.09. Effective Jan. 1, 2017.
- Section 14 Amends AS 43.55.023(a), Oil and Gas Production Tax, Tax credits for certain losses and expenditures. For work done outside of the North Slope, a qualified capital expenditure credit of 30% is available in 2017, reducing to 20% in 2018. For Cook Inlet, a company must have regular production of oil or gas in Cook Inlet in calendar year 2016 in order to be eligible for this credit any year going forward. Also, conforming to the Section 47 repeal of the DNR credit programs in AS 38.05.180(i) and AS 41.09. Effective Jan. 1, 2017.
- Section 15 Amends AS 43.55.023(b), Oil and Gas Production Tax, Tax credits for certain losses and expenditures. The 35% net operating loss credit on the North Slope terminates at the end of 2016, except for companies with regular production of oil or gas on the North Slope in calendar year 2016, the 35% credit (refundable) is available through 2019, providing the company produces less than 20,000 barrels per day in 2016. The 25% net operating loss credit in areas other than the North Slope remains at 25% in 2017, then terminates. To receive the credit in Cook Inlet, a company must have regular production of oil or gas in Cook Inlet in calendar year 2016. Also, ensures that the application of a gross value reduction for new oil cannot increase the size of a loss. Effective Jan. 1, 2017.
- Section 16 Amends AS 43.55.023(d), Oil and Gas Production Tax, Tax credits for certain losses and expenditures. Conforms to the Section 48 repeal of AS 43.55.023(a), qualified capital expenditure credit. Effective Jan. 1, 2019.
- Section 17 Amends AS 43.55.024(i), Oil and Gas Production Tax, Additional nontransferable tax credits. Companies may apply the \$5 per-barrel new oil credit only for oil receiving the 10-year gross value reduction. Effective Jan. 1, 2017.
- Section 18 Amends AS 43.55.024(j), Oil and Gas Production Tax, Additional nontransferable tax credits. Once new oil is no longer eligible for new oil benefits and is being taxed as normal oil, the oil is also eligible for the sliding-scale per-barrel credit. Effective Jan. 1, 2017.
- Section 19 Amends AS 43.55.025(m), Oil and Gas Production Tax, Alternative tax credit for oil and gas exploration. Extends a Middle Earth credit to a company that has

spudded but not completed a well by July 1, 2016. The AS 43.55.025(a)(6) credit covers 80% of eligible costs, up to \$25 million. Effective immediately.

- Section 20 Amends AS 43.55.025(m), Oil and Gas Production Tax, Alternative tax credit for oil and gas exploration, as amended by Section 19. Conforming to the Section 49 repeal of AS 43.55.023. Effective Jan. 1, 2020.
- Section 21 Amends AS 43.55.025(o), Oil and Gas Production Tax, Alternative tax credit for oil and gas exploration. Conforms to the Section 47 repeal of AS 43.55.025 (a)(7), (l), and (n). Effective Jan. 1, 2017.
- Section 22 Amends AS 43.55.028(a), Oil and Gas Production Tax, Oil and gas tax credit fund. Removes the authority to use the fund to pay refunds for the income tax credits related to the instate refinery, LNG storage facility, and gas storage facility. Effective Jan. 1, 2017.
- Section 23 Amends AS 43.55.028(a), Oil and Gas Production Tax, Oil and gas tax credit fund, as amended by Sec. 22. Conforming to the Section 49 repeal of AS 43.55.023. Effective Jan. 1, 2020.
- Section 24 Amends AS 43.55.028(e), Oil and Gas Production Tax, Oil and gas tax credit fund. Limits the maximum state repurchase of tax credits to \$85 million per company, per year. Requires the Department of Revenue to, before purchasing credit certificates, find that the applicant is not the result of the division of a single entity into multiple entities that would reasonably have been expected to apply as a single entity. Effective Jan. 1, 2017.
- Section 25 Amends AS 43.55.028(e), Oil and Gas Production Tax, Oil and gas tax credit fund, as amended by Sec. 24. Conforms to the Section 49 repeal of AS 43.55.023. Effective Jan. 1, 2020.
- Section 26 Amends AS 43.55.028(g), Oil and Gas Production Tax, Oil and gas tax credit fund. Requires the Dept. of Revenue to adopt regulations granting preference to companies with at least 80% Alaska hire, in case there is not enough money in the Oil and Gas Tax Credit Fund to cover all applicants. Also, as credits for LNG storage facilities, gas storage facilities and instate refineries would no longer be refunded through the fund, makes conforming adjustments. Effective Jan. 1, 2017.
- Section 27 Adds a new subsection to AS 43.55.028, Oil and Gas Production Tax, Oil and gas tax credit fund. Ensures an outstanding liability to the state related to oil and gas activity is withheld from the amount of a tax certificate purchased by the Dept. of Revenue using the Oil and Gas Tax Credit Fund. The department may use the withheld amount to satisfy an outstanding liability, providing the liability is not being contested through an appeal or adjudicatory process established in law, without the taxpayer's consent. Satisfying a liability in this manner would not affect the applicant's ability to contest a liability. Effective Jan. 1, 2017.

- Section 28 Amends AS 43.55.029(a), Oil and Gas Production Tax, Assignment of tax credit certificate. Conforming to the Section 47 repeal of the well lease expenditure credit in AS 43.55.023(l). Effective Jan. 1, 2017.
- Section 29 Amends AS 43.55.029(a), Oil and Gas Production Tax, Assignment of tax credit certificate, as amended by Sec. 28. Conforms to the Sec. 48 repeal of the qualified capital expenditure credit in AS 43.55.023(a). Effective Jan. 1, 2019.
- Section 30 Amends AS 43.55.029(a), Oil and Gas Production Tax, Assignment of tax credit certificate, as amended by Secs. 28 and 29. Conforms to the Sec. 49 repeal of the net operating loss credit in AS 43.55.023(b). Effective Jan. 1, 2020.
- Section 31 Amends AS 43.55.030(a), Oil and Gas Production Tax, Filing of statements. Conforms to the repeal of the qualified capital expenditure credit in Section 48. Effective Jan. 1, 2019.
- Section 32 Amends AS 43.55.030(e), Oil and Gas Production Tax, Filing of statements. Conforms to the Section 48 repeal of the qualified capital expenditure credit, AS 43.55.023(a). Effective Jan. 1, 2019.
- Section 33 Amends AS 43.55.075(b), Oil and Gas Production Tax, Limitation on assessment and amended returns. Conforms to the Section 48 repeal of the qualified capital expenditure credit, AS 43.55.023(a). Effective Jan. 1, 2019.
- Section 34 Amends AS 43.55.160(d), Oil and Gas Production Tax, Determination of production tax value of oil and gas, as amended by Section 37. Conforms to the Section 48 repeal of AS 43.55.023. Effective Jan. 1, 2020.
- Section 35 Amends AS 43.55.160(e), Oil and Gas Production Tax, Determination of production tax value of oil and gas. Requires that, for the purposes of calculating a carried-forward annual loss, any reduction due to the Gross Value Reduction for new oil is added back to the tax calculation. This prevents the GVR from increasing the amount of a loss. Also, conforms to the new lease expenditure provisions in Section 39. Effective Jan. 1, 2017.
- Section 36 Amends AS 43.55.160(e), Oil and Gas Production Tax, Determination of production tax value of oil and gas, as amended by Sec. 35. Conforming to Section 49 repeal of AS 43.55.023. Effective Jan. 1, 2020.
- Secs. 37-38 Amend AS 43.55.160(f) and (g), Oil and Gas Production Tax, Determination of production tax value of oil and gas. For the gross value reduction for new oil, reduces the period in which the reduction applies from a lifetime benefit in current statute, to a 10-year benefit, beginning once regular production starts from a lease or property. The Alaska Oil and Gas Conservation Commission will

determine when regular production begins. For new oil already receiving the gross value reduction, the benefit terminates Jan. 1, 2026. Effective Jan. 1, 2017.

- Section 39 Amends AS 43.55.165(a), Oil and Gas Production Tax, Lease expenditures. For the North Slope, lease expenditures include lease expenditures incurred in a prior year that have not been previously deducted in determining oil and gas taxes and were not the basis of a credit. This section allows lease expenditures to carry over from a prior year. Also, conforming to the Section 47 repeal of AS 43.55.165(j) and (k). Effective Jan. 1, 2017.
- Section 40 Amends AS 43.55.165(f), Oil and Gas Production Tax, Lease expenditures. Conforming to the Section 48 repeal of the qualified capital expenditure credit, 43.55.023(a). Effective Jan. 1, 2019.
- Section 41 Amends AS 43.55.170(c), Oil and Gas Production Tax, Adjustments to lease expenditures. Conforming to the Section 48 repeal of the qualified capital expenditure credit, AS 43.55.023(a). Effective Jan. 1, 2019.
- Section 42 Amends AS 43.55.180(a), Oil and Gas Production Tax, Required report. Conforms to the Section 49 repeal of 43.55.023. Effective Jan. 1, 2020.
- Section 43 Amends AS 43.55.895(b), Oil and Gas Production Tax, Applicability to municipal entities. Requires allocation of lease expenditures and tax credits between taxable and exempt production for a municipal entity. Effective Jan. 1, 2017.
- Section 44 Adds a new paragraph to AS 43.55.900, Oil and Gas Production Tax, Definitions. Defines “regular production” as defined in AS 31.05.170. Effective Jan. 1, 2017.
- Section 45 Adds new sections to AS 43.70, Alaska Business License Act. Requires a \$250,000 surety bond for oil and gas businesses, allowing the Department of Commerce commissioner to cancel the requirement once a business is producing oil or gas in commercial quantities. Provides a framework for people with claims against a business required to post the surety bond; prioritizes satisfaction of types of claims. Effective Jan. 1, 2017.
- Section 46 Adds a new paragraph to AS 43.99.950, Revenue and Taxation, General Provisions, defining “outstanding liability to the state.” Effective Jan. 1, 2017.
- Section 47 On Jan. 1, 2017, repeals multiple sections of statute, including the old DNR exploration credit programs; the well lease expenditure credit; and pre-2010 tax statutes. (See attached Summary of Repeals)
- Section 48 On Jan. 1, 2019, repeals the qualified capital expenditure credit. (See attached Summary of Repeals)

- Section 49 On Jan. 1, 2020, repeals all credits remaining in 43.55.023. (See attached Summary of Repeals)
- Section 50 Adds a new section to uncodified law creating a Legislative Working Group to develop a comprehensive tax regime for oil and gas in Cook Inlet and Middle Earth, to take effect Jan. 1, 2019, once the current credits are phased out. The working group's proposal is to be presented to the Legislature in the 2017 regular session, and should include evaluation of incentives other than direct monetary support, including loan guarantees. Effective immediately.
- Section 51 Applicability language.
- Section 52 Transition language related to the Jan. 1, 2017, repeal of the well lease expenditure credits, AS 43.55.023(l) and (n). Effective Jan. 1, 2017.
- Section 53 Transition language related to the repeal of the qualified capital expenditure credit. Effective Jan. 1, 2019.
- Section 54 Transition language related to the repeal of the carry-forward annual loss credit. Effective Jan. 1, 2020.
- Section 55 Transition language related to credits. Effective Jan. 1, 2020.
- Section 56 Transition language related to lease expenditures and the repeal of AS 43.55.165(j) and (k). Effective Jan. 1, 2017.
- Section 57 Transition language related to exploration and seismic expenditures. Effective Jan. 1, 2017.
- Section 58 Transition language authorizing the Department of Revenue, Department of Natural Resources, Department of Commerce, Community and Economic Development, and the Alaska Oil and Gas Conservation Commission to adopt regulations for this act. Effective immediately.
- Section 59 Transition language authorizing the Department of Revenue and Department of Natural Resources to adopt retroactive regulations. Effective immediately.
- Section 60 Immediate effective date for sections 19 (extension of Middle Earth credit for a well spudded but not completed), 50 (Legislative Working Group), 58 (authority to adopt regulations) and 59 (authority to adopt retroactive regulations).
- Section 61 Jan. 1, 2019, effective date for sections 16, 29, 31-33, 40, 41, 48, and 53.
- Section 62 Jan. 1, 2020, effective date for sections 20, 23, 25, 30, 34, 36, 42, 49, 54, and 55.
- Section 63 Jan. 1, 2017, effective date for all other sections.

CS for HB 247 \M - Summary of Repealers

Jan. 1, 2017 (Section 47)

- AS 38.05.180(i) Repeals an old Department of Natural Resources exploration incentive credit program.
- AS 41.09.010-.030, 090 Repeals a currently un-used exploration incentive credit program.
- AS 43.20.053(j)(4) Repeals the definition of "unpaid delinquent tax" in the instate refinery credit statute. A definition of "unpaid delinquent tax" is added to the income tax statute in Section 13.
- (j) In this section,
- (4) "unpaid delinquent tax" means an amount of tax for which the department has issued an assessment that has not been paid and, if contested, has not been finally resolved in the taxpayer's favor.
- AS 43.55.023(l) Repeals the 40% well lease expenditure credit.
- AS 43.55.023(n) Related to the repeal of the well lease expenditure credit.
- (n) For the purposes of (l) of this section, a well lease expenditure incurred in the state south of 68 degrees North latitude is a lease expenditure that is
- (1) directly related to an exploration well, a stratigraphic test well, a producing well, or an injection well other than a disposal well, located in the state south of 68 degrees North latitude, if the expenditure is a qualified capital expenditure and an intangible drilling and development cost authorized under 26 U.S.C. (Internal Revenue Code), as amended, and 26 C.F.R. 1.612-4, regardless of the elections made under 26 U.S.C. 263(c); in this paragraph, an expenditure directly related to a well includes an expenditure for well sidetracking, well deepening, well completion or recompletion, or well workover, regardless of whether the well is or has been a producing well; or
- (2) an expense for seismic work conducted within the boundaries of a production or exploration unit.
- AS 43.55.025(a)(5), (7) Repeals exploration credits that are only good for work done before July 2016. Retains the (a)(6) credit, which is extended for spudded but not completed wells in Middle Earth, in Section 22.
- (a) Subject to the terms and conditions of this section, a credit against the production tax levied by AS 43.55.011(e) is allowed for exploration expenditures that qualify under (b) of this section in an amount equal to one of the following:

(5) 80, 90, or 100 percent, or a lesser amount described in (1) of this section, of the total exploration expenditures described in (b)(1) and (2) of this section and not excluded by (b)(3) and (4) of this section that qualify only under (l) of this section;

(7) the lesser of \$7,500,000 or 75 percent of the total seismic exploration expenditures described in (n) of this section and that qualify under (b) of this section.

- AS 43.55.025(l) Repeals the jack-up rig credit eligibility criteria, conforming to the repeal of the AS 43.55.025 (a)(5) credit.
- AS 43.55.025(n) Repeals eligibility criteria for a seismic exploration credit associated with AS 43.55.025 (a)(7), which is repealed.
- AS 43.55.165(j) Repeals the "standard deduction" limitation on lease expenditure inflation that expired in 2010.
- AS 43.55.165(k) Repeals the "standard deduction" limitation on lease expenditure inflation that expired in 2010.

Jan. 1, 2019 (Section 48)

- AS 43.55.023(a) Repeals the qualified capital expenditure credit.
- AS 43.55.023(o) Conforming to the repeal of the qualified capital expenditure credit.

(o) In this section, "qualified capital expenditure"

(1) means, except as otherwise provided in (2) of this subsection, an expenditure that is a lease expenditure under AS 43.55.165 and is

(A) incurred for geological or geophysical exploration or

(B) treated as a capitalized expenditure under 26 U.S.C. (Internal Revenue Code), as amended, regardless of elections made under 26 U.S.C. 263(c) (Internal Revenue Code), as amended, and is

(i) treated as a capitalized expenditure for federal income tax reporting purposes by the person incurring the expenditure; or

(ii) eligible to be deducted as an expense under 26 U.S.C. 263(c) (Internal Revenue Code), as amended;

(2) does not include an expenditure incurred to acquire an asset (A) the cost of previously acquiring which was a lease expenditure under AS 43.55.165 or would have been a lease expenditure under AS 43.55.165 if it had been incurred after

March 31, 2006; for purposes of this subparagraph, "asset" includes geological, geophysical, and well data and interpretations; or (B) that has previously been placed in service in the state; an expenditure to acquire an asset is not excluded under this paragraph if not more than an immaterial portion of the asset meets a description under this paragraph.

- AS 43.55.028(i) Conforming to the repeal of the qualified capital expenditure credit.
- (i) In this section, "qualified capital expenditure" has the meaning given in AS 43.55.023.
- AS 43.55.075(d)(1) Conforming to the repeal of the qualified capital expenditure credit.
- (d) In this section,
- (1) "qualified capital expenditure" has the meaning given in AS 43.55.023;
- AS 43.55.165(e)(18) Conforming to the repeal of the qualified capital expenditure credit.
- (e) For purposes of this section, lease expenditures do not include
- (18) that portion of expenditures, that would otherwise be qualified capital expenditures, as defined in AS 43.55.023, incurred during a calendar year that are less than the product of \$0.30 multiplied by the total taxable production from each lease or property, in BTU equivalent barrels, during that calendar year, except that, when a portion of a calendar year is subject to this provision, the expenditures and volumes shall be prorated within that calendar year;
- AS 43.55.890(6) Conforming to the repeal of the qualified capital expenditure credit.
- AS 43.55.890: Notwithstanding any contrary provision of AS 40.25.100, and regardless of whether the information is considered under AS 43.05.230(e) to constitute statistics classified to prevent the identification of particular returns or reports, the department may publish the following information under this chapter, if aggregated among three or more producers or explorers, showing by month or calendar year and by lease or property, unit, or area of the state:
- (6) qualified capital expenditures, as defined in AS 43.55.023;

Jan. 1, 2020 (Section 49)

- AS 43.55.023 Repeals the single remaining AS 43.55.023 credit, (b), for net operating losses on the North Slope
- AS 43.55.165(f) Conforming to the repeal of AS 43.55.023.

AS 43.55.165, Oil and Gas Production Tax; Lease expenditures; (f) For purposes of AS 43.55.023(a) and (b) and only as to expenditures incurred to explore for an oil or gas deposit located within land in which an explorer does not own a working interest, the term “producer” in this section includes “explorer.”

AS 43.55.170(c)

Conforming to the repeal of AS 43.55.023.

AS 43.55.170, Oil and Gas Production Tax, Adjustments to lease expenditure; (c) For purposes of AS 43.55.023(a) and (b) and only as to expenditures incurred to explore for an oil or gas deposit located within land in which an explorer does not own a working interest, the term “producer” in this section includes “explorer.”

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Pulling Together to Build Our Future

Oil and Gas Tax Credit Reform

CS HB247(RLS)\D

Department of Revenue

Initial Response to Rules Committee Proposal

May 11, 2016

Major Bill Concepts in Governor's Proposal

- 1. Exploration Credits-** *sunset and transition*
- 2. Cook Inlet Drilling Credits-** *phase out while retaining operating loss credits*
- 3. Repurchase Limits-** *limit cash outlay*
- 4. Remove Exceptions / Loopholes**
- 5. Strengthen Minimum Tax-** *prevent certain credits from going below the floor, plus increase to 5%*
- 6. Other Provisions-** *technical cleanup, transparency, interest rate reform*



Credit Cost in Perspective

Credit Cost in Perspective

FY 2007 thru 2015, \$7.4 Billion in Credits

North Slope

- \$4.3 billion credits against tax liability
 - Major producers; mostly 20% capital credit in ACES and per-taxable-barrel credit in SB21
- \$2.1 billion refunded credits
 - New producers and explorers developing new fields

Non-North Slope (Cook Inlet & Middle Earth)

- \$100 million credits against tax liability
 - Another \$500 to \$800 million Cook Inlet tax reductions (through 2013) due to the tax cap still tied to ELF
- \$900 million refunded credits (most since 2013)

Credit Cost in Perspective

Total Petroleum Revenue FY 2007 thru 2015

North Slope

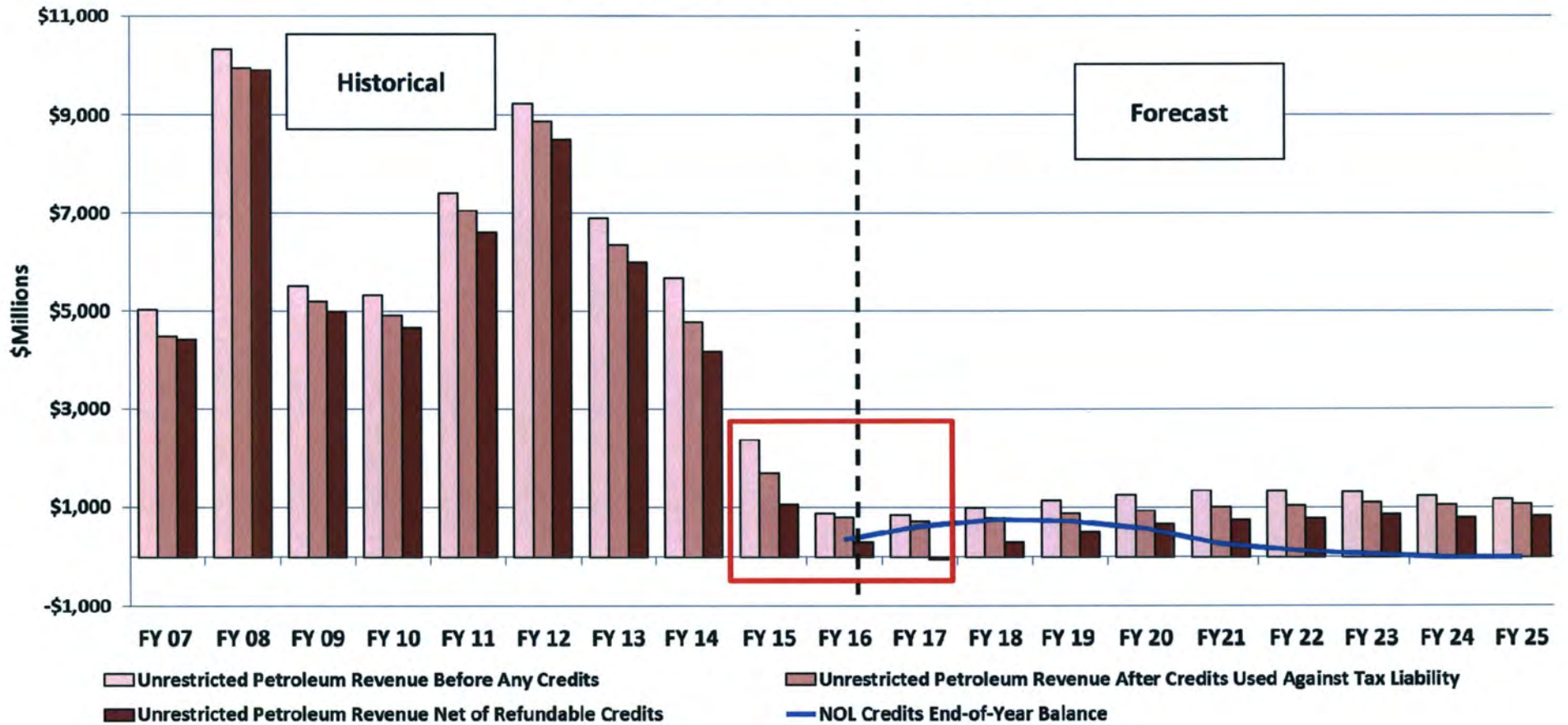
Production Tax	\$32.8 billion
Royalties (unrestricted)	\$15.0 billion
Other GF Revenue	\$4.7 billion
<u>Restricted Revenue</u>	<u>\$8.7 billion</u>
Total	\$61.1 billion

Non-North Slope (Cook Inlet & Middle Earth)

Production Tax	<\$0.1 billion
Royalties (unrestricted)	\$0.5 billion
Other GF Revenue	\$0.3 billion
<u>Restricted Revenue</u>	<u>\$0.2 billion</u>
Total	\$1.0 billion

Credit Cost in Perspective

Statewide Tax Credits and Unrestricted Petroleum Revenue



Credit Cost in Perspective

- FY16 Appropriation Capped at **\$500 million**
 - \$473 million paid out to date
 - About \$200 million North Slope, \$273 million non-NS
 - \$27 million left in fund with \$4 million in-process claims
- Current DOR Work Pool **\$675 million**
 - \$10 million in older NOL credits
 - \$22 million in older exploration credits
 - \$552 million in 2015 NOL, QCE, WLE credits
 - \$60 million in 2015 exploration credits
 - \$31 million expected via amended returns
- Remaining \$120 million will be some CY2016 quarterly QCE and WLE's, "last minute" exploration claims, and the first LNG storage and refinery claims

Credit Cost in Perspective

Of the \$3 billion in state-refunded credits through the end of FY15:

- \$1.45 billion went to six North Slope projects that now have production
- \$650 million went to 13 North Slope projects that do not have any production. Some of these are abandoned, and some are in process
- \$450 million went to six non-North Slope projects that have production
- \$450 million went to eight non-North Slope projects that do not have any production

Credit Cost in Perspective

North Slope Refundable Credits

Of the \$1.45 billion that was spent between FY07-FY15 supporting six producing projects:

- Total production through end of FY15 is 38.5 million barrels
- Total credits = **\$37.30** / barrel
 - This number will decrease over time due to additional production from these fields
- Lease expenditures for these projects, through FY15, were \$4.94 billion
 - Credit support was **29%** of lease expenditures

Credit Cost in Perspective

Cook Inlet Refundable Credits

Of the \$450 million that was spent between FY07-FY15 supporting six producing projects:

- Total production through end of FY15 is 55.9 million BOE (much of this was gas)
- Total credits = **\$7.80** / BOE or about **\$1.30** / mcf
 - This number will decrease over time due to additional production from these fields
- Lease expenditures for these projects, through FY15, were \$1.09 billion
 - Credit support was **40%** of lease expenditures

Credit Cost in Perspective

Cook Inlet Tax Caps

- Estimated value to industry \$550-\$850 over the years 2007-2013
- Total Production Estimate
 - Gas: ~ 250 million cubic feet / day for seven years = 640 BCF of gas or 106 million BOE
 - Oil: ~ 10,000 barrels / day for seven years = 26 million BOE
 - Total Production = 132 million BOE
- Using midpoint \$700 million estimate, value of caps = **\$5.30** / barrel or **\$0.88** / mcf
- **Sum of Credits + Tax Caps: \$2.18 / mcf**

Response to Rules Committee Substitute

- 1. Introduction**
- 2. Positive Features**
- 3. Concerns**
- 4. Summary of Fiscal Impact**

Introduction

- The Rules Committee Substitute makes progress towards meeting several administration goals
 - Reducing future spending / rolling back credit programs
 - Limited strengthening of “floor”
 - Transparency

Introduction

- It also maintains several features that have been in many or most versions of HB247 / SB130
 - Inability to increase an operating loss using GVR
 - Substantial ramp down of Cook Inlet credits
 - Restores compound interest, with rate increase, for delinquent taxes
 - Municipal utility lease expenditure pro-rationing
 - Repeal of dormant programs and obsolete sections
 - Surety bonding with local vendor priority
 - Local hire repurchase priority

Introduction

- However, there are several major and minor concerns with the structure of the bill
 - Maintains large future liability through carried-forward lease expenditures
 - Shift in favor of incumbent producers and away from support for independents
 - Ongoing liability without any state pre-approval or other filter
 - Delay in GVR “graduation”
 - Hidden or inadvertent CAPEX tax cut
 - New and technical language changes that could have unintended consequences

Positive Features

Reduces Future Spending

- \$75 million per company per year cap (for transition years; only small producers or developers)
 - No repurchases after 2020
 - Cook Inlet credits eliminated in 2019
 - At full implementation in FY2021, about a \$300 million bill in total fiscal impact (revenue plus savings)

However:

- Extended transition period could lead to large credit liabilities outside existing forecasted projects

Positive Features

Limited Strengthening of Minimum Tax “Floor”

- With the elimination of Net Operating Loss credits, the minimum tax is hardened against future losses
 - The \$0-\$8 per barrel credit, which is currently limited by the floor, becomes a somewhat hardened limit
 - No fiscal impact until FY2020, because losses from before the effective date will take three years to be “used up,” zeroing out taxes from major producers

However

- Does not change ability to use \$5 per barrel credit for “GVR” production to go below minimum tax
- Small Producer and Exploration credits, until they sunset, can also be used to go below the “floor”

Positive Features

Transparency

- Annually makes public the name of each person / company who received cash credits, and the total amount repurchased

However:

- No information about what the credits were used for
- Written to exclude the so-called “corporate income tax” credits (Gas and LNG storage, Refinery)
- With imminent elimination of cash credits, this is a fairly limited amount and duration of public information
- Although this would be controversial, we believe there is strong benefit in making public the amount of carried-forward lease expenditures claimed by companies.

Concerns with Rules CS

Future liability through carried-forward lease expenditures

- Since Spring 2016 Forecast, administration emphasis has been on potential NOLs from major producers
- Substantial discussion of reducing, scaling, or eliminating the size of the NOL credit
- Issue is side-stepped by eliminating the credit but retaining carried forward “lease expenditures”
- This enables losses to be monetized against future taxes at the full 35% tax rate
- At end of fiscal note period (FY26), producers will hold losses that will offset \$715 million in future taxes

Concerns with Rules CS

Shift in favor of incumbent producers and away from support for independents

- Non-producers must also carry-forward their expenditures, eliminating cash support
- Our modeling showed that the administration's initial proposal of \$25 million cap did not have dramatic impact on smaller projects, but greatly reduced the economic viability of larger ones
- Zero cash support after 2019 would impact different companies very differently
 - Incumbent producers will be able to monetize their losses as soon as prices recover, whereas independents must wait for production

Concerns with Rules CS

Ongoing liability without any state pre-approval or other filter

- No limit on potential state liability
- Could be corrected with pre-approval process or a state loan mechanism
- During transition period, the “plan of development” filter includes plans of exploration, which could broaden the potential applicants
- “Smith Bay” issue: a \$100 million exploration project in a remote location that is many years from viable

Concerns with Rules CS

Hidden or inadvertent CAPEX tax cut

- (We were told this will be fixed by amendment)
- Repeal of AS 43.55.165(e)(18) as a conforming amendment to elimination of the QCE credit
- This adds 30 cents / barrel in allowable deductions, which actually costs the state \$15-\$20 million / year once prices get above minimum tax level

Concerns with Rules CS

Delayed GVR graduation

- In amendments during SB21, and in prior committees, has been in five to seven year range
- Ten years greatly reduces benefit to the state as by that point many fields are well into their decline
- Reverse of Enalytica analysis: if longer term benefit has minimal impact on producers, it is also of minimal benefit to the state

Concerns with Rules CS

New and technical language changes that could have unintended consequences

- In the 3-year transition period, credits can be earned by any company with a plan of development, including majors (should just be non-producers)
- Definition of “regular” production for time clock to graduate the GVR (suggesting “sustained” definition)
- Carried-forward lease expenditures are not kept separate by “segment,” which can distort the eventual net profit tax paid once the expenditures are applied
- Carried forward expenditure change in .160(a) doesn’t account for the tax changes scheduled for 2022, which is in .160(h). Need to replicate this language.

Summary of Fiscal Impact

Summary Analysis of Bill Versions (\$millions) (based on Spring 2016 Forecast)

	FY 2017			FY 2018			FY 2019			FY 2020		
	HB247 (GOV)	CS HB247 (FIN) amd	CS HB247 (RLS)	HB247 (GOV)	CS HB247 (FIN) amd	CS HB247 (RLS)	HB247 (GOV)	CS HB247 (FIN) amd	CS HB247 (RLS)	HB247 (GOV)	CS HB247 (FIN) amd	CS HB247 (RLS)
Reduced Spending												
Credits Eliminated or Reduced												
North Slope	\$15	\$0	\$0	\$15	\$15	\$15	\$25	\$25	\$30	\$20	\$25	\$115
Cook Inlet / Mid Earth	\$35	\$20	\$5	\$65	\$50	\$30	\$45	\$45	\$45	\$35	\$50	\$110
Credits Deferred												
North Slope	\$30	\$0	\$0	\$80	\$0	\$0	\$95	\$0	\$0	\$45	\$0	\$0
Cook Inlet / Mid Earth	\$0	\$0	\$0	\$30	\$0	\$0	\$40	\$0	\$0	\$20	\$0	\$0
Budget Subtotal	\$80	\$20	\$5	\$190	\$65	\$45	\$205	\$70	\$75	\$120	\$75	\$225
Increased Revenue												
Floor "Hardening"	\$130	\$0	\$0	\$185	\$0	\$0	\$185	\$0	\$0	\$160	\$0	\$70
Floor Increase to 5%	\$45	\$0	\$0	\$45	\$0	\$0	\$55	\$0	\$0	\$80	\$0	\$0
CI Credit Repeal	\$15	\$5	\$0	\$10	\$15	\$0	\$15	\$15	\$10	\$15	\$15	\$15
Revenue Subtotal	\$190	\$5	\$0	\$240	\$15	\$0	\$255	\$15	\$10	\$255	\$15	\$85
Total Bill Impact	\$270	\$25	\$5	\$430	\$80	\$45	\$460	\$85	\$85	\$375	\$90	\$310
NOL Carry-Forward	\$773	\$595	\$610	\$1,128	\$708	\$720	\$1,226	\$666	\$660	\$1,223	\$498	\$685

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Thank You!

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Title: **FY 2016 North Slope Lease Expenditure Comparison:
Actual vs Forecast**

Preparer: Michael Malin, Petroleum Economist, (907) 465-2669

Date: 5/2/2016

Purpose: To show how actual reported FY 2016 North Slope lease expenditures compare to the Spring 2016 forecast.

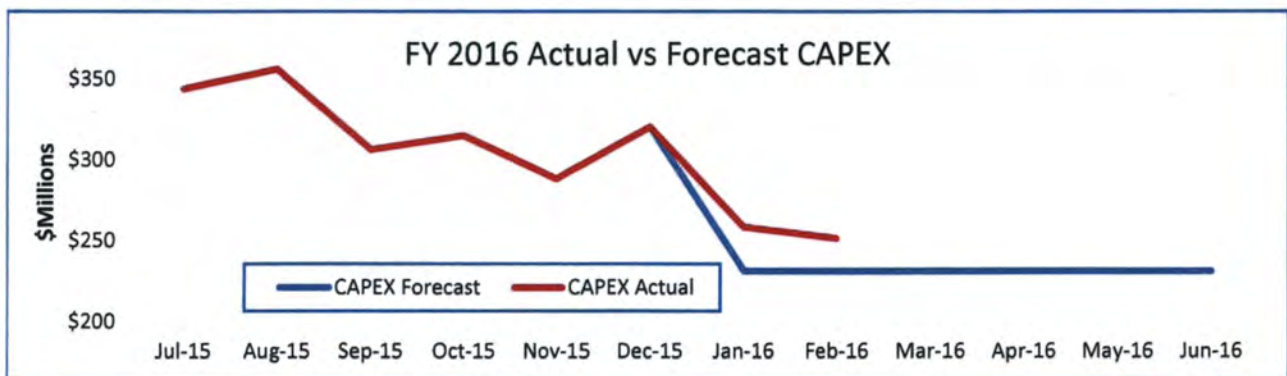
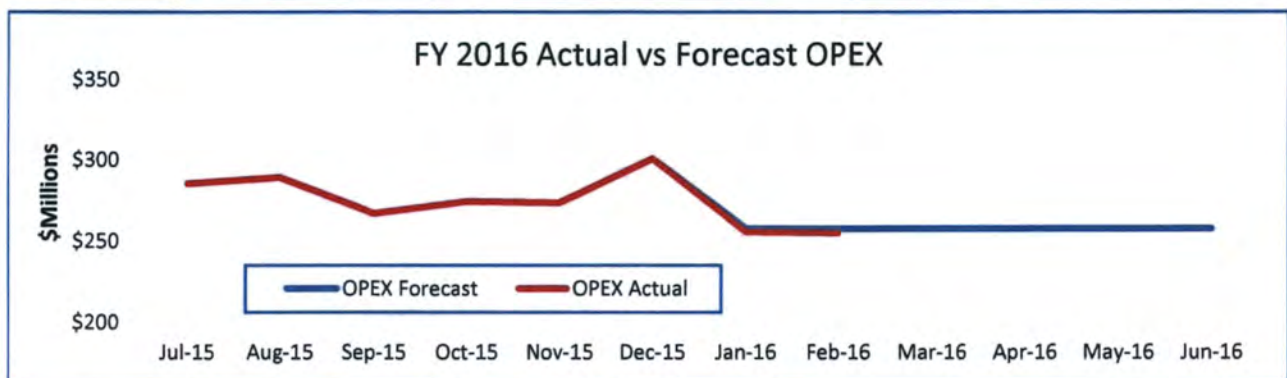
Data Source: Actuals: Taxpayer preliminary monthly filings
Forecast: FY 2016 Spring Forecast

Disclaimer: The Department of Revenue is in the process of reviewing and updating the data on which this analysis is based. As a result, future analysis could have different results.

FY 2016 North Slope Lease Expenditures: Actuals vs Forecast (\$Millions)

Revised May 2, 2016 by Michael Malin

FY 2016	NS OPEX		NS CAPEX	
	OPEX Forecast	OPEX Actual	CAPEX Forecast	CAPEX Actual
Jul-15	\$ 285	\$ 285	\$ 344	\$ 344
Aug-15	\$ 289	\$ 289	\$ 356	\$ 356
Sep-15	\$ 267	\$ 267	\$ 306	\$ 306
Oct-15	\$ 274	\$ 274	\$ 315	\$ 315
Nov-15	\$ 273	\$ 273	\$ 288	\$ 288
Dec-15	\$ 301	\$ 301	\$ 320	\$ 320
Jan-16	\$ 258	\$ 256	\$ 231	\$ 258
Feb-16	\$ 258	\$ 255	\$ 231	\$ 251
Mar-16	\$ 258		\$ 231	
Apr-16	\$ 258		\$ 231	
May-16	\$ 258		\$ 231	
Jun-16	\$ 258		\$ 231	
Difference		(\$5)		\$48



Source:

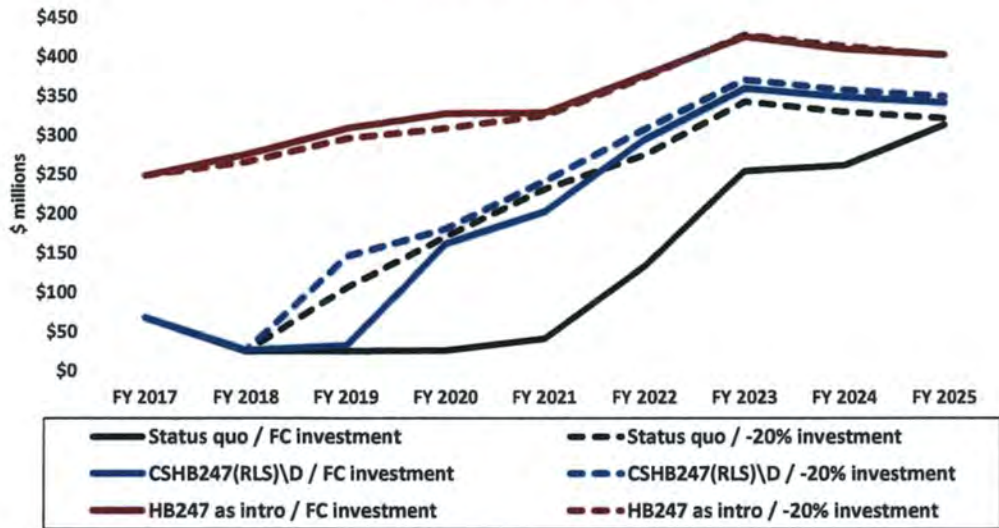
Actuals: Taxpayer preliminary monthly filings for July 2015 to February 2016

Forecast: FY 2016 Spring Forecast

Disclaimer:

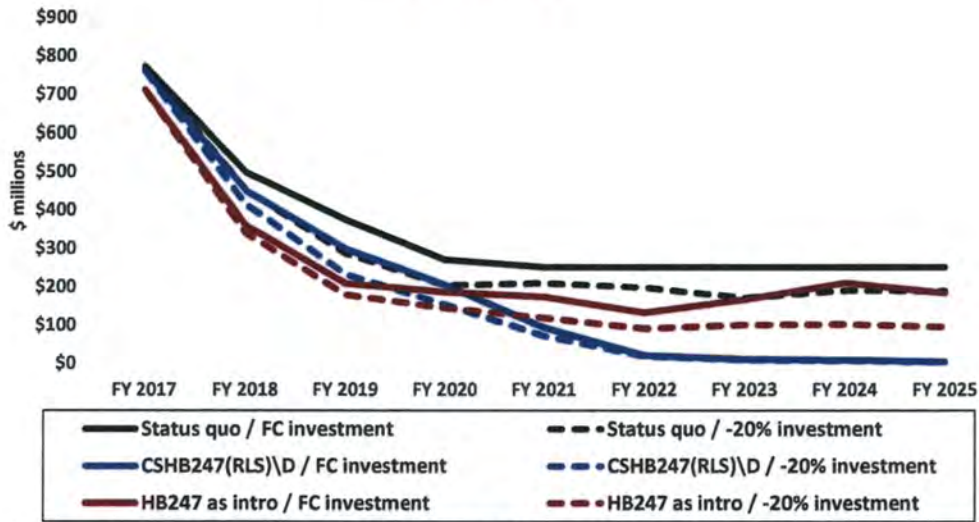
The Department of Revenue is in the process of reviewing and updating the data on which this analysis is based. As a result, future analysis could have different results.

Production Tax Revenue



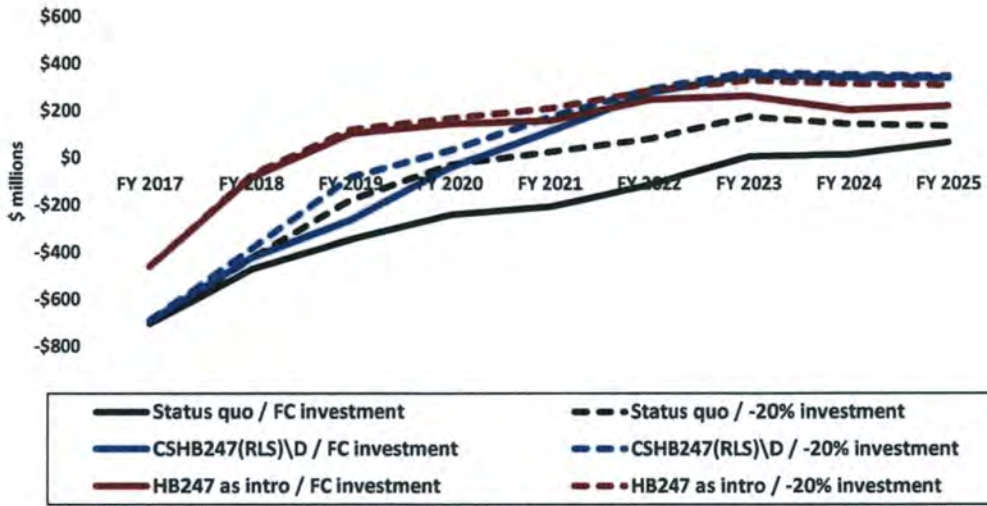
Investment scenarios are shown relative to levels in the spring 2016 forecast. Point estimates shown are one possible outcome within a range.

Refunded credits



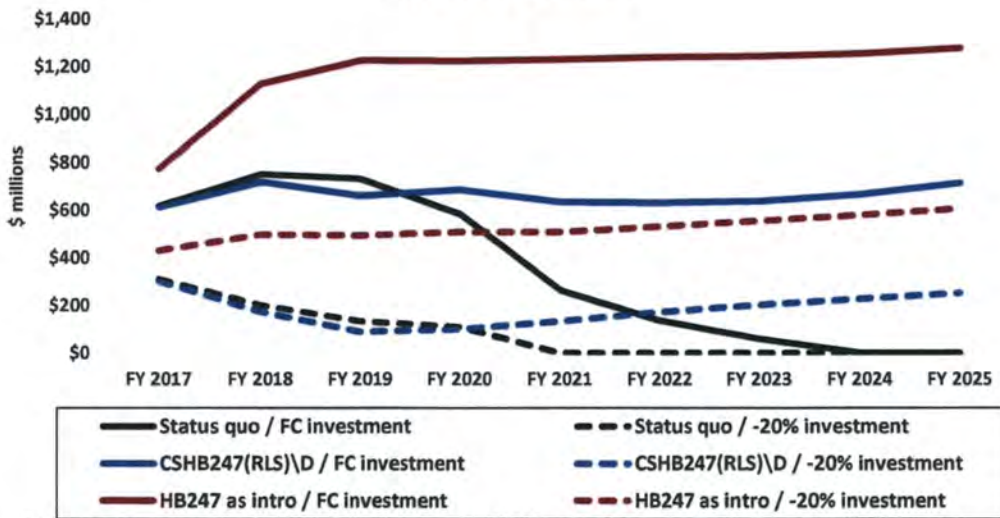
Investment scenarios are shown relative to levels in the spring 2016 forecast. Point estimates shown are one possible outcome within a range.

Production tax net of refunded credits



Investment scenarios are shown relative to levels in the spring 2016 forecast. Point estimates shown are one possible outcome within a range.

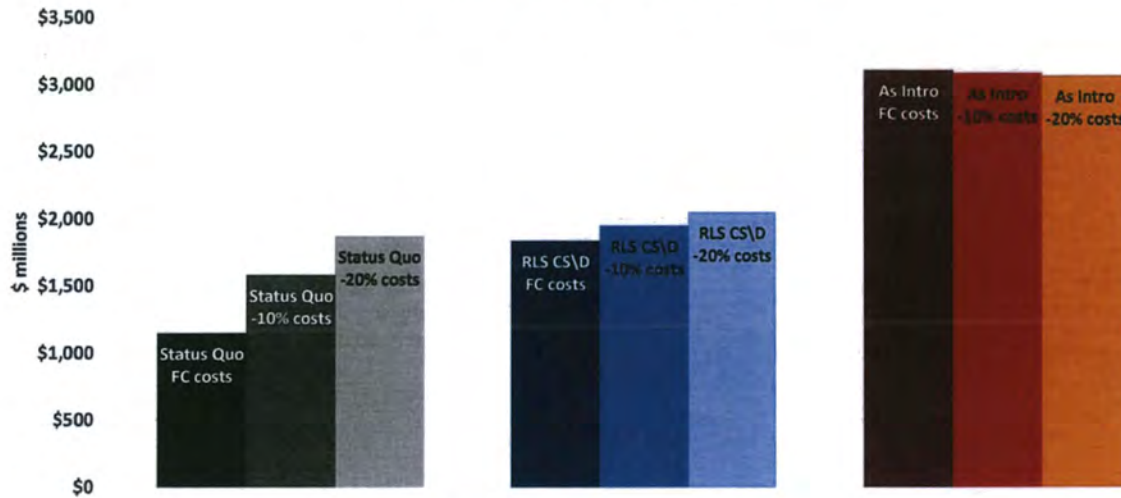
Carryforward balance *



Investment scenarios are shown relative to levels in the spring 2016 forecast. Point estimates shown are one possible outcome within a range.

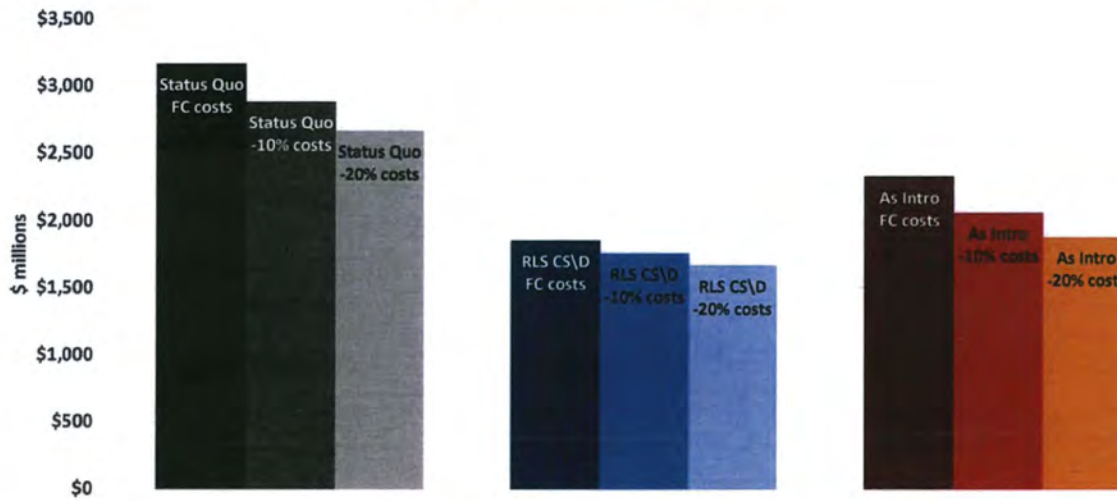
* For CSHB247(RLS), carry forward lease expenditures are converted to credit equivalent assuming 35% tax rate.

Total Production Tax Revenue, FY 17-25



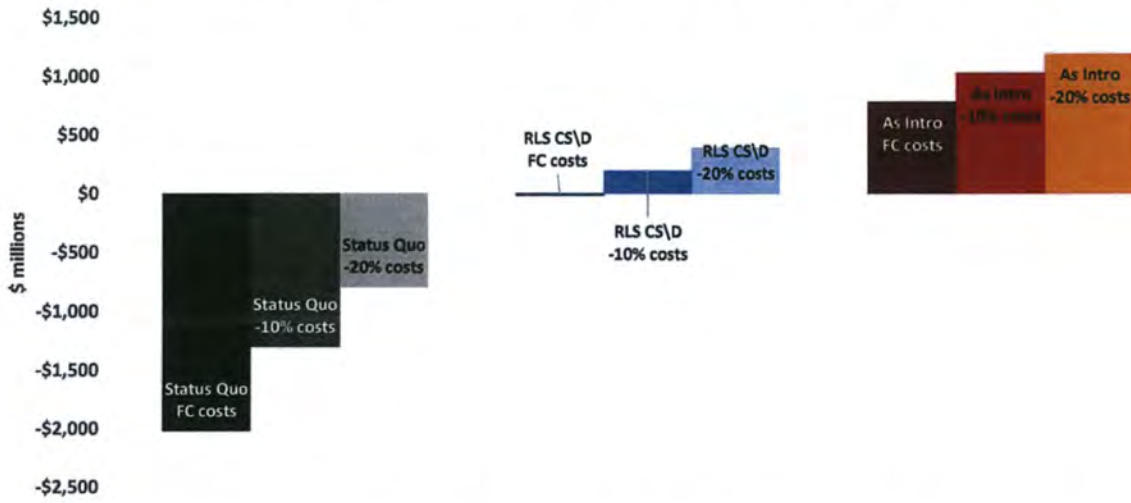
Investment scenarios are shown relative to levels in the spring 2016 forecast. Point estimates shown are one possible outcome within a range.

Total Refunded Credits, FY 17-25



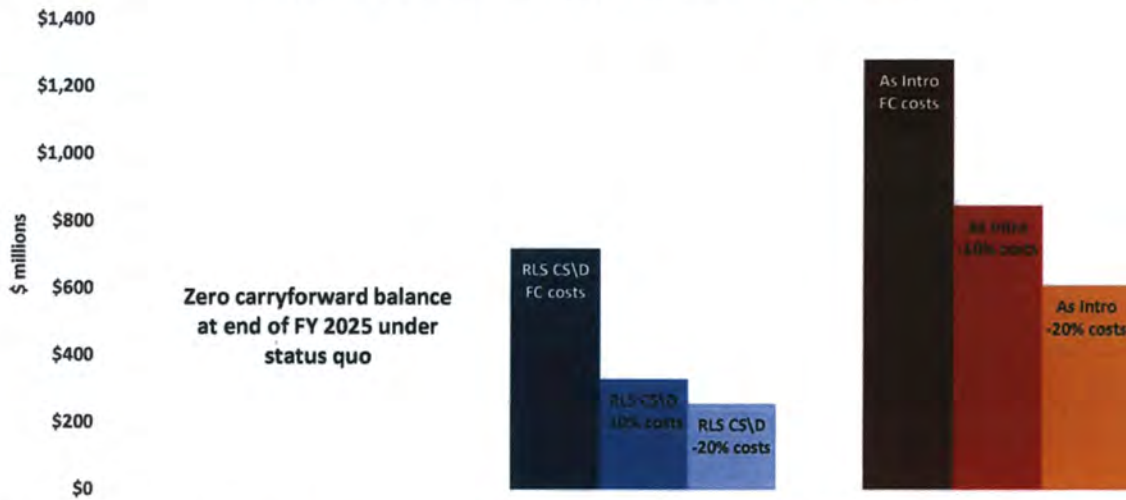
Investment scenarios are shown relative to levels in the spring 2016 forecast. Point estimates shown are one possible outcome within a range.

Total Production Tax Revenue less Refunded Credits, FY 17-25



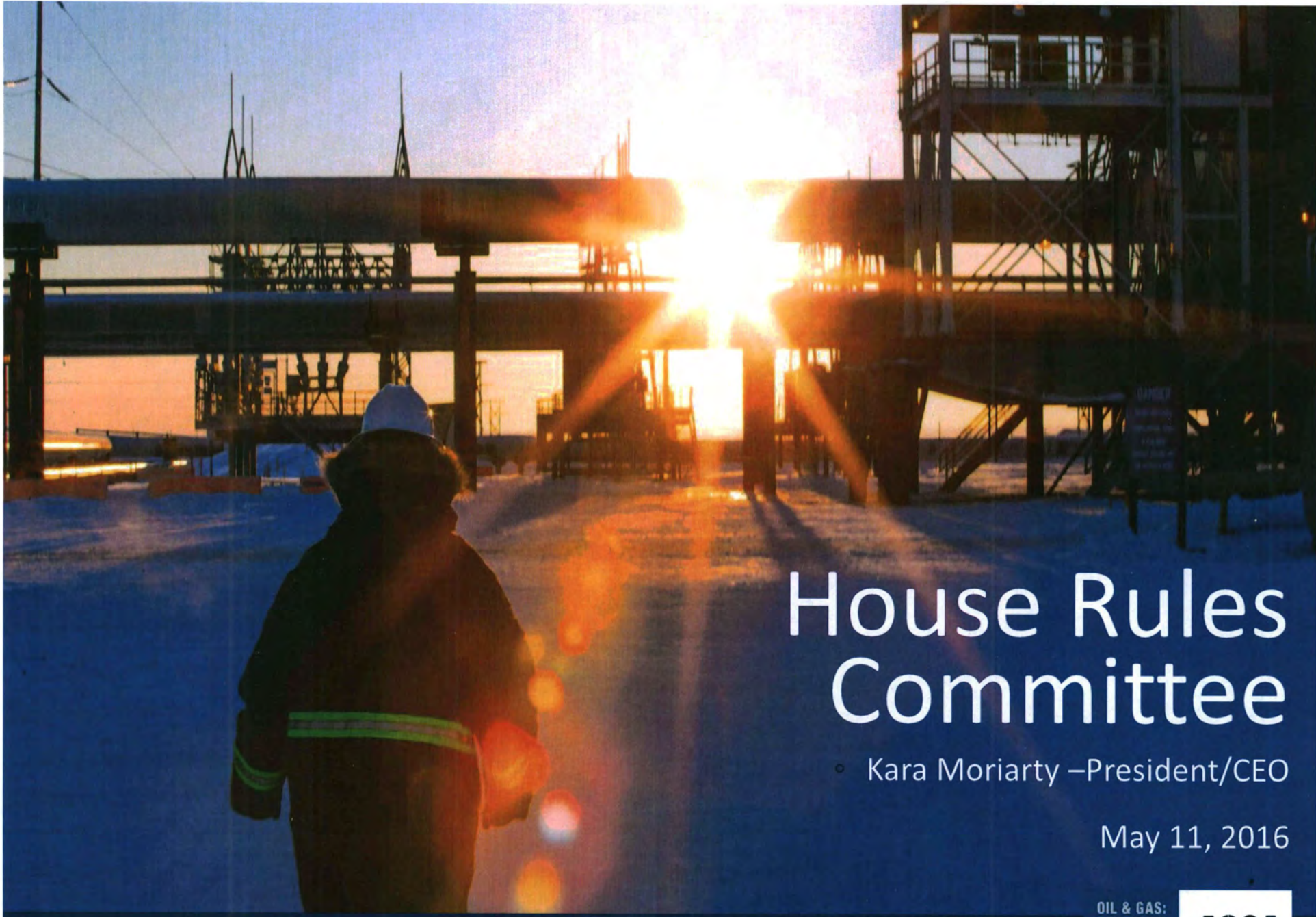
Investment scenarios are shown relative to levels in the spring 2016 forecast. Point estimates shown are one possible outcome within a range.

Carryforward Credit Balance (or equivalent), end of FY 2025



Investment scenarios are shown relative to levels in the spring 2016 forecast. Point estimates shown are one possible outcome within a range.

* For CSHB247(RLS), carry forward lease expenditures are converted to credit equivalent assuming 35% tax rate.

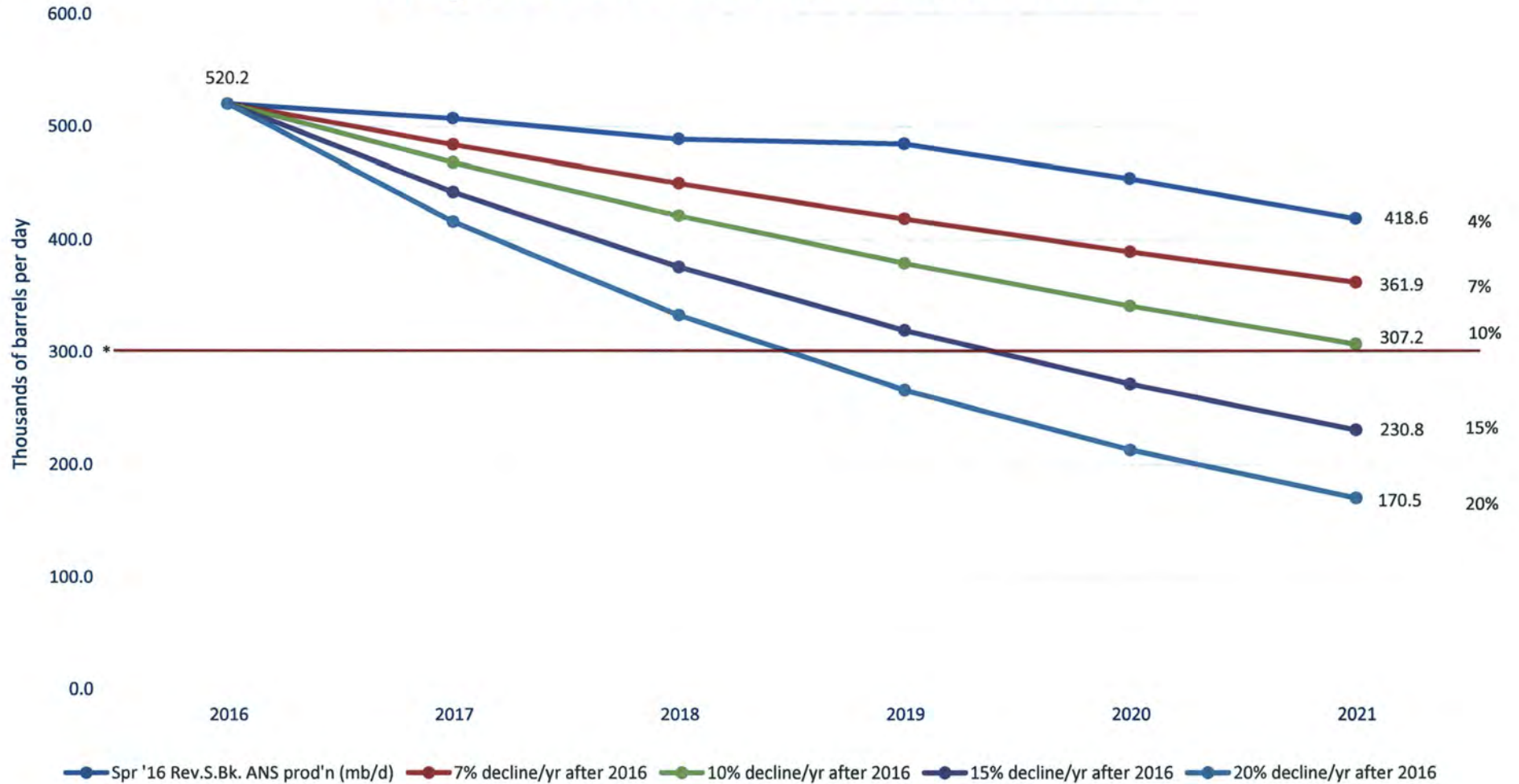


House Rules Committee

◦ Kara Moriarty –President/CEO

May 11, 2016

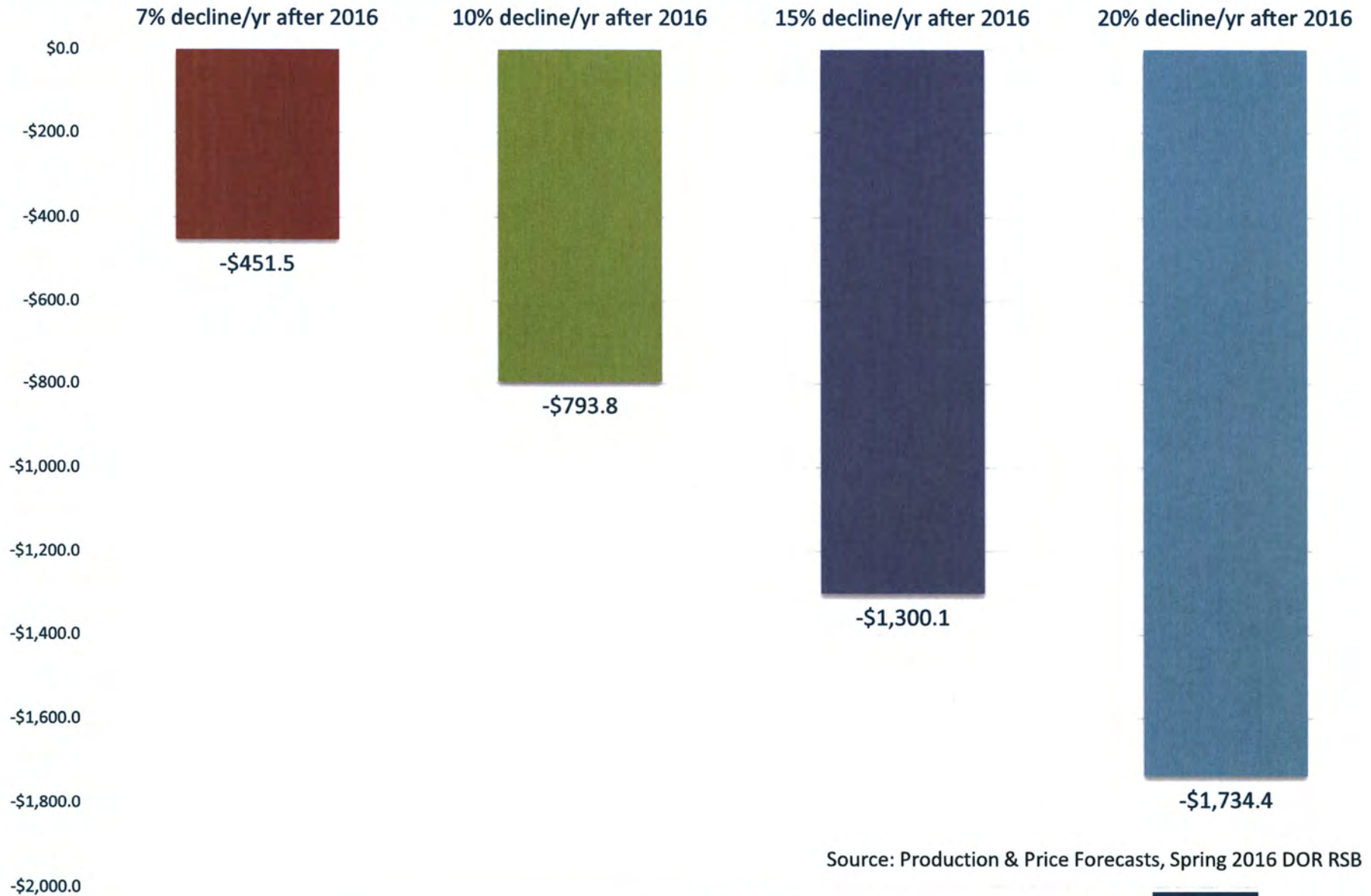
Projected Production Decline Curves



Source: Production & Price Forecasts, Spring 2016 DOR RSB

*According to Alyeska Pipeline Service Company, the Trans-Alaska Pipeline System (TAPS) faces a significant operational obstacle at 300,000 barrels per day. Despite some of the best and most innovative people in the industry focused on this scenario, an operational solution has not yet been identified to sustain TAPS operations below this level.

Cumulative Reduction in Royalty Value after 5 years/Decline (\$MM)




House Rules Committee

CSHB247(RLS)\ D

Scott Jepsen, VP External Affairs
Paul Rusch, VP Finance
ConocoPhillips Alaska

May 11, 2016

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Tax Credits and Applicability to COP

Tax Credit Type	Total FY17 estimate, \$MM	Total reimbursable	COP reimbursement	Total used against severance tax liability	COP used against severance tax liability
Net operating loss	452	370	0 – Not eligible	82	0. Possible for calendar year '16, but self correcting.
Exploration	76	76	0 – Not eligible	0	Possible for 2016. Expires this year.
Small producer	27	NA	NA	27	0 – Not eligible
Per barrel production credit	16	NA	NA	16	Depends upon oil price and expenditures.
Cook Inlet and Middle Earth	337	326	0 – Not eligible	11	0. Assumes sale of Tyonek. Kenai LNG not deductible.
Total	908	772	0 – Not eligible	136	Potential for an NOL. Dependent upon oil price and expenditures.

- In 2015, COP incurred obligations to the SoA of \$665MM. Negative cash flow in excess of \$100MM.
- In 1Q 2016, incurred obligations of \$77MM. Cash flow approximately -\$100MM.

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May 11, 2016

Agenda

- Look back since SB21 passed
- Economic Environment
- Key Concerns with CSHB247(RLS)\D
- 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 during construction
- **Active Exploration Program**
 - Two wells drilled in 2014
 - Acquired GMT1 Seismic – 2015
 - Three wells in 2016 (NPRA)



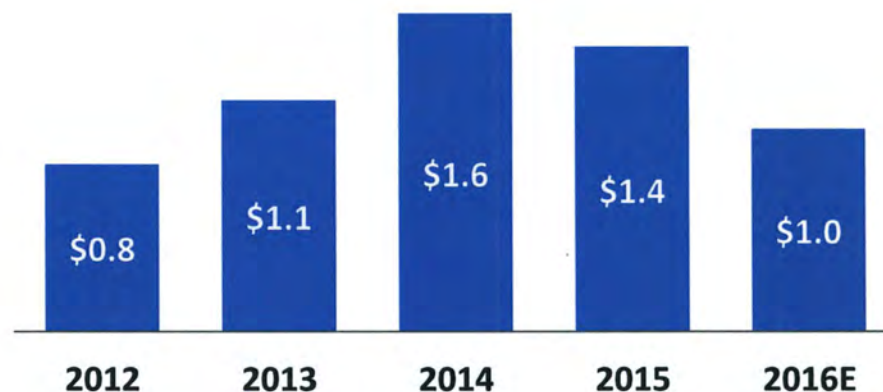
Capital Spending Trends

ConocoPhillips Capital Spend (\$B)



Total Company capital reduced 63% since 2014

ConocoPhillips Alaska Capital Spend (\$B)

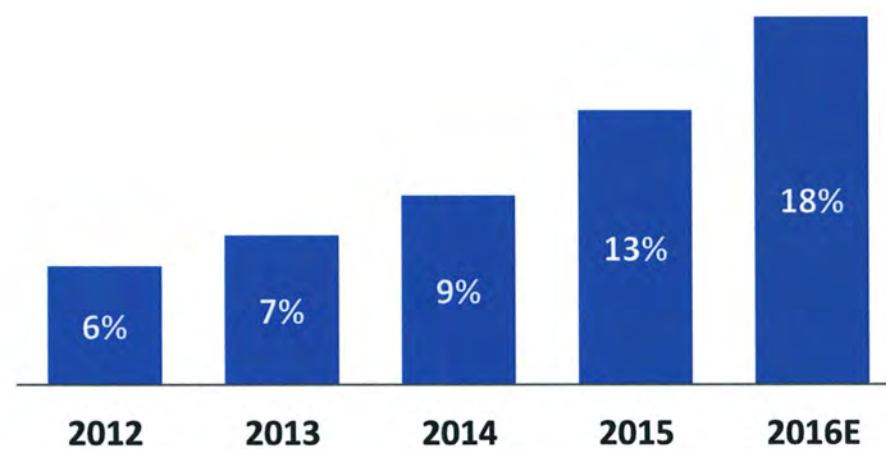


2016E Alaska capex ~ 25% higher than ACES years (~\$0.8 B/yr 2007-2012)

ANS WC Oil Prices (\$/bbl)

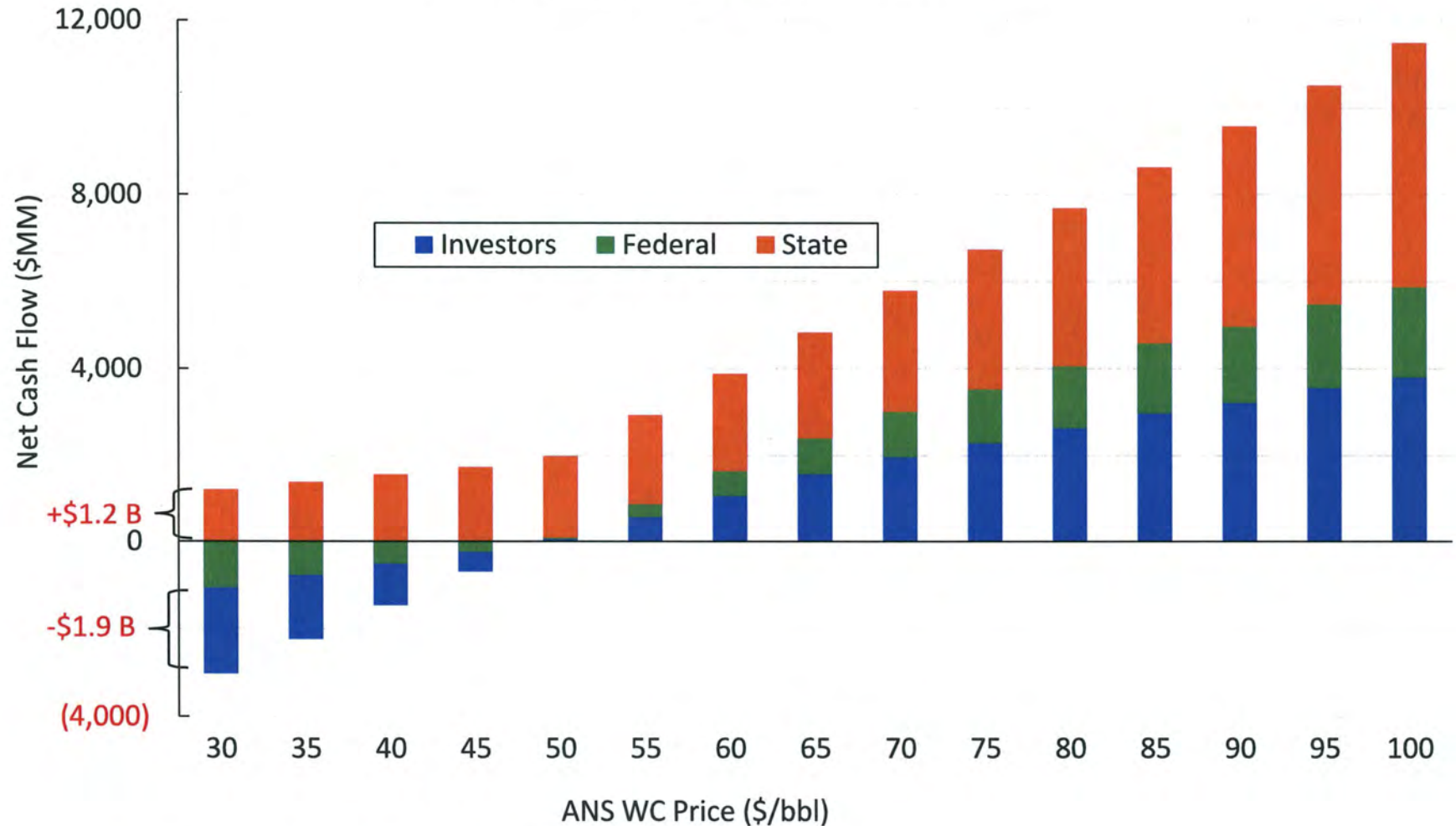


Alaska Capex as % of COP Total



North Slope Investors Negative at Current Pricing

2017 FY Cash Flow - Spring 2016 RSB assumptions



State share shown excludes tax credits other than production tax credits

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Key Concerns with Original HB247

- 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 & Q1 2016
- Hard minimum tax floor
 - Represents a potential tax increase when oil prices are low – moving in the wrong direction
- Increase interest rate on taxes due
 - 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 credits to the monthly installment contradicts the principle of an annual tax levy
- Taxpayer confidentiality

View on Current Draft CSHB247 (RLS) \ D

- NOL tax credit – extend through 2019 consistent with small producer tax credits
 - Not anticipating long-term loss position
- Interest rate increased without addressing underlying audit issues
- GVR 10-year time limit potentially makes new oil developments less competitive
- Disclosure requirements reasonably restricted to reimbursable credit related information

Observations

- CSHB247(RLS) \ D an improvement over original bill
- Any changes that increase tax burden/costs could adversely impact ConocoPhillips current and future investments
- Significant changes in tax law would validate concerns regarding State's ability to implement a stable oil and gas fiscal policy
 - Only 20 months since SB21 ratified by voters
 - Long-term investment requires durable, reasonable fiscal framework

House Rules Committee


CSHB247(RLS)\ D

Scott Jepsen, VP External Affairs

Paul Rusch, VP Finance

ConocoPhillips Alaska

May 11, 2016

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1. Strong Investment Value of Tax Credits
2. Overview of Cosmopolitan Unit
3. Specific Impact of HB 247 CS on BlueCrest



Via Teleconference

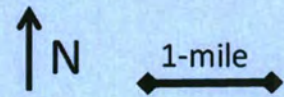



J. Benjamin Johnson
House Rules Committee Testimony
May 11, 2016


Cosmopolitan Project Area

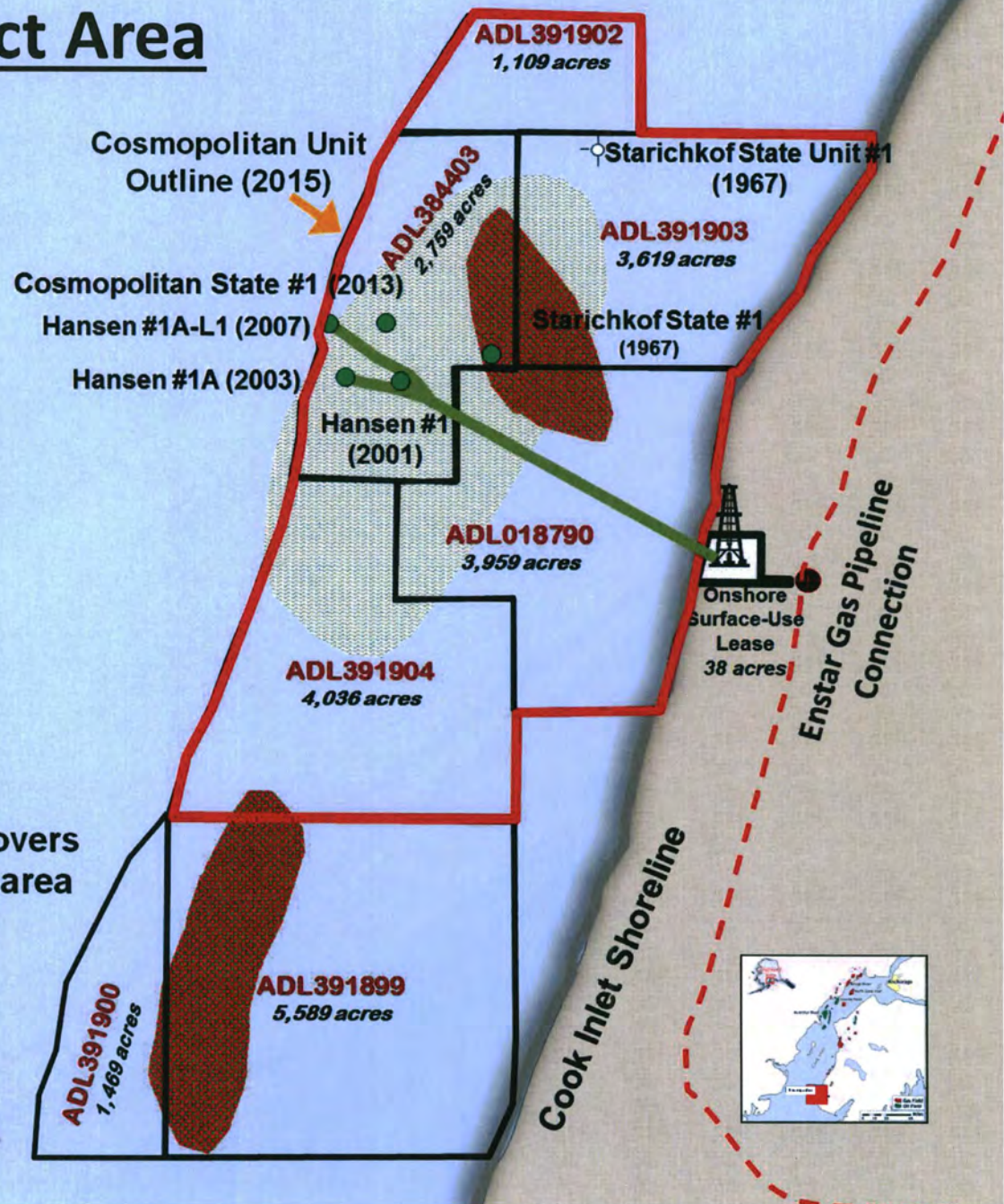
- 100% owned and operated by BlueCrest
- 7 State leases
- 22,540 acres offshore
- 38-acre onshore surface lease
- 6 wells drilled to date
- 6 known oil zones
- 6+ known gas zones
- 2 identified exploratory prospects

3-D Seismic covers entire Project area (2005)



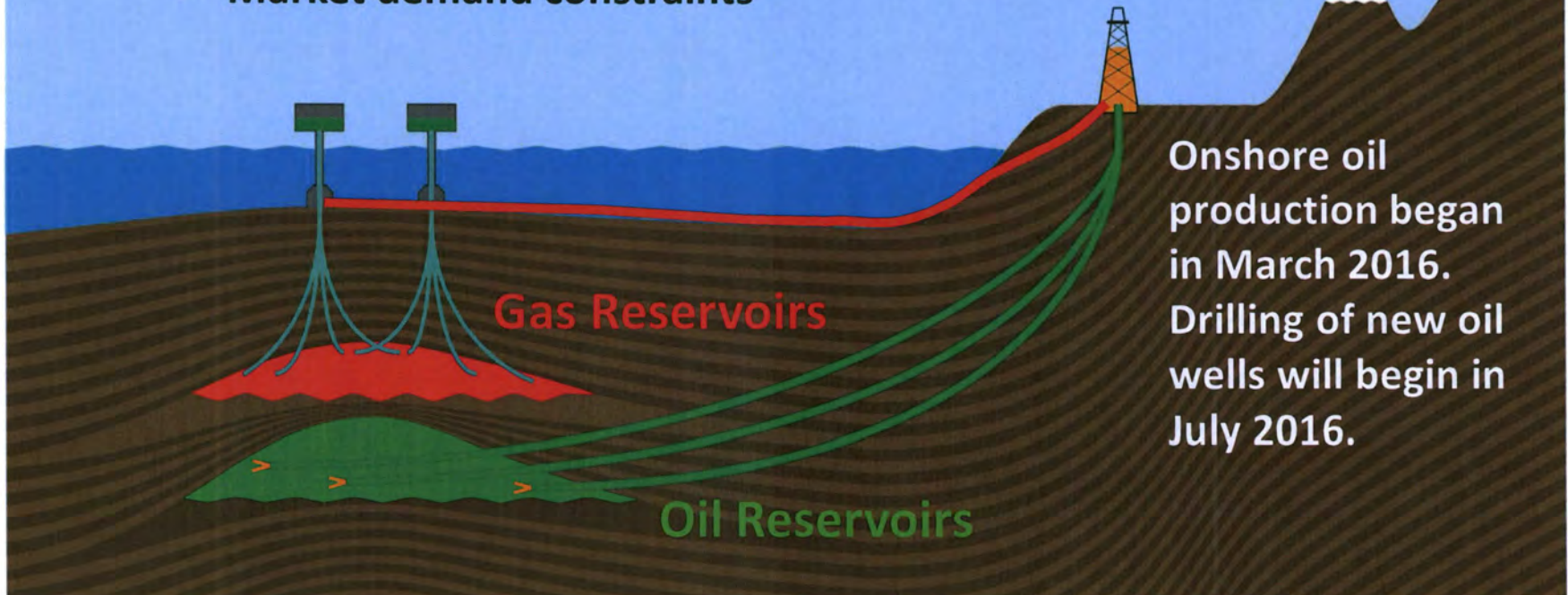
 Approximate areal extent of known productive reservoirs

 Approximate areal extent of identified exploratory prospects



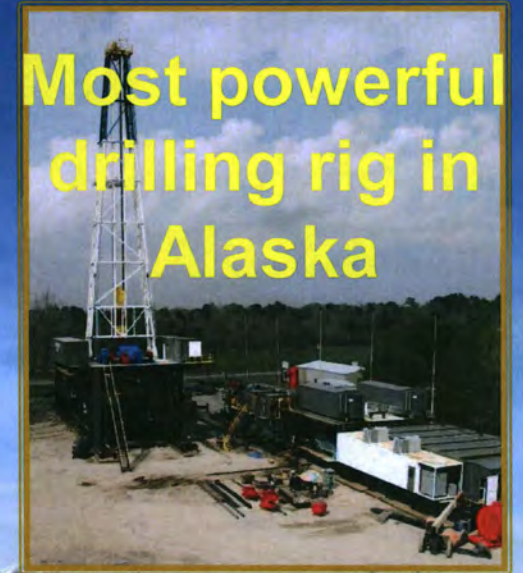
Cosmopolitan Unit Development

- Separate oil and gas reservoirs are located approximately three miles offshore in the Cook Inlet
- The oil reservoirs can be reached by drilling wells from onshore
- The gas reservoirs are not as deep and can only be reached with offshore wells and platforms
 - Gas development is now on hold due to:
 - Economic limitations
 - Market demand constraints



Cosmopolitan Progress as of 05/10/2016

Most powerful
drilling rig in
Alaska



38-acre Drill Site and Production Facility

Tangible Results

BlueCrest sells first oil

Posted: April 26, 2016 - 9:05pm | Updated: April 26, 2016 - 9:15pm



Photo courtesy Carlile Transportation Systems
Workers unload an oil tanker full of oil from the Cosmopolitan development near Anchor Point at the Tesoro refinery in Nikiski on Thursday, April 21.

By ELIZABETH EARL

Peninsula Clarion

BlueCrest Energy sold its first barrel of oil from its new Cosmopolitan development last week to the Tesoro refinery in Nikiski.

Carlile Transportation Systems, a trucking and logistics company that provides oilfield support, transported the first oil produced by the facility on Thursday to Tesoro's refinery.

The company expects to drive two tankers a day from the Cosmopolitan site near Anchor Point to the refinery each day, according to a press release from Carlile.

Tesoro Kenai Refinery Vice President Cameron Hunt said in the press release that Tesoro was

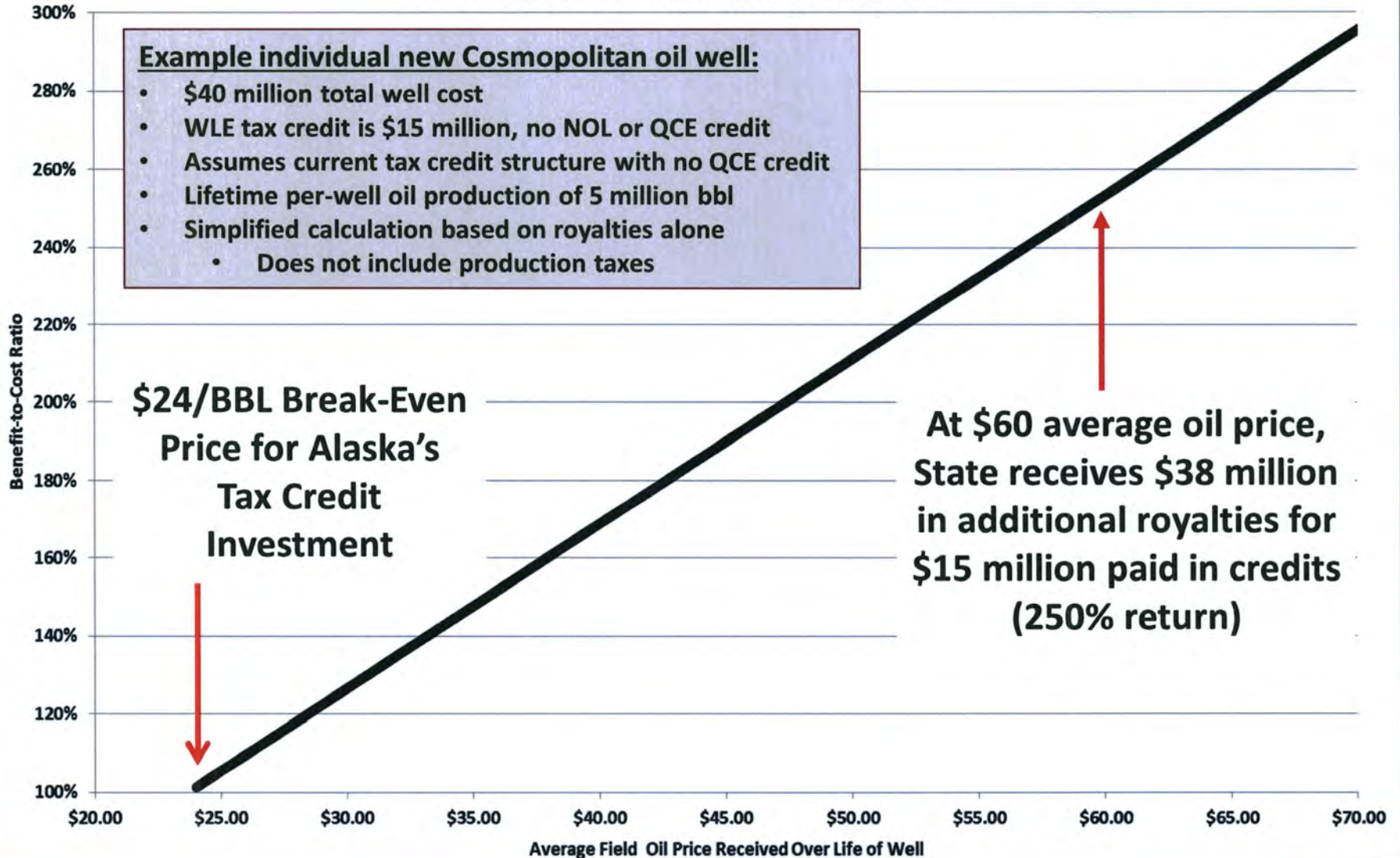
Continuation of Cook Inlet Credits

- **Cook Inlet oil has high value to the State**
 - Lower infrastructure deductions and higher quality than NS
 - All CI oil is refined and used in Alaska
- **Credits are particularly important with low oil prices**
- **Continued drilling in new developments after start-up is mostly impacted by the WLE credits**
 - Higher WLE credits facilitate continued drilling
 - The existing 40% credit allows drilling of new wells
 - \$10/bbl lower oil prices than without the credit
- **Once a drilling program has been suspended, even higher prices are required to resume**
- **For each new development well drilled as a result of continued credits, the return to the State is low-risk and high-reward**

State's Investment Return through Royalties from Each New Cosmopolitan Well

BlueCrest Calculation of State's Benefit-to-Cost Ratio versus Average Lease Oil Price

Assumes only WLE Tax Credit Paid (total 38% of Well Cost)



Per-Company Limits for Cash Payments

- **BlueCrest has already invested in good faith, based on the tax policy in existence when the investments were committed**
- **BlueCrest has financed the Cosmopolitan development assuming the credits would be fully paid on time**
- **BlueCrest has already entered into (and financed) spending commitments through 2016, based on the State's existing credit repurchase practice**

Effective Date

An effective date prior to early 2017 is too soon for reductions in tax credits for ongoing work that has already been contracted for and is now underway

BlueCrest's funding plan for initial Cosmopolitan oil development

Total cost to reach sustainability (2 new wells): \$525 million

Funding sources

Cash investment by shareholders: \$200 million

AIDEA loan on drilling rig: \$30 million

Development loan: \$150 million

Tax credits received to date: \$24 million

Tax credits for 2015 & 2016 spending (2 years, current law): \$121 million

**We are getting close,
but we must
finish the climb!**



Drilling begins July 2016

Answers to questions on Rules CS

Please note that, in the interest of expedience, where I have made reference to specific fiscal regimes, the details cited were accurate to the best of my knowledge when I last did specific research on these fiscal regimes; I haven't checked for updates or changes in the last year or two, since these are used for illustrative purposes only, and given the timeframe of legislative discussion, I wanted to be able to get these answers back as quickly as possible.

Regarding net profit systems elsewhere in the world:

- a. **Do they let you recover costs?** Recovery of costs is the defining feature of any net profit tax; it is deductibility of costs that differentiates net from gross taxes. The ability to carry forward costs that cannot be deducted in the year in which they were incurred because the company is in a loss position is similarly common to almost all net profit taxes (whether broad-based, economy-wide income taxes, or specific petroleum sector taxes). Alaska has always been unusual in providing this carry-forward ability through a separate credit; the overwhelming majority of jurisdictions simply do this by having undeducted expenses (losses) be carried forward to deduct against future years' income or cashflow.
 Exceptions:
 - i. The only example I am aware of of a net profit system that does not allow carry forward of expenses is in Trinidad & Tobago, and there it applies only to very small components of the overall fiscal regime. There, the core of the fiscal regime is a 50% Petroleum Profits Tax, under which losses may be carried forward indefinitely. However, there are small components of the regime – an unemployment levy and a petroleum production levy (5% and 4% tax rates respectively) which are notionally levied on a net basis, but which do not allow carry forward of losses. This is about the only example I can think of at the moment of a net tax (in this case a very small piece of the overall system) that does not allow carry forward of losses.

- b. **Do they cap how many years you can carry forward losses? If so, how many years?** Some jurisdictions allow unlimited carry forward of undeducted expenses, other systems impose a cap with regard to the number of years of carry forward. In my experience, specific petroleum rent taxes are more likely to have unlimited carry forward, while limitations on carry forward are more often found in general corporate income taxes.
 Details:
 - i. In the US at the general federal income tax level, US Code 172(b)(1)(A) allows taxpayers to carry losses backward (ie use against past liability, for a refund) 2 years, and forward 20 years.
 - ii. Alaska, to my understanding, mirrors the federal code in the carry forward and backward it allows for state corporate income tax. Most US states follow the federal example in allowing 20 years of carry forward, although several states limit to 15, 12 or 10 years, and a few limit to 7 or 5.
 - iii. Internationally, many of the petroleum net-tax jurisdictions that look most like Alaska's production tax (ie UK, Australia, Norway) allow unlimited carry-forward, and in many cases allow for carry forward with some form of interest/uplift to maintain the time value of those deductions.
 - iv. In Australia, undeducted expenses are carried forward indefinitely at an uplift rate of the long-term government bond rate + 5% each year (or + 15% for the case of exploration-related expenses). The purpose of this uplift is to maintain the time value of money for companies of these undeducted costs.

- v. In the UK similarly, many undeducted costs receive a 10% annual uplift, for a maximum of 6 years, although carry forward itself is not limited, and losses can also be carried backward one year.
 - vi. In Norway, for the first four years of development costs are 'uplifted' (ie the deduction value is increased) by 5.5% each year, so that after four years the costs are worth 22% more than the actual costs incurred. This figure was previously 30% (7.5% per year) and was reduced in 2013.
 - vii. The Netherlands has different carry-forward rules for their petroleum profit tax (the State Profit Share, or SPS) and their corporate income tax. For corporate income tax, losses can be carried forward up to 9 years and back 1 year, while for SPS losses can be carried forward indefinitely, and back 3 years.
 - viii. In a wide range of other countries where corporate income tax is a key part of the overall fiscal regime, time-limited loss carry-forward is common place, with the most common limits being 5, 7, 10 or 15 years.
- c. **What considerations should we think about if we cap the number of years you can carry forward?** The desire to cap the number of years that expenses may be carried forward to protect the state is certainly very reasonable. The key thing that must be understood is that unlike the regimes referred to above that limit the number of years that losses may be carried forward, Alaska has in place the gross minimum tax, which will effectively become binding against losses as a result of switching from a NOL credit to a system of simply deducting carried-forward expenditures.

This means that, in a persistent low-price environment, it could take companies many more years than might otherwise be the case to be in a position to have sufficient liability above the floor gross tax amount to be able to deduct carried forward expenses. For this reason, a time limit at the shorter end of the spectrum referred to above (for instance, 5 years) may not be reasonable.

In my opinion, given the presence of the 4% gross minimum floor, a 7 year limit on how long expenses may be carried forward is probably the minimum that might be reasonable. Companies may have some significant concerns about the possibility that a permanent loss of deduction value could occur through the combination of such a limit and the gross floor; however in general I think many companies will also understand that if we remain in this challenged a price/cost environment for multiple years, the political willingness of the state to maintain an indefinite buildup of undeducted costs (either as costs or as credits) is going to be limited – an explicit, statutory limit may in some ways be preferable to an implicit but uncertain, political limit.

Finally, with the proposed phase-out of refundable NOL credits, it is important to point out that for explorers or new developers without current production, any clock for a time-limited carry forward would likely need to start at the commencement of regular production. One might also want to consider a longer time-horizon for recovery of costs for such companies, since new developers evidently have far more costs to recover (relative to their future revenue) in most cases than legacy producers who are temporarily in a loss situation as a result of low prices.

Please don't hesitate to let me know if there are further questions on these matters.

Best regards,

Janak Mayer

Chairman & Chief Technologist