

ALASKA LEGISLATURE

HOUSE and SENATE FINANCE COMMITTEE FILES, 2005-2006 3090

1 with the terms of a unit operating agreement or similar operating agreement if the
2 Department of Revenue finds that

3 (A) the pertinent provisions of the operating agreement are
4 substantially consistent with the Department of Revenue's determinations and
5 standards otherwise applicable under this subsection; and

6 (B) at least one working interest owner party to the agreement,
7 other than the operator, has substantial incentive and ability to effectively audit
8 billings under the agreement;

9 (3) an activity does not need to be physically located on or near the
10 premises of the lease or property from which oil or gas is recovered in order for the
11 cost of the activity to be a cost upstream of the point of production of the oil or gas.

12 (d) For purposes of (c) of this section, "direct costs"

13 (1) includes

14 (A) an expenditure, when incurred, to acquire an item if the
15 acquisition cost is otherwise a direct cost, notwithstanding that the expenditure
16 may be required to be capitalized rather than treated as an expense for financial
17 accounting or federal income tax purposes;

18 (B) payments of property taxes, sales and use taxes, motor fuel
19 taxes, and excise taxes;

20 (C) a reasonable allowance, as determined under regulations
21 adopted by the department, for overhead expenses directly related to exploring
22 for, developing, and producing oil or gas deposits located within leases or
23 properties or other land in the state;

24 (2) does not include

25 (A) depreciation, depletion, or amortization;

26 (B) oil or gas royalty payments, production payments, lease
27 profit shares, or other payments or distributions of a share of oil or gas
28 production, profit, or revenue;

29 (C) taxes based on or measured by net income;

30 (D) interest or other financing charges or costs of raising equity
31 or debt capital;

1 (E) acquisition costs for a lease or property or exploration
2 license;

3 (F) costs arising from fraud, wilful misconduct, or negligence;

4 (G) fines or penalties imposed by law;

5 (H) costs of arbitration, litigation, or other dispute resolution
6 activities that involve the state or concern the rights or obligations among
7 owners of interests in, or rights to production from, one or more leases or
8 properties or a unit;

9 (I) donations;

10 (J) costs incurred in organizing a partnership, joint venture, or
11 other business entity or arrangement;

12 (K) amounts paid to indemnify the state; the exclusion
13 provided by this paragraph does not apply to the costs of obtaining insurance
14 or a surety bond from a third-party insurer or surety;

15 (L) surcharges levied under AS 43.55.201 or 43.55.300;

16 (M) for a transaction that is an internal transfer or is otherwise
17 not an arm's length transaction, expenditures incurred that are in excess of fair
18 market value;

19 (N) an expenditure incurred to purchase an interest in any
20 corporation, partnership, limited liability company, business trust, or any other
21 business entity, whether or not the transaction is treated as an asset sale for
22 federal income tax purposes;

23 (O) a tax levied under AS 43.55.011;

24 (P) the portion of costs incurred for dismantlement, removal,
25 surrender, or abandonment of a well, facility, pipeline, platform, or other
26 structure, or for the restoration of a lease, field, unit, area, body of water, or
27 right-of-way in conjunction with dismantlement, removal, surrender, or
28 abandonment, that is attributable to production of oil or gas occurring before
29 July 1, 2006; the portion is calculated as a ratio of the amount of oil and gas
30 production associated with the well, facility, pipeline, platform, or other
31 structure, lease, field, unit, area, body of water, or right-of-way occurring

1 before July 1, 2006 to the total amount of oil and gas production associated
2 with that well, facility, pipeline, platform, or other structure, lease, field, unit,
3 area, body of water, or right-of-way through the end of the calendar month
4 before commencement of the dismantlement, removal, surrender, or
5 abandonment; for purposes of the ratio calculated under this subparagraph,
6 6,000 cubic feet of gas is considered to be equivalent to one barrel of oil.

7 (e) A producer's lease expenditures must be adjusted by subtracting certain
8 payments or credits received by the producer, as provided in this subsection. If one or
9 more payments or credits subject to this subsection are received by a producer during
10 a month or, under (f) of this section, during a calendar year, and if either the total
11 amount of the payments or credits exceeds the amount of the producer's lease
12 expenditures or the producer has no lease expenditures, the producer shall nevertheless
13 subtract those payments or credits from the lease expenditures or from zero,
14 respectively, and the producer's adjusted lease expenditures for that month or calendar
15 year are a negative number and shall be applied to the calculation under (a) of this
16 section as a negative number. The payments or credits that a producer shall subtract
17 from the producer's lease expenditures, or from zero, under this subsection are
18 payments or credits, other than tax credits, received by the producer for

19 (1) the use by another person of a production facility in which the
20 producer has an ownership interest or the management by the producer of a production
21 facility under a management agreement providing for the producer to receive a
22 management fee;

23 (2) a reimbursement or similar payment that offsets the producer's
24 lease expenditures, including a payment from the state or federal government for
25 reimbursement of the producer's upstream costs, including costs for gathering,
26 separating, cleaning, dehydration, compressing, or other field handling associated with
27 the production of oil or gas upstream of the point of production;

28 (3) the sale or other transfer of

29 (A) an asset, including geological, geophysical, or well data or
30 interpretations, acquired by the producer as a result of a lease expenditure or an
31 expenditure that would be a lease expenditure if it were incurred on or after

1 July 1, 2006; for purposes of this subparagraph,

2 (i) if a producer removes from the state, for use outside
3 the state, an asset described in this subparagraph, the value of the asset
4 at the time it is removed is considered a payment received by the
5 producer for sale or transfer of the asset;

6 (ii) for a transaction that is an internal transfer or is
7 otherwise not an arm's length transaction, if the sale or transfer of the
8 asset is made for less than fair market value, the amount subtracted
9 must be the fair market value; and

10 (B) oil or gas

11 (i) that is not considered produced from a lease or
12 property under AS 43.55.020(e); and

13 (ii) the cost of acquiring which is a lease expenditure
14 incurred by the person that acquires the oil or gas.

15 (f) In place of the adjusted lease expenditures for a month under (a) of this
16 section, a producer may, at any time, elect to substitute, for every month of a calendar
17 year, 1/12 of the producer's adjusted lease expenditures for the calendar year. An
18 election made under this subsection applies to calculation of the tax under
19 AS 43.55.011(e) and (g).

20 (g) The department shall specify or approve a reasonable allocation method
21 for determining the portion of a cost that is appropriately treated as a lease expenditure
22 under (c) of this section if a cost that would otherwise constitute a lease expenditure
23 under (c) of this section is incurred to explore for, develop, or produce

24 (1) both an oil or gas deposit located within land outside the state and
25 an oil or gas deposit located within a lease or property, or other land, in the state; or

26 (2) an oil or gas deposit located partly within land outside the state and
27 partly within a lease or property, or other land, in the state.

28 (h) For purposes of AS 43.55.024(a) and (b) and only as to expenditures
29 incurred to explore for an oil or gas deposit located within land in which an explorer
30 does not own a working interest, the term "producer" in (b), (c), and (e) of this section
31 includes "explorer."

1 (i) The department may adopt regulations that establish additional standards
 2 necessary to carrying out the purposes of this section, including the incorporation of
 3 the concepts of 26 U.S.C. 482 (Internal Revenue Code), as amended, the related or
 4 accompanying regulations of each of that section, and any ruling or guidance issued
 5 by the United States Internal Revenue Service that relates to that section.

6 (j) For purposes of this section,

7 (1) "explore" includes conducting geological or geophysical
 8 exploration, including drilling a stratigraphic test well;

9 (2) "ordinary and necessary" has the meaning given to "ordinary and
 10 necessary" in 26 U.S.C. 162 (Internal Revenue Code), as amended, and regulations
 11 adopted under that section;

12 (3) "stratigraphic test well" means a well drilled for the sole purpose of
 13 obtaining geological information to aid in exploring for an oil or gas deposit and the
 14 target zones of which are located in the state.

15 **Sec. 43.55.170. Additional nontransferable tax credit.** (a) For a month for
 16 which a producer's tax liability under AS 43.55.011(e) exceeds zero before application
 17 of any credits under this chapter, a producer that is qualified under (c) of this section
 18 and, during the calendar year, has incurred a qualified capital expenditure, as that term
 19 is defined in AS 43.55.024, may apply a tax credit under this section, in an amount
 20 that does not exceed one-half of the amount of that expenditure, against that liability.
 21 An unused portion of a tax credit may be applied to the extent otherwise allowed
 22 under this section for one or more months during the same calendar year. A tax credit
 23 authorized by this subsection may not be applied

24 (1) to reduce a producer's tax liability under AS 43.55.011(e) for any
 25 month below zero;

26 (2) if application of the credit would cause the total of the tax credits
 27 applied by the producer under this subsection during a calendar year to exceed
 28 \$12,000,000; or

29 (3) by a producer that

30 (A) had commercial production of oil or gas from at least one
 31 lease or property in the state before July 1, 2006, if, during 2016, application of

1 the credit would cause the total of the tax credits applied by the producer under
2 this section to exceed \$6,000,000; or

3 (B) did not have commercial production from a lease or
4 property in the state before July 1, 2006, if application of the credit would
5 cause the total of all tax credits applied by the producer under this section to
6 exceed \$120,000,000.

7 (b) The producer may take the tax credit under this section for a period of not
8 more than 120 consecutive months. The 120-month period commences in the first
9 month that begins on or after July 1, 2006, and during which the producer has
10 commercial production of oil or gas from a lease or property in the state.

11 (c) On written application by a producer, including any information the
12 department may require, the department shall determine whether the producer
13 qualifies under this section for a calendar year. To qualify under this section, a
14 producer must demonstrate that its operation in the state or its ownership of an interest
15 in a lease or property in the state as a distinct producer entity would not result in the
16 division among multiple producer entities of any production tax liability under
17 AS 43.55.011(e) that would be reasonably expected to be attributed to a single
18 producer entity if the tax credit provided in (a) of this section did not exist.

19 (d) An unused tax credit or portion of a tax credit under this section is not
20 transferable under AS 43.55.024(d), and may not be carried forward to or used in a
21 later calendar year.

22 (e) The use of a tax credit under this section does not prevent a producer from
23 taking a tax credit under AS 43.55.024(a) or 43.55.025 for the same qualified capital
24 expenditure.

25 **Sec. 43.55.180. Required reports.** (a) The Department of Revenue shall

26 (1) study

27 (A) the effects of the tax rates under AS 43.55.011(f) and of
28 potential changes in those tax rates on state revenue and on oil and gas
29 exploration, development, and production on private land; and

30 (B) the fairness of the tax rates under AS 43.55.011(f) and of
31 potential changes in those tax rates for private landowners; and

1 (2) prepare a report on or before the first day of the 2013 regular
2 session of the legislature on the results of the study made under (1) of this subsection,
3 including a recommendation as to whether those tax rates should be changed; the
4 department shall notify the legislature that the report prepared under this paragraph is
5 available.

6 (b) The Department of Revenue shall

7 (1) study the effects of the credits authorized by AS 43.55.025 and
8 43.55.170 on state revenue, on the encouragement of exploration, development, and
9 production of oil and gas deposits located in the state, and on the encouragement of
10 new entrants into the oil and gas industry in the state; and

11 (2) prepare a report on or before the first day of the 2015 regular
12 session of the legislature on the results of the study made under (1) of this subsection,
13 and shall include with the report a recommendation as to whether the legislature
14 should extend the availability of the credit under AS 43.55.025 beyond June 30, 2016;
15 the department shall notify the legislature that the report prepared under this paragraph
16 is available.

17 * Sec. 27. AS 43.55.201 is amended to read:

18 Sec. 43.55.201. Surcharge levied. (a) Every producer of oil shall pay a
19 surcharge of \$.01 [\$.02] per barrel of oil produced from each lease or property in the
20 state, less any oil the ownership or right to which is exempt from taxation.

21 (b) The surcharge imposed by (a) of this section is in addition to the tax
22 imposed by AS 43.55.011 and is due on the last day of the month on oil produced
23 from each lease or property during the preceding month. The surcharge [SHALL
24 BE PAID IN THE SAME MANNER AS THE TAX IMPOSED BY AS 43.55.011 -
25 43.55.150; AND] is in addition to the surcharge imposed by AS 43.55.300 -
26 43.55.310.

27 (c) A producer of oil shall make reports of production in the same manner and
28 under the same penalties as required under AS 43.55.011 - 43.55.180 [AS 43.55.011 -
29 43.55.150].

30 * Sec. 28. AS 43.55.201 is amended by adding a new subsection to read:

31 (d) Oil not considered under AS 43.55.020(c) to be produced from a lease or

1 property is not considered to be produced from a lease or property for purposes of this
2 section.

3 * Sec. 29. AS 43.55.300 is amended to read:

4 Sec. 43.55.300. Surcharge levied. (a) Every producer of oil shall pay a
5 surcharge of \$.04 [\$.03] per barrel of oil produced from each lease or property in the
6 state, less any oil the ownership or right to which is exempt from taxation.

7 (b) The surcharge imposed by (a) of this section is in addition to the tax
8 imposed by AS 43.55.011 and is due on the last day of the month on oil produced
9 from each lease or property during the preceding month. The surcharge [SHALL
10 BE PAID IN THE SAME MANNER AS THE TAX IMPOSED BY AS 43.55.011 -
11 43.55.150; AND] is in addition to the surcharge imposed by AS 43.55.201 -
12 43.55.231.

13 (c) A producer of oil shall make reports of production in the same manner and
14 under the same penalties as required under AS 43.55.011 - 43.55.180 [AS 43.55.011 -
15 43.55.150].

16 * Sec. 30. AS 43.55.300 is amended by adding a new subsection to read:

17 (d) Oil not considered under AS 43.55.020(e) to be produced from a lease or
18 property is not considered to be produced from a lease or property for purposes of this
19 section.

20 * Sec. 31. AS 43.55.900(6) is repealed and reenacted to read:

21 (6) "gas" means

22 (A) all natural, associated, or casinghead gas;

23 (B) all hydrocarbons that

24 (i) are recovered by mechanical separation of well
25 fluids or by gas processing in a gas processing plant; and

26 (ii) exist in a gaseous phase at the completion of
27 mechanical separation and any gas processing in a gas processing plant;

28 and

29 (C) all other hydrocarbons produced from a well not defined as

30 oil;

31 * Sec. 32. AS 43.55.900(7) is repealed and reenacted to read:

1 (7) "gross value at the point of production" means

2 (A) for oil, the value of the oil at its point of production
3 without deduction of any costs upstream of that point of production;

4 (B) for gas, the value of the gas at its point of production
5 without deduction of any costs upstream of that point of production;

6 * Sec. 33. AS 43.55.900(10) is repealed and reenacted to read:

7 (10) "oil" means

8 (A) crude petroleum oil; and

9 (B) all liquid hydrocarbons that are recovered by mechanical
10 separation of well fluids or by gas processing in a gas processing plant;

11 * Sec. 34. AS 43.55.900 is amended by adding new paragraphs to read:

12 (17) "Cook Inlet sedimentary basin" has the meaning given in
13 regulations adopted to implement AS 38.05.180(f)(4);

14 (18) "explorer" means a person who, in exploring for new oil or gas
15 reserves, incurs expenditures;

16 (19) "gas processing"

17 (A) means processing a gaseous mixture of hydrocarbons

18 (i) by means of absorption, adsorption, externally
19 applied refrigeration, artificial compression followed by adiabatic
20 expansion using the Joule-Thomson effect, or another physical process
21 that is not mechanical separation; and

22 (ii) for the purpose of extracting and recovering liquid
23 hydrocarbons;

24 (B) does not include gas treatment;

25 (20) "gas processing plant" means a facility that

26 (A) extracts and recovers liquid hydrocarbons from a gaseous
27 mixture of hydrocarbons by gas processing; and

28 (B) is located upstream of any gas treatment and upstream of
29 the inlet of any gas pipeline system transporting gas to a market;

30 (21) "gas treatment"

31 (A) means conditioning gas and removing from gas

1 nonhydrocarbon substances for the purpose of rendering the gas acceptable for
2 tender and acceptance into a gas pipeline system;

3 (B) includes incidentally removing liquid hydrocarbons from
4 the gas;

5 (C) does not include

6 (i) dehydration required to facilitate the movement of
7 gas from the well to the point where gas processing takes place;

8 (ii) the scrubbing of liquids from gas to facilitate gas
9 processing;

10 (22) "landowner's royalty interest" means

11 (A) a lessor's royalty interest under an oil and gas lease; or

12 (B) a royalty interest that is

13 (i) held by a surface owner of land from which oil or
14 gas is produced; and

15 (ii) granted in exchange for the right to use the surface
16 of that land or as compensation for damage to the surface of that land;

17 (23) "oil and gas lease" includes an oil and gas lease, a gas only lease,
18 and an oil only lease;

19 (24) "point of production" means

20 (A) for oil, the automatic custody transfer meter or device
21 through which the oil enters into the facilities of a carrier pipeline or other
22 transportation carrier in a condition of pipeline quality; in the absence of an
23 automatic custody transfer meter or device, "point of production" means the
24 mechanism or device to measure the quantity of oil that has been approved by
25 the department for that purpose, through which the oil is tendered and accepted
26 in a condition of pipeline quality into the facilities of a carrier pipeline or other
27 transportation carrier or into a field topping plant;

28 (B) for gas, other than gas described in (C) of this paragraph,
29 that is

30 (i) not subjected to or recovered by mechanical
31 separation or run through a gas processing plant, the first point where

1 the gas is accurately metered;

2 (ii) subjected to or recovered by mechanical separation
3 but not run through a gas processing plant, the first point where the gas
4 is accurately metered after completion of mechanical separation;

5 (iii) run through a gas processing plant, the first point
6 where the gas is accurately metered downstream of the plant;

7 (C) for gas run through an integrated gas processing plant and
8 gas treatment facility that does not accurately meter the gas after the gas
9 processing and before the gas treatment, the first point where gas processing is
10 completed or where gas treatment begins, whichever is further upstream.

11 * Sec. 35. AS 43.55.011(a), 43.55.011(b), 43.55.011(c), 43.55.012, 43.55.013, 43.55.016,
12 43.55.025(k)(1), 43.55.025(k)(3), 43.55.900(1), 43.55.900(8), 43.55.900(11), 43.55.900(12),
13 and 43.55.900(16) are repealed.

14 * Sec. 36. The uncodified law of the State of Alaska is amended by adding a new section to
15 read:

16 APPLICABILITY. (a) Sections 5, 7 - 10, 12, 13, 15 - 18, 20, 24, 25, and 27 - 35 of
17 this Act and AS 43.55.160 and 43.55.170, enacted by sec. 26 of this Act, apply to oil and gas
18 produced on or after July 1, 2006.

19 (b) Section 11 of this Act applies to oil and gas produced before, on, or after the
20 effective date of sec. 11 of this Act.

21 * Sec. 37. The uncodified law of the State of Alaska is amended by adding a new section to
22 read:

23 TRANSITIONAL PROVISIONS. (a) Notwithstanding any contrary provision of
24 AS 43.55.024(a), enacted by sec. 12 of this Act, for oil and gas produced on or after July 1,
25 2006, and before January 1, 2007, the phrase "every month an annualized tax credit in an
26 amount equal to 1 2/3 percent" in AS 43.55.024(a)(1)(B), enacted by sec. 12 of this Act, shall
27 be replaced by the phrase "every month during the period July 1, 2006, through December 31,
28 2006, an annualized tax credit in an amount equal to 3 1/3 percent."

29 (b) Notwithstanding any contrary provision of AS 43.55.024(e), enacted by sec. 12 of
30 this Act, for oil and gas produced on or after July 1, 2006, and before January 1, 2007, the
31 phrase "a calendar year" in AS 43.55.024(e), enacted by sec. 12 of this Act, shall be replaced

1 by the phrase "the last six months of the calendar year."

2 (c) Notwithstanding any contrary provision of AS 43.55.024(i)(2), enacted by sec. 12
3 of this Act, for oil and gas produced on or after July 1, 2006, and before January 1, 2007,

4 (1) the number "1/24" in AS 43.55.024(i)(2)(B), enacted by sec. 12 of this
5 Act, shall be replaced by the number "1/12";

6 (2) the phrase "calendar year" in AS 43.55.024(i)(2)(B), enacted by sec. 12 of
7 this Act, shall be replaced by the phrase "last six months of the calendar year."

8 (d) Notwithstanding any contrary provision of AS 43.55.160(f), enacted by sec. 26 of
9 this Act, for oil and gas produced on or after July 1, 2006, and before January 1, 2007, the
10 phrase "for every month of a calendar year, 1/12 of the producer's adjusted lease expenditures
11 for the calendar year" in AS 43.55.160(f), enacted by sec. 26 of this Act, shall be replaced by
12 the phrase "for each of the last six months of 2006, one-sixth of the producer's adjusted lease
13 expenditures for that six-month period."

14 (e) Notwithstanding any contrary provision of AS 43.55.170(a), enacted by sec. 26 of
15 this Act, for oil and gas produced on or after July 1, 2006, and before January 1, 2007, the
16 amount of "\$12,000,000" in AS 43.55.170(a)(2), enacted by sec. 26 of this Act, shall be
17 replaced by "\$6,000,000."

18 (f) For oil and gas produced before July 1, 2006, the provisions of AS 43.55, and
19 regulations adopted under AS 43.55, that were in effect before July 1, 2006, and that were
20 applicable to the oil and gas continue to apply to that oil and gas.

21 (g) Notwithstanding any contrary provision of AS 43.55.020(a), as repealed and
22 reenacted by sec. 7 of this Act, for oil and gas produced on or after July 1, 2006, and before
23 the first day of the first month that begins at least 180 days after the effective date of sec. 7 of
24 this Act,

25 (1) the amount of the taxes that would have been levied on the producer under
26 AS 43.55, as the provisions of that chapter read on June 30, 2006, is due on the last day of
27 each calendar month on the oil and gas that was produced from each lease or property during
28 the preceding month;

29 (2) the portion, if any, of the taxes levied under AS 43.55.011(e) - (g), enacted
30 by sec. 5 of this Act, that is due under AS 43.55.020(a), as repealed and reenacted by sec. 7 of
31 this Act, and that remains unpaid, net of any credits applied as allowed by law, is due on the

1 last day of the first month that begins at least 180 days after the effective date of sec. 5 of this
2 Act.

3 (h) Notwithstanding any contrary provision of AS 43.55.030(a), as amended by sec.
4 18 of this Act, for oil and gas produced on or after July 1, 2006, and before the first day of the
5 first month that begins at least 180 days after the effective date of sec. 18 of this Act, the
6 person paying the tax shall file with the Department of Revenue, at the time an amount of tax
7 is due

8 (1) under (g)(1) of this section, the statement required under former
9 AS 43.55.030(a), as that subsection read on June 30, 2006; and

10 (2) under (g)(2) of this section, the statements required under
11 AS 43.55.030(a), as amended by sec. 18 of this Act.

12 (i) Notwithstanding any contrary provision of AS 43.55.201(a) or (b), as amended by
13 sec. 27 of this Act, or AS 43.55.300(a) or (b), as amended by sec. 29 of this Act, for oil
14 produced on or after July 1, 2006, and before the first day of the first month that begins at
15 least 180 days after the effective date of secs. 27 and 29 of this Act,

16 (1) the amount of the surcharges that would have been imposed on the
17 producer under AS 43.55, as the provisions of that chapter read on June 30, 2006, is due on
18 the last day of each calendar month on oil produced from each lease or property during the
19 preceding month;

20 (2) the portion, if any, of the surcharges imposed under AS 43.55.201(a), as
21 amended by sec. 27 of this Act, and AS 43.55.300(a), as amended by sec. 29 of this Act, and
22 that remains unpaid is due on the last day of the first month that begins at least 180 days after
23 the effective date of secs. 27 and 29 of this Act.

24 (j) Notwithstanding any contrary provision of AS 43.55.201(c), as amended by sec.
25 27 of this Act, or AS 43.55.300(c), as amended by sec. 29 of this Act, for oil produced on or
26 after July 1, 2006, and before the first day of the first month that begins at least 180 days after
27 the effective date of secs. 27 and 29 of this Act, at the time an amount of surcharge is due,

28 (1) under (i)(1) of this section, the producer shall file the report of production
29 required under former AS 43.55.201(c) and 43.55.300(c), as those provisions read on June 30,
30 2006; and

31 (2) under (i)(2) of this section, the producer shall file the report of production

1 required under former AS 43.55.201(c), as amended by sec. 27 of this Act, and
2 AS 43.55.300(c), as amended by sec. 29 of this Act.

3 (k) For purposes of taxes to be calculated and due under (g)(1) of this section and
4 statements to be filed under (h)(1) of this section, regulations that were adopted by the
5 Department of Revenue under AS 43.55, as the provisions of that chapter read on June 30,
6 2006, and that were in effect on that date apply to those taxes and statements.

7 * Sec. 38. The uncodified law of the State of Alaska is amended by adding a new section to
8 read:

9 TRANSITION: REGULATIONS AND RETROACTIVITY OF REGULATIONS. (a)
10 The Department of Revenue may proceed to adopt regulations to implement the changes
11 made by this Act. The regulations take effect under AS 44.62 (Administrative Procedure Act),
12 but not before the effective date of the law implemented by the regulation.

13 (b) Notwithstanding any contrary provision of AS 44.62.240, a regulation adopted by
14 the Department of Revenue to implement, interpret make specific, or otherwise carry out the
15 provisions of secs. 5, 7 - 10, 12, 13, 15 - 18, 20, 24 - 35, and 37 of this Act may apply
16 retroactively as of July 1, 2006, if the Department of Revenue expressly designates in the
17 regulation that the regulation applies retroactively to that date.

18 * Sec. 39. The uncodified law of the State of Alaska is amended by adding a new section to
19 read:

20 REVISOR'S INSTRUCTION. The revisor of statutes is instructed to change the
21 heading of

22 (1) AS 43.55 from "Oil and Gas Production Taxes and Oil Surcharge" to "Oil
23 and Gas Production Tax and Oil Surcharge";

24 (2) article 1 of AS 43.55 from "Oil and Gas Properties Production Taxes" to
25 "Oil and Gas Production Tax";

26 (3) AS 43.55.011 from "Oil production tax" to "Oil and gas production tax";

27 (4) AS 43.55.025 from "Tax credit for oil and gas exploration or gas only
28 exploration" to "Alternative tax credit for oil and gas exploration";

29 (5) AS 43.55.150 from "Determination of gross value" to "Determination of
30 gross value at the point of production."

31 * Sec. 40. The uncodified law of the State of Alaska is amended by adding a new section to

1 read:

2 CONTINGENT RETROACTIVITY OF PROVISIONS OF ACT. If, under sec. 40 of
3 this Act, this Act takes effect on or after July 1, 2006, sections 5, 7 - 10, 12, 13, 15 - 18, 20,
4 24 - 37 of this Act are retroactive to July 1, 2006.

5 * Sec. 41. This Act takes effect July 1, 2006.

SPONSOR
STATEMENT

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SPONSOR STATEMENT CSHB 488 (RES)

Wednesday, March 22, 2006 / Tim Benintendi, Staff, 465-3715

(version 24-GH2052/L)

COMMITTEE REPORT: 6 "Do Pass" / 1 "Do Not Pass" / 1 "Amend"

CSHB 488 (RES) would convert Alaska's oil severance tax structure from the Economic Limit Factor (ELF) method, to a petroleum profits tax (PPT) method. The governor's version would increase revenue by about \$705 million per year, on average, over the next five years. The House Resources Committee (HRC) version would increase revenue by about \$816 million per year, on average, over the same five years.

The severance tax is one of four levies paid by the oil industry in Alaska, the others being royalties, property taxes, and income taxes. Tax deductions and tax credits continue to be used to motivate industry for exploration, production, and development activities. The objectives of the bill remain as follows: Increase the state's share or "government take," under conditions of high oil market prices; provide industry with new or expanded incentives to explore and produce from marginal and frontier fields; and to ensure motivation for continued activity in the Cook Inlet fields.

The HRC proposed several changes to the governor's bill, most notably, installing a two-pronged progressivity feature on the PPT tax rate. In the governor's version, the PPT rate is a flat 20% regardless of the market price of oil. The HRC version also uses the 20% rate, but only at market prices up to \$50 per barrel (WTI benchmark). At market prices between \$50 and \$110 per barrel, the progressivity feature adds 3/10% of the wellhead value for every dollar the market price is over \$50. A single year of additional revenue in times of high market prices can offset many years of lower revenues when prices are close to their historical average.

If there is a dramatic price shock or the value of oil continues to rise at market prices over \$110 per barrel, the tax generates an additional 37.5% of wellhead value for the state. We would get a greater share at very high market prices. As prices climb, the combined effect of the 20% PPT base rate and the 37.5% progressivity factor (which is deductible in calculating the amount payable under the PPT rate) approaches 50% of the oil's value in Alaska. The committee felt this two-pronged progressivity feature would keep investment opportunity in Alaska strong, while allowing the state to share in windfalls at high spikes of market prices.

Another policy change from the governor's bill to the HRC version was the elimination of transition costs as deductions from the production tax. The governor provided a deduction for investment costs incurred in the past five-years, feeling that investments made in that period and directly tied to the production of oil which would be taxed at the new rate, should be allowed. After hearing considerable testimony on this component, the HRC deleted it completely.

Exploration tax credits of 40% under SB 185 (Ch. 59, SLA 03) will be extended ten years under the HRC version, and the governor's credit rate of 20% remains intact. This is intended to motivate explorers and independent firms. As is currently done, a company will be able to choose from the two options as they assess which is most beneficial to them.

The House Resources Committee allowed no credit for abandonment costs, but such expenses remain tax-deductible. And, in terms of a private royalty severance tax rate, the HRC version set it at 5%.

As introduced, the governor's version of HB 488 proposes to make the current oil spill contingency surcharge (which is currently 5-cents per barrel) creditable against the PPT. The HRC left the current statute in place, but modified the program. The current 2-cents per barrel which goes into the Response Mitigation Account (RMA), is reduced to 1-cent. This surcharge will continue in suspension as long as the RMA balance holds at \$50 million. The remaining 3-cent per barrel surcharge, which is deposited into the Prevention Mitigation Account (PMA), increases to 4-cents per barrel under the HRC substitute bill.

The governor provided a \$73 million annual allowance for all producers, against which a 20% credit would be applied, resulting in a \$14.6 million tax credit per company, annually. The merits of this allowance and credit incentive eluded committee members, so this provision was changed to a direct tax credit, dollar for dollar, on the first \$12 million worth of capital investment for exploration, production, or development work. This annual credit is non-transferable, non-salable, not eligible for carry-forward, and can only be applied to a current year's severance tax. Should a company spend less than \$12 million, the credit would be applied to whatever amount they did spend.

As protection for explorers and new entrants to Alaska, the HRC devised a tax credit repurchasing program for those credits a company earns on expenditures of up to \$10 million per year for investments in exploration and/or lease purchases in Alaska.

The effective date for HB 488 as introduced by the governor, was July 1, 2006. The HRC version changed that to April 1st, also the beginning of a fiscal quarter, but a change which would bring the state another \$200 million this year.

SECTIONAL
ANALYSIS

LEGAL SERVICES

DIVISION OF LEGAL AND RESEARCH SERVICES
LEGISLATIVE AFFAIRS AGENCY
STATE OF ALASKA

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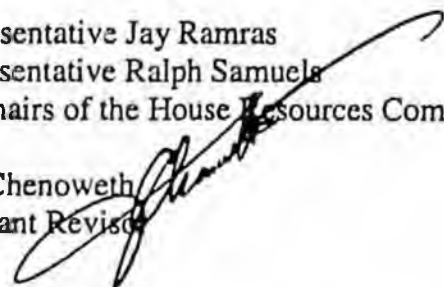
State Capitol
Juneau, Alaska 99801-1182
Deliveries to: 129 6th St., Rm. 329

MEMORANDUM

March 24, 2006

SUBJECT: CSHB 488(RES) -- sectional analysis
(Work Order No. 24-GH2052\L)

TO: Representative Jay Ramras
Representative Ralph Samuels
Co-Chairs of the House Resources Committee

FROM: Jack Chenoweth
Assistant Revisioner 

The House Resources Committee Substitute proposes to repeal the state's current oil and gas properties production tax and replace it with a production tax on oil and gas. The replacement tax is to be based on a percentage of the production tax value of oil and gas, the determination of which is prescribed by the bill. The measure makes a number of related and conforming additions and changes.

The measure is an administration-sponsored bill, so in the preparation of this memo, for provisions not substantively altered by the Resources Committee, I have drawn on the explanatory language of the administration's February 21 sectional analysis of the bill as introduced.

PROVISIONS IMPOSING A PRODUCTION TAX ON THE NET VALUE OF OIL AND GAS:

Provisions imposing the tax and setting the basic tax rate(s) --

Bill section 5: The bill section enacts (as a repeal and reenactment of AS 43.55.011(a) levying a tax on a percentage of the gross value at the point of production) the tax levy as a production tax on both oil and gas, with exceptions and limitations noted in the provision's text, and sets the rate of levy at 20 percent of the production tax value of the taxable oil and gas.

Bill section 6: As part of this bill section, a new subsection, AS 43.55.011(e), is added to authorize a levy and set a rate of levy on oil and gas produced that constitutes a lessor's royalty interest under an oil and gas lease. The rate specifies a rate of five percent of the gross value at the point of production. It also sets out an alternative rate of 20 percent of the gross value that applies under circumstances in which there is evidence the producer's receipt of consideration from the lessor offsets the producer's royalty obligation.

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Provisions authorizing a progressively higher tax rate for oil when the price exceeds \$50 per barrel --

As part of **bill section 6**, proposed AS 43.55.011(f) sets out an oil price index by which the tax levy on oil is adjusted by an addition .3 percent of gross value per dollar in excess of \$50, based on Gulf Coast prices for West Texas Intermediate crude. Subsection (g) caps the index increase when the average price reaches \$110 per barrel. Subsection (h) sets out the manner in which the index may be calculated and authorizes use of a substitute formula under circumstances specified in the subsection.

Provisions authorizing a progressively higher tax rate for gas when the price of gas exceeds \$8 per million BTUs --

Again, as part of **bill section 6**, proposed AS 43.55.011(i) sets out a natural gas price index by which the tax levy on gas is adjusted by 2 percent of gross value when the average Henry Hub price exceeds \$8 per million BTUs. Subsection (j) caps the index increase at 18.75 and subsection (k) spells out the manner in which the index may be calculated and authorizes use of a substitute formula under circumstances specified in the subsection.

Provisions relating to the determination of the production tax value of oil and gas --

The oil and gas production tax levy is imposed as a percentage of the production tax value of the taxable oil and gas. Calculation of the production tax value is set out in AS 43.55.160, added by **bill section 28**:

-- Under AS 43.55.160(a), the calculation begins with the determination of the gross value at the point of production of all of a producer's taxable oil and gas statewide. The producer may deduct taxes paid that are attributable to application of the indexed production tax rate increases as well as the deductible costs of oil and gas exploration, development, and production (adjusted deductible lease expenses). Subsection (a) contains language that precludes net value calculation from falling below zero.

-- Subsection (b) sets out rules for the producer's claim and use of unused deductions.

-- Subsection (c) spells out the exploration, development, and production costs that qualify as deductible lease expenses ("total costs upstream of the point of production . . . incurred on or after January 1, 2006, . . . and that are direct, ordinary, and necessary costs for exploring for, developing, or producing oil or gas deposit"), and provides guidance to the department as to evidence of those costs, especially in situations involving activities occurring under operating agreements.

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-- Subsection (d) spells out allowable direct costs and costs that may not be deductible because they are not direct costs.

-- The mechanics of making adjustments to a producer's lease expenditures are addressed in subsection (e). Adjustments are required to account for reimbursements, assets sales, and other producer receipts.

-- Subsection (f) authorizes substitution of determination of adjusted lease expenditures on a monthly basis, at the election of the producer.

--The provisions of subsections (g) - (i) spell out additional authority of the department with respect to tax administration, while subsection (j) supplies definitions of terms used.

Tax credit provisions --

The measure contains two separate sections authorizing tax credits.

Bill section 14 adds a new section, AS 43.55.024, that sets out tax credits for certain expenditures and losses. In the section,

-- Subsection (a) authorizes a tax credit of 20 percent of "qualified capital expenditures"--the term is defined in subsection (j)--against the production tax on the net value of taxable oil, bars claim of the tax if the same expenditures are used to claim a credit under AS 43.55.025 (existing tax credit for oil and gas exploration or gas only exploration), and authorizes claim and application of the credit on a monthly basis if, under AS 43.55.160(f), the producer has elected to substitute determination of adjusted lease expenditures on a monthly basis.

-- Subsection (b) authorizes election of a 20 percent tax credit on the basis of carried forward annual losses, defined in the subsection as "the producer's . . . adjusted lease expenditures under AS 43.55.160 for a previous calendar year that was not deductible in any month under AS 43.55.160(a) and (b)."

-- Subsection (c) precludes a tax credit from reducing the producer's tax liability below zero but authorizes application of the unused portion of the credit in a later month.

-- Subsections (d) and (e) establish a system by which tax credits for expenditures and losses as authorized by the section may be transferred through transferable tax credit certificates. Subsection (f) authorizes the department to repurchase credit certificates and, subject to appropriation, make cash refunds, but repurchase and refunds must comply with the requirements spelled out in paragraphs (1) - (5).

-- Subsections (g) and (h) spell out the authority of the department with respect to the administration of transferable tax credit certificates.

-- Subsection (i) bars a producer from making a claim of a tax credit for expenditures to acquire and use certain assets or for costs associated with abandonment.

AS 43.55.170, enacted as part of **bill section 28**, sets out a second or additional tax credit. The section allows the producer to claim a credit for qualified capital expenditures (as that term is defined in AS 43.55.024). The credit may not be applied to reduce the producer's tax liability to less than zero. Unused portions of the credit may be carried forward from month-to-month within a calendar year, may not exceed a total of \$12,000,000 for a calendar year, and may not be carried forward into a following calendar year. These credits are not transferable and not refundable. The authorization for these additional credits expires March 31, 2016.

Provisions relating to tax payment and the administration of the tax --

Bill section 8: The bill section enacts (as a repeal and reenactment of AS 43.55.020(a)) a requirement of monthly payment of the net value production tax on oil, with payment due at the end of the calendar month for production during the preceding month. The provision spells out conditions when a tax due is delinquent, the handling of overpayments, and limitations on interest that may be payable on tax overpayments.

Bill section 10, amending AS 43.55.020(d), deals with a producer's right to charge a private royalty owner for the share of production taxes attributable to royalty oil and gas. The amending language adds a method of determining the royalty share of taxes in the absence of an agreement between the producer and royalty owner to use a different method.

Bill section 11 expands the current production tax exemption for gas that is used in lease operations by including oil that is used in those lease operations. The section also clarifies the manner of tax treatment of flared gas, based on authorization to do so from the Alaska Oil and Gas Conservation Commission.

Bill sections 1 and 12: The latter provision amends AS 43.55.020(f) allowing the Department of Revenue to require production tax to be paid on the basis of prevailing value. It clarifies that the provision applies not only when the sale price differs from the prevailing value but also when the oil or gas on which tax is due is not sold at all. The former sets out a statement of intent for the amendment made to the permanent law provision.

Bill section 13: As is done earlier in the bill with respect to oil, proposed AS 43.55.020(g) enacts a requirement of monthly payment of the net value production tax on amounts due under the lessor's royalty share provisions, on the indexed production tax rate increases as applied to oil and the indexed production tax rate increases as applied to gas. Payment is due at the end of the calendar month for production during the preceding month and, if not paid, the tax due is delinquent. Proposed AS 43.55.020(h)

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authorizes imposition and collection of a five percent civil penalty on the difference between the amount not paid and a 90 percent threshold if payment, when due, falls below that threshold.

Bill section 20: This section, proposing amendments to AS 43.55.030(a), clarifies what the Department of Revenue may obtain as information relevant to determining taxes due under AS 43.55.

Bill section 21 amends AS 43.55.030(d) to delete a per day penalty for failure to file a tax return under AS 43.55. Other provisions in this measure and in AS 43 are applicable to late filing of tax return documents.

Bill section 22, adding AS 43.55.030(e), sets out a requirement of an annual "true-up" of the prior year monthly returns and directs submission of adjustments or corrections of the previously-filed statements.

Bill section 23, amending AS 43.55.040, clarifies the department's power to obtain information relevant to determining taxes imposed under AS 43.55 by adding the authority to require filing of regular statements or reports. In addition, the bill section modifies the statutory confidentiality restrictions related to use of information in returns and reports when necessary to determine a taxpayer's liability, particularly as those provisions may be applicable to persons -- state officers and employees and privately-retained contractors -- who may have access to the information.

Bill section 27: AS 43.55.150 deals with determining the gross value at the point of production of oil and gas. The addition of new subsection (d) authorizes the Department of Revenue to allow producers to calculate that gross value with a formula that uses a producer's royalty agreement with the state, a royalty value or valuation method accepted by the Department of Natural Resources or the United States Department of the Interior, or another formula using factors such as published price indices.

OTHER SUBSTANTIVE PROVISIONS AFFECTING OIL PRODUCTION AND GAS PRODUCTION TAXES:

Bill section 16: The amendment to AS 43.55.025(b) extends the current production tax credit for exploration expenditures, authorized by AS 43.55.025, from the current deadline of July 2007 (July 2010 for the North Slope and Cook Inlet activities) to July 1, 2016, on a statewide basis.

Bill section 29: The amendments to AS 43.55.201 modify the component of the so-called nickel-per-barrel surcharge that directs a portion of the money to the response account in the oil and hazardous substance release prevention and response fund, reducing by one cent the amount directed to that account, and making necessary conforming changes to cross-references.

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Bill section 30: The addition of AS 43.55.201(d) relieves from payment of this component of the tax surcharge oil that is exempt from the production tax because it is used in lease operations.

Bill section 31: The amendments to AS 43.55.300 modify the component of the so-called nickel-per-barrel surcharge that directs a portion of the money to the release prevention account in the oil and hazardous substance release prevention and response fund, increasing by one cent the amount directed to that account, and making necessary conforming changes to cross-references.

Bill section 32: The addition of AS 43.55.300(d) relieves from payment of this component of the tax surcharge oil that is exempt from the production tax because it is used in lease operations.

Bill sections 33 - 35 amend definitions of terms used in the chapter: "gas", "gross value at the point of production," and "oil."¹

Bill section 36 adds definitions for "explorer" (for use in the chapter), "gas processing", and "gas treatment".²

PROVISIONS PROPOSING REPEAL OF THE CURRENT OIL AND GAS PROPERTIES PRODUCTION TAX:

In addition to repeals and reenactments made in bill sections 1 and 8, bill section 37 collects and sets out repeals of provisions relating to the current oil and gas properties production tax that are obsolete or unnecessary due to other changes proposed in the measure:

-- repeal of AS 43.55.011(b) and (c) delete the provisions spelling out the percentage-of-value and cents-per-barrel tax methodologies applicable to taxation of oil;

-- repeal of AS 43.55.012(b) repeals the special cents-per-barrel provisions for heavy oil;

¹ By cross-reference, the change in the definition of "gas" has the effect of changing the definition of "gas" as used in AS 43.82, the Alaska Stranded Gas Development Act. See AS 43.82.900.

² As to the definitions, the administration's initial sectional analysis noted that

Under these definitions, gas processing is considered an operation upstream of the point of production for gas, and generally the line between what is oil and what is gas corresponds to what substances are in liquid form and what substances are in gaseous form, respectively, at the point of production.

-- repeal of AS 43.55.013 eliminates the economic limit factor, or ELF;

-- repeal of AS 43.55.016 deletes the current gas production tax;

-- repeal of AS 43.55.025(k)(3) eliminates the definition of "explorer" as applicable to the current tax credit for oil and gas exploration; the term is defined for the chapter by an addition made in bill section 36;

-- repeal of paragraphs (1), (8), (11), (12) and (16) of AS 43.55.900 eliminate definitions appearing in other repealed sections --"API gravity", "intangible drilling expense", "oil production operation", "old crude oil", and "well days".

CONFORMING ADDITIONS AND AMENDMENTS:

Bill section 2 amends criminal provisions for unauthorized disclosure of confidential records. The section imposes criminal penalties on current or former officers and employees for unauthorized disclosure; the amendment extends the penalties to others, private persons such as legal counsel and consultants, who make an unauthorized disclosure of otherwise confidential information to which they have had access.

Bill sections 3 and 4 authorize a producer who is a taxpayer under the Alaska Net Income Tax Act, AS 43.20, to deduct the production tax payments and disallows the adding back of the production taxes levied and paid in the determination of the producer's corporate income tax.

Bill section 7 conforms certain statutory language to that used in the Internal Revenue Code and incorporates by reference a definition for a term used elsewhere in the chapter.

Bill section 9 makes a corrective amendment to AS 43.55.020(b).

Bill sections 15, 17, 18, and 19: The provisions are in the nature of conforming amendments made to various subsections of AS 43.55.025, authorizing the current tax credit for oil and gas exploration or gas only exploration. The amendments insert or substitute reference to the specific subsection levying the production tax on oil and gas. The changes are necessary because, as proposed in the original bill and the committee substitute, the chapter (AS 43.55) would have multiple tax credits rather than the one existing tax credit for oil and gas, or gas only, exploration.

Bill section 24 proposes amendments to AS 43.55.080, directing that production taxes be deposited into the general fund, to incorporate exceptions imposed under the constitutional budget reserve fund amendment, and making a conforming amendment due to addition of new sections to article 1 of AS 43.55.

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Bill section 25, amending AS 43.55.135, sets out a conforming amendment due to addition of new sections to article 1 of AS 43.55.

Bill section 26, amending AS 43.55.150(a), makes conforming amendments relating to the determination of gross value to be calculated and in the reference due to addition of new sections to article 1.

APPLICABILITY, TRANSITIONAL, AND RELATED PROVISIONS:

Bill section 38 specifies that provisions relating to the new tax on the production tax value of oil and gas apply to oil and gas produced on or after April 1, 2006, and that the provision under which the Department of Revenue collects the tax on the basis of prevailing value and that clarifies how that value is to be measured, confirming long-standing agency policy, applies to all production without reference to date.

Bill section 39 sets out a series of transitional provisions that clarify how certain calendar year rules added by the new tax will apply during the first nine-month period that the tax is in effect, that authorize the claim of tax credit for expenditures and losses based on expenditures made on or after January 1, 2006, that set out a transitional schedule for tax payments, and that former regulations in effect under the previous severance tax statute continue to govern oil and gas produced before the April 1, 2006, effective date of the new production tax.

Bill section 40 authorizes adoption of new regulations and provides that the new regulations adopted may apply retroactively as of the April 1, 2006, effective date of the new production tax.

Bill section 41 prescribes editorial instructions for the revisor of statutes.

Bill section 42 adds a provision authorizing retroactive application of expenditures incurred on or after January 1, 2006, for expenditures that support the tax credit claims under the new production tax.

In the event the bill becomes law after April 1, 2006, **bill section 43** makes the provisions of the measure that are identified as taking effect on that date retrospectively effective to that date.

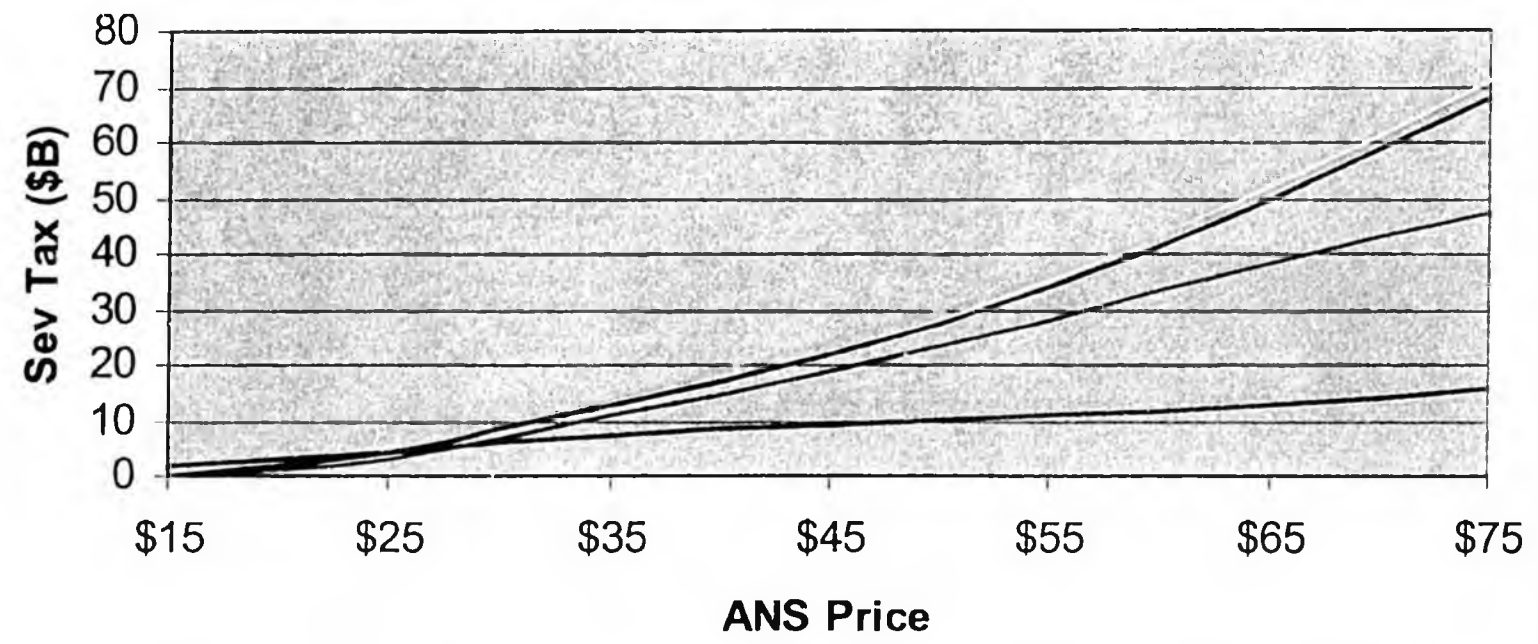
Bill sections 44 and 45 are the measure's effective dates. The production tax provisions have an April 1 effective date; the remainder of the bill is given immediate effect.

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ADMINISTRATION

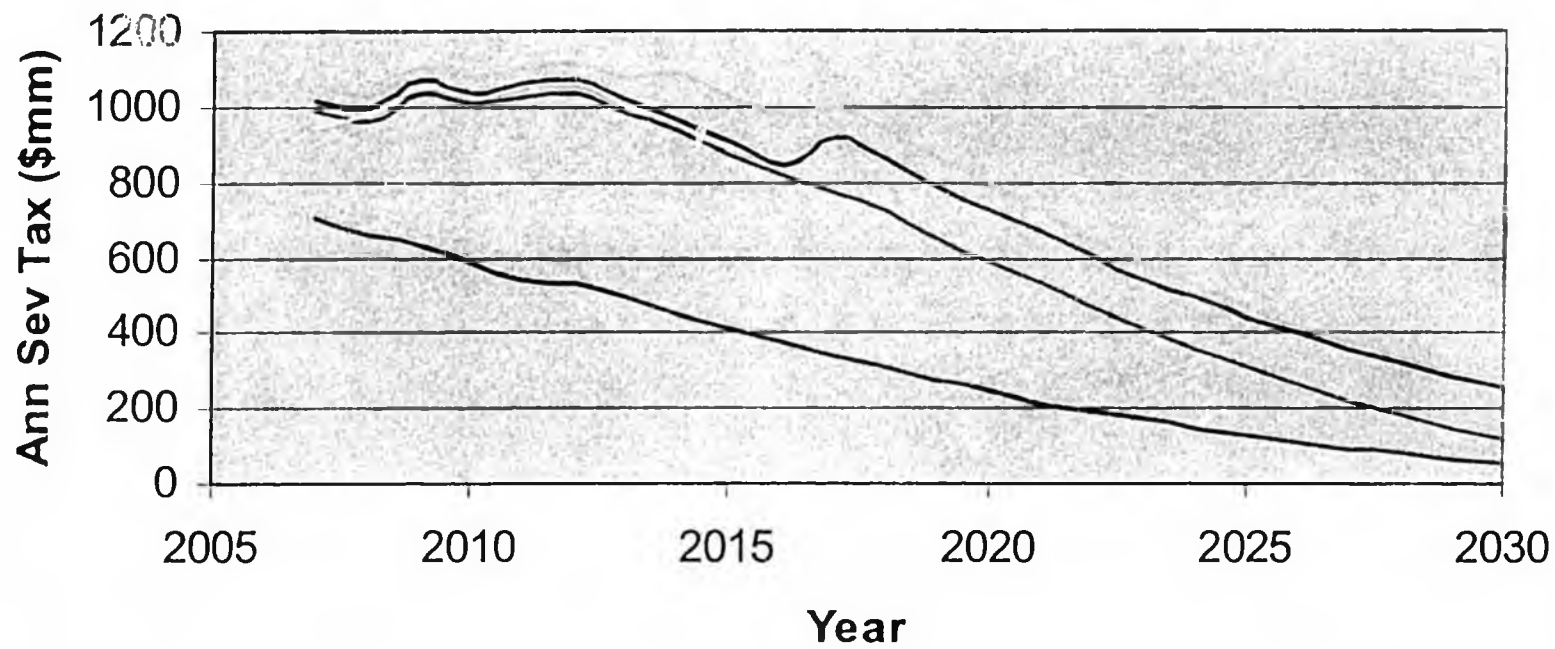
DRAFT
HB 488 House Finance CS
Comparative Revenues
Alaska Department of Revenue
May 5, 2006

Cumulative Severance Tax 2007-2030 (\$Billions)



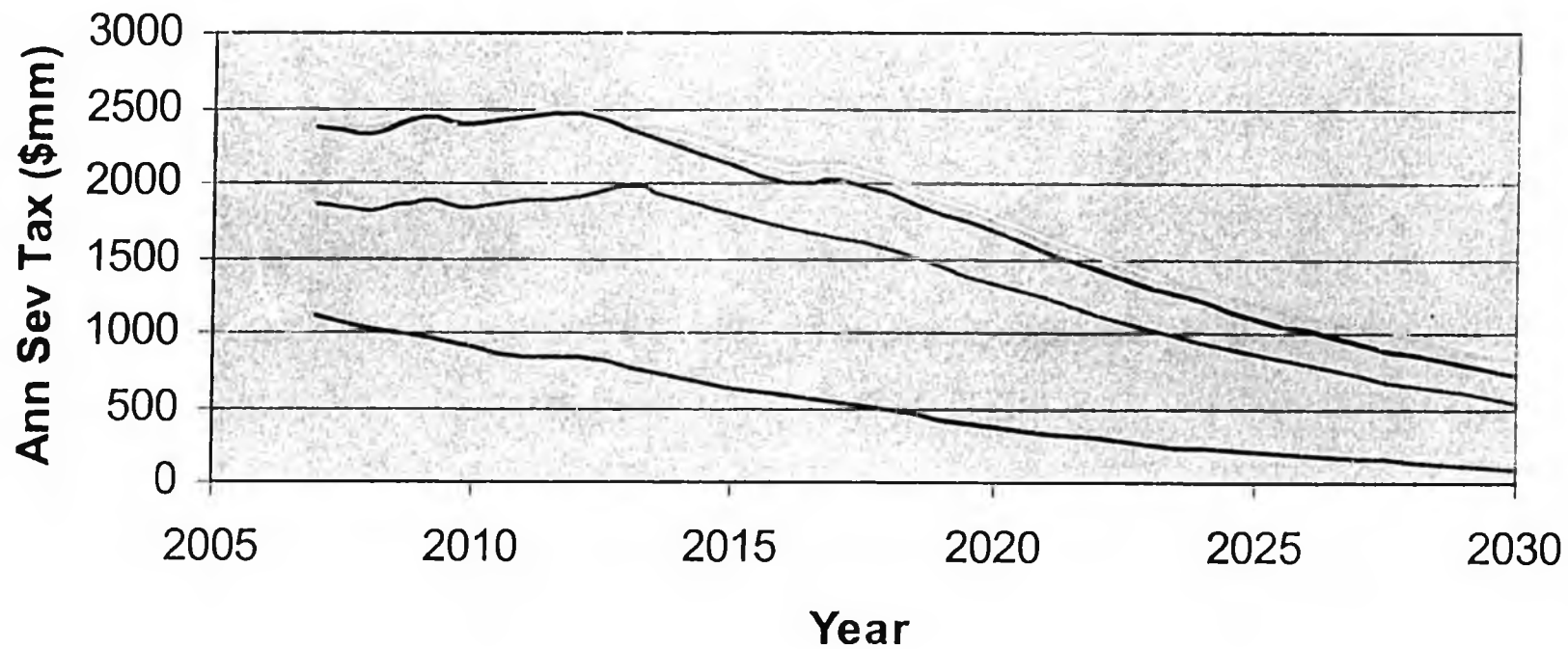
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Annual Severance Tax @ \$40 2007-2030 (\$Millions)



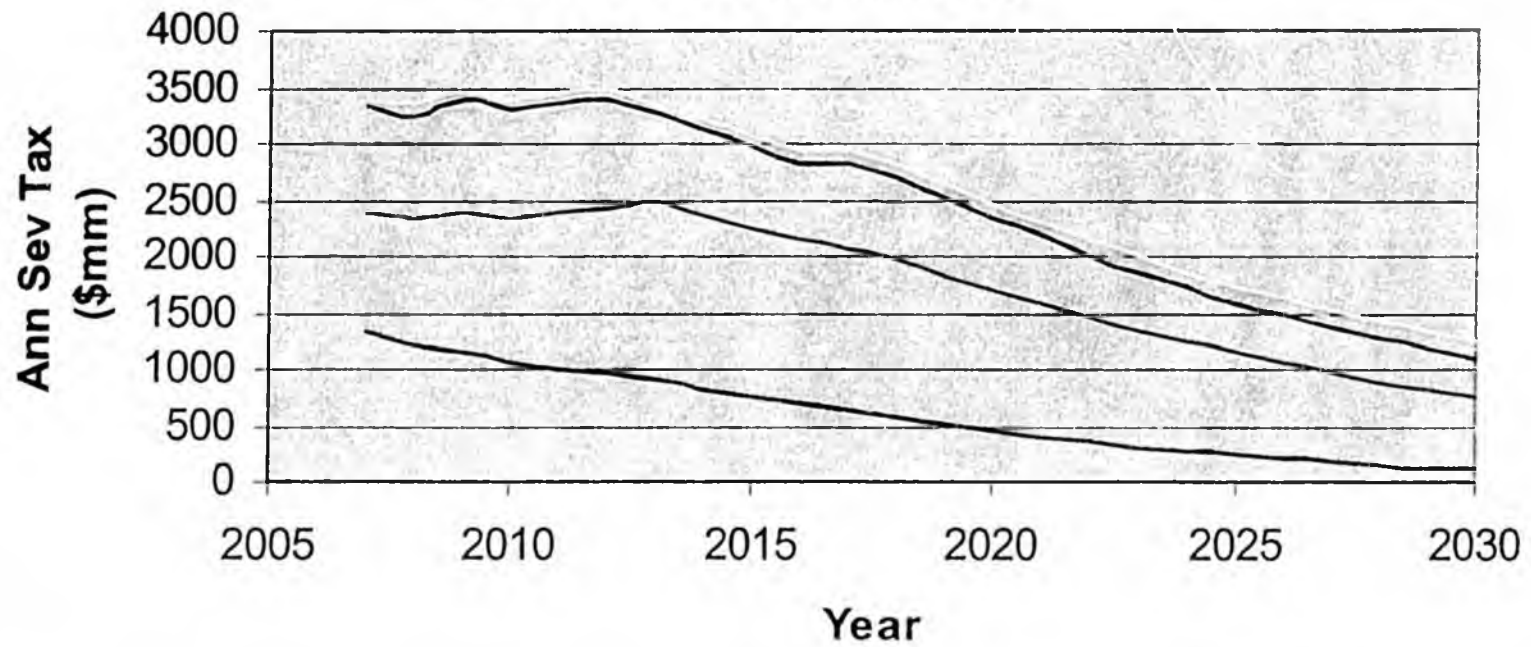
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Annual Severance Tax @ \$60 2007-2030 (\$Millions)



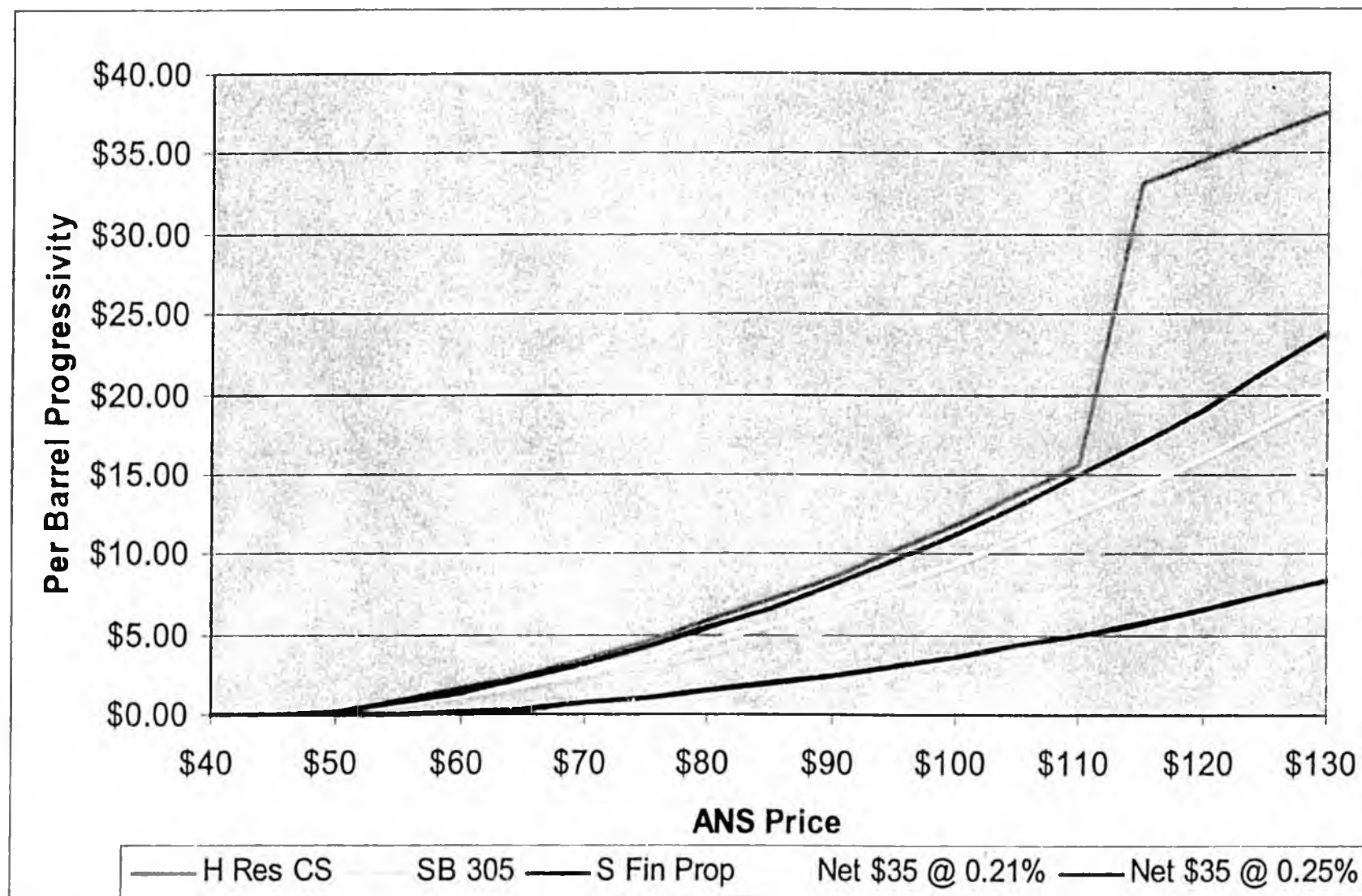
— sq — gov — house res cs — sb 305 — house fin cs

Annual Severance Tax @ \$70 2007-2030 (\$Millions)



— sq — gov house res cs sb 305 — house fin cs

Per Barrel Progressivity Surcharge on Net \$35 at 0.21% and 0.25%



Alaska Oil and Gas Association



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April 13, 2006

The Honorable Mike Chenault
Co-Chair, Committee on Finance
The Alaska House of Representatives
Alaska State Capitol, Room 505
Juneau, AK 99801-1182

The Honorable Lyda Green
Co-Chair, Committee on Finance
The Alaska Senate
Alaska State Capitol, Room 516
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The Honorable Kevin Meyer
Co-Chair, Committee on Finance
The Alaska House of Representatives
Alaska State Capitol, Room 515
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The Honorable Gary Wilken
Co-Chair, Committee on Finance
The Alaska Senate
Alaska State Capitol, Room 518
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The Honorable Bill Stoltze
Vice Chair, Committee on Finance
The Alaska House of Representatives
Alaska State Capitol, Room 501
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The Honorable Con Bunde
Vice Chair, Committee on Finance
The Alaska Senate
Alaska State Capitol, Room 506
Juneau, AK 99801-1182

Re: Senate Bill No. 305 / House Bill No. 488 ("PPT")
Proposed Amendments

Dear Finance Committee Co-Chairs and Vice Chairs:

The Alaska Oil and Gas Association (AOGA) wishes to thank you and your respective committees for the hearings you have been holding on this legislation to replace the existing ELF-based production tax with a new "Petroleum Production Tax" (PPT) based on the value of oil and gas after costs of producing it have been deducted. AOGA is a non-profit trade association whose 17 member companies represent the majority of oil and gas exploration, production, transportation, refining and marketing activities in Alaska. Our present comments and recommended technical amendments to the legislation have been approved by the Tax Committee without dissent.

With something as complex as the PPT, producers will need to have as much certainty and clarity as possible about how to calculate their PPT correctly. The Legislature too — as the Branch of government that sets state tax policy — deserves to know that any PPT law which it enacts will be administered and applied as the Legislature intends. We believe the PPT could be improved to better achieve these objectives. To this end we offer a number of technical amendments for your consideration. The actual text of our proposed amendments is attached. What follows below are explanations of what each amendment would do and why it should be adopted.

Amendment No. 1

This amendment relates to the so called 90% or 95% "safe harbor" provisions in the House and Senate Resources Committee CS's respectively. As structured in the original bill and both Resources CS's, these provisions are unworkable and inappropriate.

Two key elements of PPT are based on federal income-tax concepts. One is the use of the federal definition of "ordinary and necessary" in determining the scope of field expenditures that will be deductible under the PPT. The other is the use of the federal definition of "capital expenditure" to determine whether an expenditure gives rise to a tax credit against PPT.

Using these federal concepts offers three major advantages. One, everybody among the producers and in DOR understands what these concepts mean. There is a large and detailed body of federal statutes, regulations, rulings, and administrative and judicial precedents that establish these meanings. Two, using the federal concepts greatly simplifies DOR's task in writing regulations to implement the PPT, which will save time in getting the regulations in place to start implementing and complying with this new tax. Three, using the federal definitions lets the IRS do the heavy lifting in terms of auditing these expenditures and determining that they have been classified properly. When the IRS is done auditing, this allows DOR auditors to say "me too" to those audit adjustments just as they do now for federal items incorporated into the state income tax.

The present 90% and 95% safe-harbor provisions are structured on the assumption that the bookkeeping and accounting for deductible expenditures and credit-generating investments is on a monthly basis, thus allowing this level of precision in estimating the PPT payment each month. However, the records, accounting and IRS audits of the federal concepts being used for PPT are all maintained and performed on a full-year basis rather than a monthly one. There is nothing in this federally based approach that divides a year's cost items into individual monthly packets cleanly.

This does not mean that PPT cannot be paid on a monthly basis. The IRS, and Alaska and many other states in the context of their state income taxes, require businesses to make estimated payments during the tax year, with a final true-up the following March to the actual numbers for that year. In the income tax area these estimated payments are most commonly done on a quarterly basis, but there is nothing to prevent monthly estimated payments for PPT. We believe monthly estimated payments are possible and can be done on a reasonable and fair basis.

The IRS, Alaska in its income tax, and other states with their income taxes recognize that taxpayers making the early estimated payments for a tax year cannot accurately predict how the year will turn out for them. But as the year goes by, there are fewer months left to estimate and more months of actual data to use in calculating the estimated payments. By the last estimated payment for the year, that estimate should be pretty accurate even though the books for the year may not yet have closed and the figures become final. The IRS, and Alaska and the other states, figure that by the time the last estimated payment is made, taxpayers should be able to get it right so that at least 90% of the actual tax for the year is paid up with that last estimated payment. This is the source of the safe harbor concept and the original 90%, and we believe this federal and state rule in the income tax context is appropriate for PPT as well.

We all know that in the business world, it is better to come in under budget than over. But in the PPT world, being under budget means that, if you relied on your budget in the early months of the year to estimate your total deductions and credits for the remaining months, you will have overstated those deductions and credits if the actual expenditures for the year end up being under budget. But by the time you first start becoming aware of this toward the middle or end of the year, you are likely to have already filed and paid your monthly PPT for a fair number of prior months.

Under the original version of the PPT and both Resources CS's, a producer in this situation would be subject to an underpayment penalty, perhaps with interest, if it fails to estimate the correct amount of monthly PPT for the early

months of each year. This penalizes the producer, essentially, for not having the ability to see into the future how the year will turn out. Such a penalty is neither fair nor appropriate.

Our proposed amendment adapts the income-tax system of estimated payments so they are made monthly instead of quarterly. It also prevents the possibility that taxpayers might exploit the time-value of money by reporting very low estimated payments for the early months and then getting caught up to the 90% level with their last one or two estimated payments for the year.

Amendment No. 2

The provisions on the capex credit in the original legislation and both Resources CS's do not allow a credit for acquiring a capital asset that has already been used in this state by someone else, unless no more than an "immaterial portion" of that asset is used. See proposed AS 43.55.024(e). We do not disagree with this basic concept. However, we do believe that the term "immaterial" is too vague and subjective, and that using it as the test will lead to numerous disputes and squabbles over relatively minor items.

Our proposed amendment would replace this vague standard of immateriality by saying the credit for acquiring a used asset is not allowed unless no more than 15% of that asset is used (e.g., a replaced fender or windshield on an otherwise unused motor vehicle).

Amendment No. 3

Currently both Resources CS's and the original version all provide in AS 43.55.160(c) that deductions are allowed for "total costs upstream of the point of production of oil and gas that are incurred[.]"

We believe this description of the costs is potentially ambiguous. For instance, there can be no plausible dispute that the costs of the operations centers and dormitories for the workers in the fields on the North Slope should be deductible costs for those fields, nor is there any question that the cost of helicoptering workers out to the platforms in Cook Inlet should be deductible. But if you follow the course of the production fluids as they flow from the Christmas tree through the surface facilities and gathering lines to the point of production, neither of these costs shows up anywhere along that route. Are these costs "upstream of the point of production"? Clearly, this is the wrong test.

We also believe this description is potentially too narrow. It may be that simulations of well work or other processes in the field may be conducted on computers physically removed from the site of the field itself. If these costs are so directly related to the field work that the operator can bill them out to the working-interest owners as field operating costs, why should it matter whether they are "upstream of the point of production" or not? For that matter, the same ambiguity about whether they physically are "upstream" or not, also applies to them as it does to the operations centers and dormitories.

We believe it would be unambiguous, fairer and more appropriate to allow deductions for the "total costs in support of activities upstream of the point of production[.]" This is especially true whenever DOR utilizes the authority elsewhere in AS 43.55.160(c) to authorize the use of a producer's billings from the operator as that producer's deductible expenditures for that field.

Amendment No. 4

Proposed AS 43.55.160(c) in the original legislation and both Resources CS's provides that DOR, in determining the scope of the categories and kinds of expenditures that will be deductible for PPT, "shall give substantial weight" to industry practices and standards as reflected in existing unit operating agreements. We believe DOR should be required to "apply" the practices and standards reflected in those operating agreements, instead of merely giving

them "substantial weight."

In recommending this for your consideration, we would emphasize that there are two similar-appearing, but very different issues surrounding AS 43.55.160. One is the identification of the kinds and categories of expenditures that are deductible at all. The other is verification that the expenditures reported as falling into these deductible categories are properly included in those categories. The former is fundamentally a question of tax policy. The latter is primarily an audit issue.

Our concern is that the tax policy in the first question not be allowed to become just an audit issue as well.

We believe the cash expenditures that an operator under a unit operating agreement or similar agreement is allowed to bill to the other working-interest owners, partners or other participants reflect appropriate and reliable boundaries for what kinds of costs should be deductible. No one gives authority to an operator to spend their money without making certain that those expenditures are going to be spent on the right things. The operating agreements set tight limits on what an operator may or may not spend money for.

Those other participants have drawn a tight circle, and a clear one, about what is or is not an appropriate expenditure by the operator on their behalf. We believe DOR should "adopt" the wisdom and experience that are reflected in the operating agreements that arise from a true adversity of interest between the operator and those whom the operator bills and are patterned closely after other agreements where there was such an adversity of interest.

Amendment No. 5

Proposed AS 43.55.160(e) requires that a producer's deductible lease expenditures for a field be offset for "any payment or credit" that it receives from someone else as payment for the use of facilities in the field, was a reimbursement of chargeable field costs against a royalty interest of the state or federal government, or as proceeds from the sale of a capital asset.

We do not disagree with the purpose of these provisions. Rather, we want to avoid uncertainty in their administration and application to producers. This amendment clarifies that to the extent a reimbursement is for a producer's deductible expenditures under AS 43.55.160, the reimbursement will offset the deduction. This will ensure that every barrel is taxed once and no expenditure is deducted twice under 43.55.160.

Amendment No. 6

Alaska and many other states do not allow a deduction under their income taxes for taxes paid to another jurisdiction that are based on or measured by net income. Washington, for example, has an excise tax that allows a credit for other excise taxes paid to another jurisdiction. Currently there is no question that the ELF-based severance tax is an excise tax and is not an income tax, and there is similarly no question that it is creditable against the State of Washington's Business and Occupation ("B&O") excise tax and that it is deductible against the income taxes of many states.

The PPT is based on the gross value of oil or gas, minus the expenditures incurred to produce that oil or gas. The PPT legislation explicitly provides that PPT is deductible for Alaska's corporate income tax because it is not an income tax. However, Alaska cannot pass legislation that binds other states so that the PPT is creditable against Washington's B&O tax and deductible under the income taxes of other states.

What Alaska can do to keep PPT deductible and creditable is to clarify that it is not a tax on income or profits, but rather is an excise tax imposed on the act of severing and producing the oil or gas. Our proposed changes in terminology would make it clear that the PPT is an excise tax, not an income tax, and maintain the status quo of how the present production tax is treated in Alaska and elsewhere.

Senators Green, Wilken and Bunde
Representatives Chenault, Meyer and Stoltze
Senate Bill No. 305/House Bill No. 488 ("PPT")
April 13, 2006
Page 5

Thank you for this opportunity to share our recommendations with you and for your consideration of the amendments we offer. Please do not hesitate to contact us if you have any questions or comments about our present suggestions, or if we may be of further assistance to you.

Very truly yours,

ALASKA OIL AND GAS ASSOCIATION

/s/

Judith M. Brady
Executive Director

Attachment

cc: All Legislators (w/attachment)

AOGA'S PROPOSED PPT AMENDMENTS
to CSHB 488(RES) and CSSB 305(RES)

April 13, 2006

AMENDMENT NO. 1. 90% / 95% "SAFE HARBOR"

For CSHB 488(RES): On p. 6 line 9, between "becomes delinquent" and the period at the end of that sentence, insert "unless the producer has reasonable cause under (h) of this section for the underpayment"

On p. 7 line 23, between "becomes delinquent" and the period at the end of that sentence, insert "unless the producer has reasonable cause under (h) of this section for the underpayment"

For CSSB 305(RES): On p. 5 line 17, delete "as set out in this subsection" and replace with "monthly"

On p. 5, delete all material on lines 18-22 and "which the oil and gas were produced." on line 23, and replace with the following:

The tax, net of any credits applied under this chapter, is due on the last day of each calendar month on oil and gas produced from each lease or property during the preceding month.

On p. 7 line 24, between "becomes delinquent" and the period at the end of that sentence, insert "unless the producer has reasonable cause under (h) of this section for the underpayment"

On p. 7 line 10, delete "subsection" and replace with "subsections"

On p. 7 line 9, between "becomes delinquent" and the period at the end of that sentence, insert "unless the producer has reasonable cause under (h) of this section for the underpayment"

For CSHB 488(RES): On p. 7 lines 24-31, delete all material and replace with the following:

For CSSB 305(RES): On p. 7, between lines 9 and 10 insert the following:

(h) A producer has reasonable cause for an underpayment of tax under this section for any month if the total tax paid under this section for its taxable production during that month and the prior months of that calendar year is at least 90 percent of the total amount of tax due under this section for that month and those prior months as determined on the basis of the producer's

cumulative actual lease expenditures for the year as of the last day of that month and the lease expenditures budgeted for the remainder of the year as of that same day. A producer may also establish reasonable cause under this subsection for an underpayment on the basis of "reasonable cause" as defined for purposes of AS 43.05.220(a) or 26 U.S.C. 6651 (Internal Revenue Code) and Treasury Regulation § 301.6651-1(c).

AMENDMENT NO. 2. DEFINING AN "IMMATERIAL" USED PORTION OF AN OTHERWISE UNUSED ASSET

For CSHB 488(RES): On p. 10 line 30, delete "an immaterial portion" and replace with "15 percent"

For CSSB 305(RES): On p. 9 line 25, delete "an immaterial portion" and replace with "15 percent"

AMENDMENT NO. 3. DEDUCTIBLE "UPSTREAM" COSTS

For CSHB 488(RES): On p. 19 line 13, at the beginning of the line insert "in support of activities" before "upstream"

For CSSB 305(RES): On p. 15 line 29, at the beginning of the line insert "in support of activities" before "upstream"

AMENDMENT NO. 4. DEFINING SCOPE OF DEDUCTIBLE COSTS BY APPLYING INDUSTRY PRACTICE

For CSHB 488(RES): On p. 19 line 27, delete "give substantial weight to" and replace with "apply"

On p. 19 line 29, delete "as to costs" and replace with "in determining the amount"

On p. 20 line 1, delete ", not" and replace with "other than"

On p. 20 line 3, between "(B)" and "the standards" insert the following:

in the absence of unit operating agreements or similar operating agreements that were in effect on or before December 1, 2005, and were subject to negotiation with working interest owners, other than the operator, with substantial bargaining power.

For CSSB 305 (RES): On p. 16 line 8, delete "give substantial weight to" and replace with "apply"

On p. 16 line 10, delete "as to costs" and replace with "in determining the amount"

On p. 16 line 13, delete “, not” and replace with “other than”

On p. 16 line 15, between “(B)” and “the standards” insert the following:

in the absence of unit operating agreements or similar operating agreements that were in effect on or before December 1, 2005, and were subject to negotiation with working interest owners, other than the operator, with substantial bargaining power,

On p. 18, delete all material in lines 13-16, and in line 17 delete “(O)” and replace with “(N)”

On p. 19 line 18, delete “; the provisions of (k) and (l) of this”

On p. 19 line 19, delete “section apply to an asset that is subject to this subparagraph”

Beginning on p. 21 line 5 through p. 22 line 8 inclusive, delete all material

On p. 22 line 9, delete “(n)” and replace with “(k)”

AMENDMENT NO. 5. CLARIFYING OFFSETS AGAINST LEASE EXPENDITURES

For CSHB 488(RES): On p. 21 line 31, insert after “are” “the net working interest share of”

On p. 22 line 2, insert after “ownership interest” the phrase “to the extent that payment or credit is a deductible lease expenditure for that payor under 43.55.160.”

On p. 22 line 4, insert after “lease expenditures” “to the extent that payment or credit is for a deductible lease expenditure under 43.55.160”

For CSSB 305(RES): On p. 19 line 1, insert “the net working interest share of” before “payments or credits” at the beginning of the line

On p. 19 line 5, insert after “management fee” the phrase “to the extent that payment or credit is a deductible lease expenditure for that payor under 43.55.160.”

On p. 19 line 7, insert after “lease expenditures” “to the extent that payment or credit is for a deductible lease expenditure under 43.55.160”

AMENDMENT NO. 6. TO ENSURE DEDUCTIBILITY OF PPT UNDER OTHER STATES' INCOME TAXES

For CSHB 488(RES): On p. 1 line 1, delete “oil production tax and gas production tax” and replace with “oil and gas properties production tax”

On p. 1 lines 2, 6, 7 and 9, delete "production tax" and replace with "severance tax"

On p. 2, line 7, delete "production tax value" and replace with "gross severance value"

On p. 2, lines 7-8, delete "a tax on the production tax value of oil and gas" that carries over between the two lines and replace with "a severance tax on oil and gas"

On p. 2 lines 9 and 12, delete "production tax" and replace with "severance tax"

On p. 2 line 16, delete "a new section" and replace with "new sections"

On p. 2, between lines 20 and 21, insert the following:

INTENT OF AS 43.55.011(a) AS AMENDED BY THIS ACT AND OF AS 43.55.011(i) ENACTED BY THIS ACT. It is the intent of the legislature to tax the activity of severing oil and gas from the ground and the tax is to be measured on the value of oil and gas production as it is severed. The legislature recognizes that the costs permitted to be deducted under AS 43.55.160 are not properly included in the measure of the gross value of the oil and gas as they are severed, but rather are a measure of the cost and effort needed to complete the production of the oil and gas after severance; and therefore such costs are excluded from the measure of the tax.

On p. 3 lines 25-26: delete "production tax value" that carries over between the two lines and replace with "gross severance value"

On p. 5 lines 4-5, delete "gross value at the point of production" and replace with "gross severance value"

On p. 6, between lines 3 and 4 insert the following new Bill Section and renumber the remaining Bill Sections and the respective cross-references to them accordingly:

* Sec. 8. AS 43.55.017(c) is amended to read:

(c) The taxes imposed by the chapter are excise taxes on severing or extracting oil and gas from the ground. The taxes are not income or franchise taxes or taxes upon the sale of oil or gas products and are not imposed in lieu of such taxes.

On p. 8 line 4, delete "production tax value" and replace with "gross severance value"

On p. 11 lines 19 and 31; on p. 12 lines 29 and 30; and on p. 14 lines 3, 4, 6 (twice), 11, 12, 14, 15, 18, 19, 22 and 24, delete "production" and replace with "[PRODUCTION]"

On p. 18 line 13, delete "production tax value" and replace with "gross severance value"

On p. 18 lines 15, 20, 22 and 28 and on p. 19 lines 2 and 19, delete "production tax value" and replace with "gross severance value"

On p. 30 line 11, delete "PRODUCTION" at the beginning of the line

On p. 30 lines 11-12, delete "PRODUCTION TAX VALUE" that carries over between the two lines and replace with "GROSS SEVERANCE VALUE"

For CSSB 305(RES): On p. 1 line 1, delete "production tax" and replace with "severance tax"

On p. 1 line 2, insert "properties" before "production" at the beginning of the line and delete "(severance)"

On p. 1 line 3, insert "gross severance" between "determination of the" and "value"

On p. 1 lines 4, 5, 9 and 10 and on p. 2 line 6, delete "production tax" and replace with "severance tax"

On p. 2 line 10, delete "a new section" and replace with "new sections"

On p. 2, between lines 14 and 15, insert the following:

INTENT OF AS 43.55.011(e) ENACTED BY THIS ACT. It is the intent of the legislature to tax the activity of severing oil and gas from the ground and the tax is to be measured on the value of oil and gas production as it is severed. The legislature recognizes that the costs permitted to be deducted under AS 43.55.160 are not properly included in the measure of the gross value of the oil and gas as they are severed, but rather are a measure of the cost and effort needed to complete the production of the oil and gas after severance; and therefore such costs are excluded from the measure of the tax.

On p. 3 lines 17-18, delete "production tax value" that carries over between the two lines and replace with "gross severance value"

On p. 5 line 17, delete "production" and insert "under AS 43.55.011" between "oil and gas" and "shall be paid"

On p. 6 line 3, delete "production" and insert "under AS 43.55.011" between "gas" and "shall be paid"

On p. 6, between lines 3 and 4 insert the following new Bill Section and renumber the remaining Bill Sections and the respective cross-references to them accordingly:

* Sec. 7. AS 43.55.017(c) is amended to read:

(c) The taxes imposed by the chapter are excise taxes on severing or extracting oil and gas from the ground. The taxes are not income or franchise taxes or taxes upon the sale of oil or gas products and are not imposed in lieu of such taxes.

On p. 14 line 29, delete "production tax value" and replace with "gross severance value"

On p. 15 lines 1, 5, 7, 13, 18 and 25; on p. 19 line 28; on p. 20 lines 2, 4 and 19, delete "production tax value" and replace with "gross severance value"

On p. 28 lines 7 and 9, delete "Production" and replace with "Severance"

On p. 28 line 10, delete "production" and replace with "severance"

STATE OF ALASKA

DEPARTMENT OF REVENUE

OFFICE OF THE COMMISSIONER

3-31-06

FRANK H. MURKOWSKI, GOVERNOR

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March 31, 2006

Representative Mike Chenault, Co-Chair
House Finance Committee
State Capitol, Room 505
Juneau, AK 99801

Representative Kevin Meyer, Co-Chair
House Finance Committee
State Capitol, Room 515
Juneau, AK 99801

Re: Questions on PPT Legislation (CS for HB 488(RES))

Dear Representatives Chenault and Meyer,

Thank you for the opportunity to respond to questions posed during recent committee hearings. To date, we have received the following questions:

1. Why did the Governor offer five year transition (clawback) when capital has already been depreciated in the tax rate over a five to seven year period?

The Governor believes that this is a fairness issue. Once enacted, the PPT will measure tax based on net profit. These will be profits generated by investments made prior to the effective date of the legislation. The cost of all new investments will be reflected in the calculation of net profits; the costs will be deducted. However, the costs incurred for recent investments would not otherwise be reflected in the calculation. Without the transition deduction, the producer would be taxed on the profits generated by assets which would not be properly represented in the profit calculation.

Much of the oil and gas equipment is depreciated over seven years for federal tax purposes. In addition, certain oil and gas equipment is depreciated over 15 years. To our knowledge, the only oil and gas equipment with a 5-year life is offshore drilling equipment. It is notable, also, that these lives are those articulated for federal tax purposes. For accounting purposes, the depreciable lives are often longer than the lives under federal tax law. This means that very few of the assets are fully depreciated, even for those assets purchased five years ago.

The Governor believes that it is fair to give a five-year lookback for, in effect, depreciation expense on recent investments that are generating future profits which will be subject to tax.

2. Requested a written explanation of progressivity clause versus Governor's Bill.

As presented by the Governor, HB 488 included a fair tax rate of 20% of net profit. The Governor believes this strikes a good balance for long term state fiscal health. That bill did not include a progressive tax rate. Over the long run, increased revenues should be driven by increased investment and production rather than swings in commodity prices.

The CS for HB 388(RES) includes a two-pronged progressive tax rate. At prices between \$50 and \$100 per barrel, the progressive rate adds 3/10% of the wellhead value for every dollar the market price is over \$50. If the price of oil exceeds \$110 per barrel, the tax jumps up to 37.5% of gross wellhead value. The Governor believes that this is excessive, and will hinder future investment in the state.

3. Provide information on the decline of oil field production over next 50 years by field

See Attachment Section, indexed by question number.

4. I've been told that the incentives for the Major Producers are not the same as it would be for the new explorers. If that is so, what other incentives could we offer to make "wildcatters" interested in Alaska?

The Governor's bill was specifically designed to entice new entrants, particularly "wildcatters" to Alaska. The Governor's bill provides a 20% tax credit for exploration and capital investments, which could be immediately monetized by the explorer. In addition, current statute AS 43.55.025 provides a 40% credit for certain exploration expenditures. The Governor believes that these incentives are very adequate to promote new exploration.

5. Transition provisions should be allowed because no oil has been produced from those capital investments. But were those investments made at prices less than \$25/bbl and so would be recovered much more quickly at \$60/bbl? How is this accounted for in the clawback provision?

The transitional deduction (or "clawback") accounts for recent investments by, in effect, allowing depreciation expense to be recognized in the calculation of the net profits generated by those assets. From an accounting standpoint, depreciation expense is recognized on a systematic basis over the life of the asset. The asset is considered to generate net income evenly over the life of the asset. A windfall in one year does not change the asset's ability to generate income later in its useful life.

6. How much severance tax (dollars) did Alaska lose because the Kuparuk Tax went below the legacy field tax rate in 1998-99?

See Attachment Section, indexed by question number.

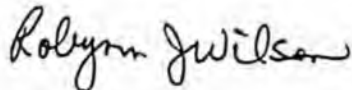
Letter to Reps. Chenault and Meyer
March 31, 2006
Page 3

7. How might we smooth the progressivity curve to eliminate or moderate the steep increase at \$110?

The elimination of the steep increase can be accomplished by changing the values at page 4 line 18, AS 43.55.011(g)(2) to reflect the desired price/index ceiling. If the index of 125 at \$110 is removed, and the progressivity tops out at \$110, then the top surcharge rate would be 18% applied to gross value.

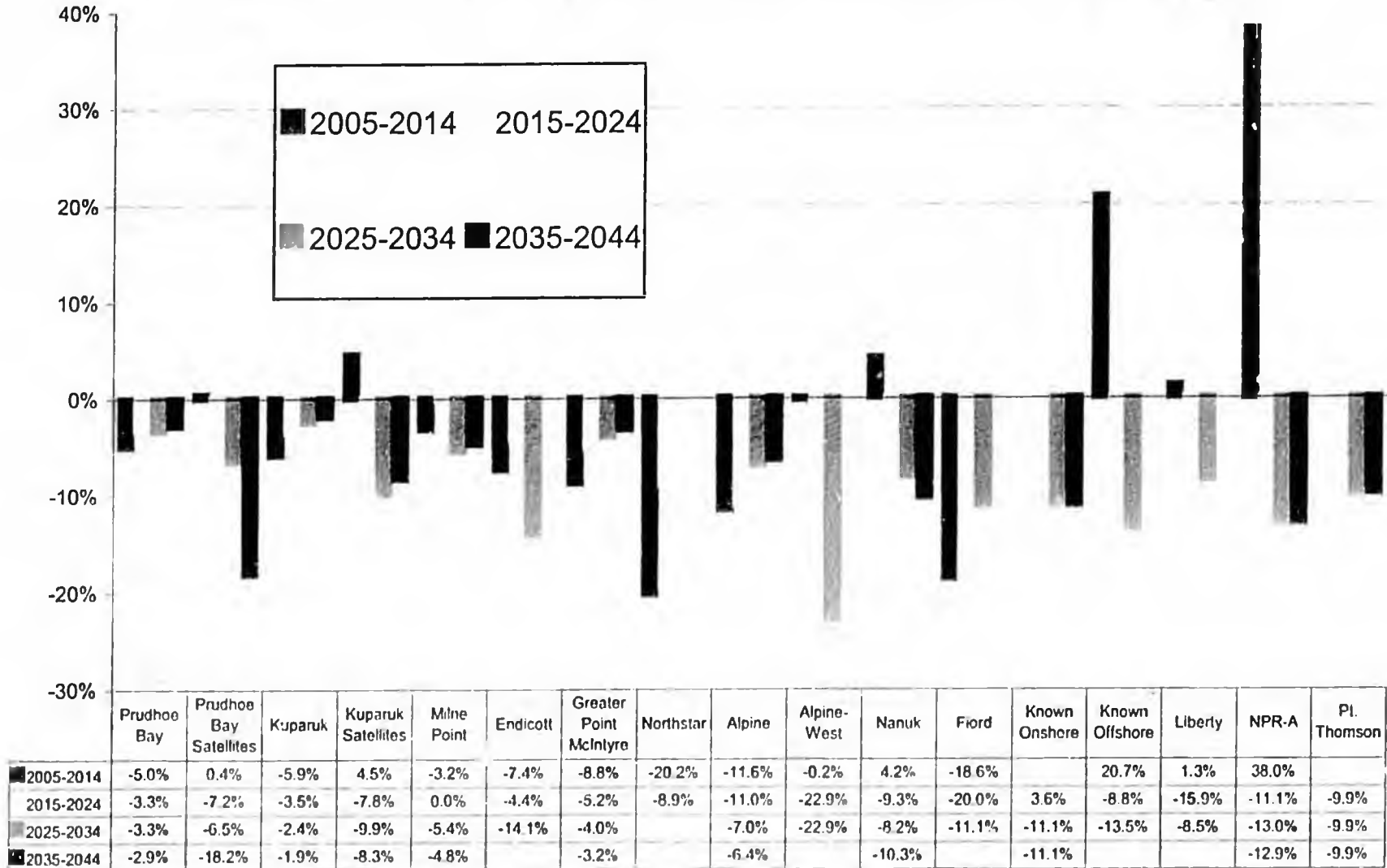
I hope that this information is helpful. Please let us know if you would like any additional information. Thank you for the opportunity to be of assistance.

Sincerely,



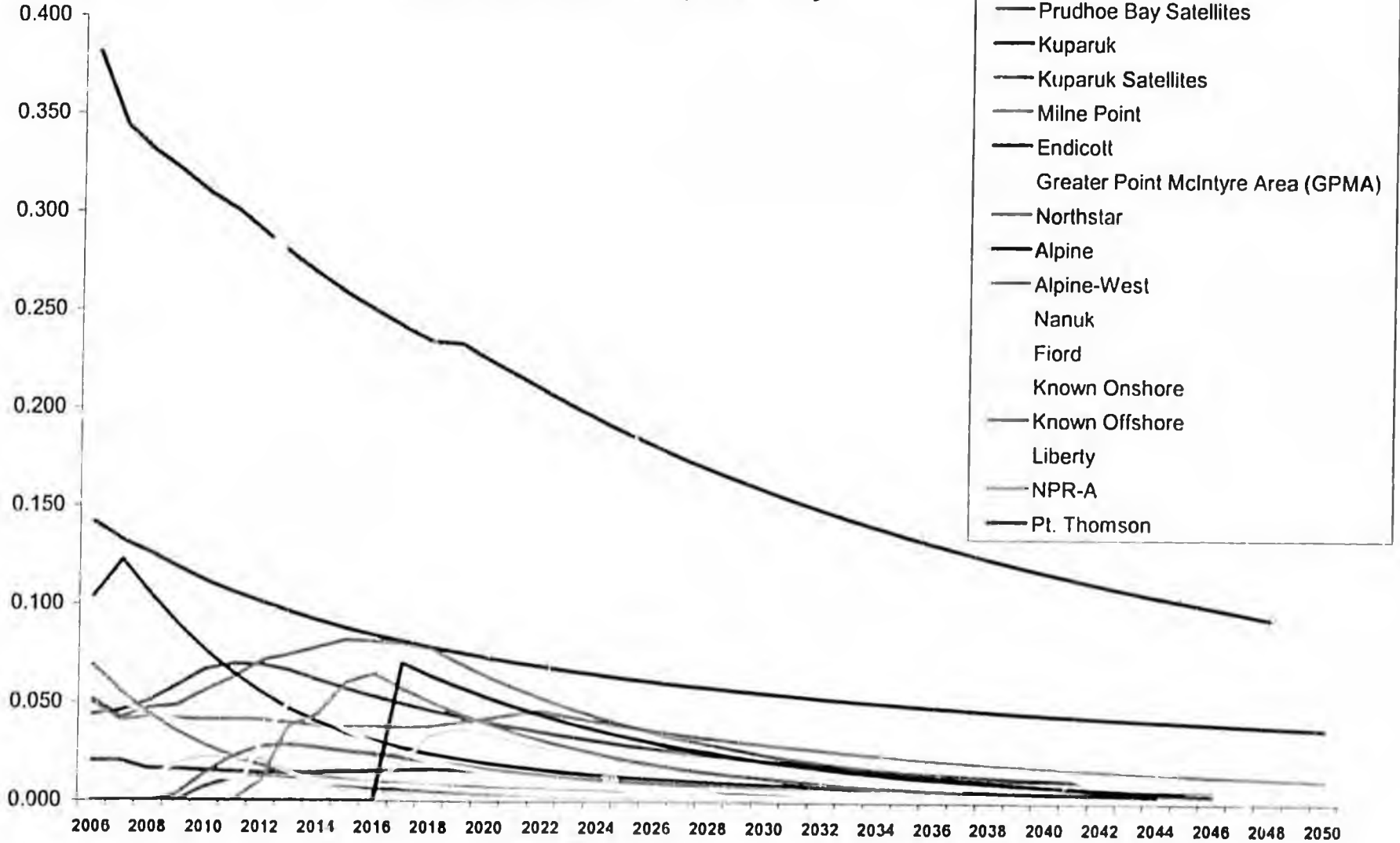
Robynn J. Wilson
Director, Tax Division
Department of Revenue

10-Year ANS Decline Rates by Field Based on DOR Spring 2006 Revenue Sources Book



ANS Production FY 2006-2050

Million Barrels per Day



Alaska Department of Revenue-Tax Division

Production Volume By Field: Million Barrels per Day
 - based on Spring 2006 Revenue Sources Book -

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)									Spring 2006	
	Prudhoe		Kuparuk		Milne	Greater Point McIntyre Area		Alpine-			Known	Known	Liberty	NPR-A	Thomson	PL	TOTAL			
FY	Prudhoe Bay	Bay Satellites	Kuparuk	Satellites	Point	Endicott	(GPMA)	Northstar	Alpine West	Nanut	Flord	Onshore	Offshore					ANS		
2006	0.381	0.044	0.142	0.052	0.050	0.021	0.056	0.069	0.104	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.917	
2007	0.344	0.046	0.133	0.042	0.041	0.020	0.050	0.055	0.122	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.854	
2008	0.331	0.051	0.126	0.047	0.043	0.017	0.045	0.044	0.105	0.000	0.006	0.011	0.000	0.000	0.000	0.000	0.000	0.000	0.825	
2009	0.321	0.059	0.119	0.048	0.042	0.016	0.041	0.035	0.090	0.000	0.011	0.019	0.000	0.003	0.000	0.000	0.000	0.000	0.803	
2010	0.309	0.067	0.112	0.056	0.041	0.016	0.037	0.028	0.076	0.007	0.012	0.023	0.000	0.014	0.000	0.000	0.000	0.000	0.799	
2011	0.301	0.069	0.106	0.063	0.042	0.015	0.034	0.023	0.065	0.012	0.012	0.023	0.000	0.023	0.000	0.000	0.000	0.000	0.786	
2012	0.289	0.069	0.101	0.071	0.041	0.014	0.032	0.018	0.055	0.012	0.011	0.021	0.000	0.028	0.030	0.010	0.000	0.000	0.802	
2013	0.277	0.066	0.096	0.074	0.040	0.015	0.030	0.015	0.047	0.011	0.010	0.015	0.000	0.028	0.050	0.038	0.000	0.000	0.813	
2014	0.267	0.061	0.092	0.078	0.038	0.015	0.028	0.012	0.040	0.010	0.010	0.008	0.010	0.027	0.045	0.044	0.000	0.000	0.785	
2015	0.257	0.057	0.088	0.082	0.038	0.015	0.026	0.011	0.035	0.008	0.009	0.005	0.010	0.025	0.036	0.060	0.000	0.000	0.762	
2016	0.249	0.053	0.084	0.081	0.038	0.015	0.025	0.009	0.031	0.007	0.008	0.004	0.010	0.024	0.030	0.064	0.000	0.000	0.732	
2017	0.241	0.049	0.081	0.080	0.037	0.016	0.023	0.009	0.027	0.005	0.008	0.003	0.019	0.022	0.025	0.057	0.070	0.000	0.772	
2018	0.233	0.046	0.078	0.078	0.038	0.016	0.022	0.008	0.024	0.004	0.007	0.003	0.033	0.020	0.021	0.050	0.064	0.000	0.746	
2019	0.233	0.043	0.075	0.070	0.040	0.016	0.021	0.007	0.022	0.004	0.006	0.003	0.037	0.019	0.017	0.044	0.058	0.000	0.714	
2020	0.224	0.040	0.073	0.064	0.042	0.015	0.020	0.007	0.019	0.003	0.006	0.002	0.034	0.017	0.015	0.039	0.053	0.000	0.673	
2021	0.217	0.038	0.070	0.058	0.044	0.015	0.019	0.006	0.018	0.002	0.005	0.002	0.030	0.015	0.013	0.035	0.048	0.000	0.635	
2022	0.208	0.035	0.068	0.052	0.046	0.014	0.018	0.006	0.016	0.002	0.005	0.002	0.027	0.014	0.012	0.031	0.044	0.000	0.599	
2023	0.201	0.033	0.068	0.047	0.043	0.012	0.017	0.005	0.015	0.002	0.004	0.001	0.025	0.013	0.010	0.027	0.040	0.000	0.561	
2024	0.194	0.031	0.064	0.043	0.040	0.011	0.017	0.005	0.013	0.001	0.004	0.001	0.022	0.012	0.009	0.024	0.036	0.000	0.527	
2025	0.187	0.029	0.063	0.039	0.038	0.010	0.016	0.005	0.012	0.001	0.004	0.001	0.020	0.011	0.008	0.021	0.033	0.000	0.488	
2026	0.180	0.027	0.061	0.035	0.036	0.009	0.015		0.011	0.001	0.003	0.001	0.018	0.010	0.007	0.019	0.030	0.000	0.463	
2027	0.174	0.025	0.059	0.032	0.034	0.007	0.015		0.011	0.001	0.003	0.001	0.016	0.010	0.007	0.017	0.027	0.000	0.438	
2028	0.168	0.023	0.058	0.029	0.032	0.006	0.014		0.010	0.001	0.003	0.001	0.015	0.009	0.006	0.015	0.025	0.000	0.414	
2029	0.163	0.022	0.056	0.027	0.030	0.005	0.013		0.009		0.003	0.001	0.013	0.008	0.006	0.013	0.023	0.000	0.392	
2030	0.157	0.021	0.055	0.024	0.029	0.005	0.013		0.009		0.003	0.001	0.012	0.007	0.005	0.012	0.021	0.000	0.372	
2031	0.152	0.019	0.054	0.022	0.027	0.005	0.012		0.008		0.003		0.011	0.003	0.005	0.010	0.019	0.000	0.353	
2032	0.148	0.018	0.052	0.020	0.026		0.012		0.008		0.002		0.010	0.005	0.005	0.009	0.017	0.000	0.331	
2033	0.143	0.017	0.051	0.018	0.025		0.012		0.007		0.002		0.009			0.008	0.015	0.000	0.307	
2034	0.139	0.016	0.050	0.017	0.024		0.011		0.007		0.002		0.008			0.007	0.014	0.000	0.294	
2035	0.135	0.015	0.049	0.015	0.022		0.011		0.006		0.002		0.007			0.006	0.013	0.000	0.281	
2036	0.131	0.014	0.048	0.014	0.021		0.010		0.006		0.002		0.006			0.006	0.012	0.000	0.270	
2037	0.127	0.014	0.047	0.013	0.020		0.010		0.006		0.001		0.006			0.005	0.011	0.000	0.259	
2038	0.123	0.013	0.046	0.012	0.019		0.010		0.005		0.001						0.010	0.000	0.239	
2039	0.120	0.012	0.045	0.011	0.018		0.009		0.005		0.001						0.009	0.000	0.231	
2040	0.116	0.011	0.045	0.010	0.018		0.009		0.005		0.001						0.008	0.000	0.223	
2041	0.113	0.011	0.044	0.009	0.017		0.009		0.004		0.001						0.007	0.000	0.215	
2042	0.110	0.005	0.043	0.009	0.016		0.009		0.004		0.001						0.007	0.000	0.202	
2043	0.107	0.004	0.042	0.008	0.015		0.008		0.004		0.001						0.006	0.000	0.196	
2044	0.104	0.004	0.041	0.007	0.015		0.008		0.004		0.001						0.005	0.000	0.190	
2045	0.102	0.004	0.041	0.007	0.014		0.008										0.005	0.000	0.180	
2046	0.099	0.004	0.040	0.007	0.013		0.008											0.000	0.000	0.171
2047	0.096		0.039		0.013		0.008											0.000	0.000	0.149
2048	0.094		0.039		0.012		0.008											0.000	0.000	0.145
2049			0.038		0.012		0.008											0.000	0.000	0.050
2050			0.037		0.011		0.008											0.000	0.000	0.049

Kuparuk

Question 6

CY	Wellhead	Barrels	ELF	Oil Severance Tax Calculated		Difference ELF=1 - Actual	Difference % of ELF=1
				Actual ELF	ELF = 1		
1995	\$11.37	106,679,819	0.8389	\$133,668,008	\$159,262,528	\$25,594,520	16.1%
1996	\$15.58	99,222,333	0.7964	\$161,366,850	\$202,961,961	\$41,595,111	20.5%
1997	\$14.52	95,738,430	0.7679	\$141,878,259	\$184,520,652	\$42,642,394	23.1%
1998	\$8.35	91,399,336	0.7318	\$74,586,433	\$101,643,668	\$27,057,235	26.6%
1999	\$13.22	82,079,519	0.6479	\$91,946,796	\$144,418,941	\$52,472,145	36.3%
2000	\$23.31	74,132,053	0.5368	\$123,025,832	\$230,006,226	\$106,980,394	46.5%
2001	\$17.68	68,264,000	0.4280	\$69,478,741	\$160,661,455	\$91,182,714	56.8%
2002	\$19.31	59,039,500	0.2485	\$36,593,749	\$151,749,704	\$115,155,955	75.9%
2003	\$24.37	58,533,619	0.2360	\$44,654,940	\$189,874,800	\$145,219,859	76.5%
2004	\$33.01	53,163,557	0.0872	\$19,451,298	\$233,617,710	\$214,166,412	91.7%
2005	\$46.42	50,415,356	0.0198	\$5,537,772	\$311,519,492	\$305,981,721	98.2%
Sum over period				\$902,188,677	\$2,070,237,137	\$1,168,048,460	56.4%

Comparing CSHB 488(RES)
to Senate Bill 305
(CSSB 305(FIN) am)

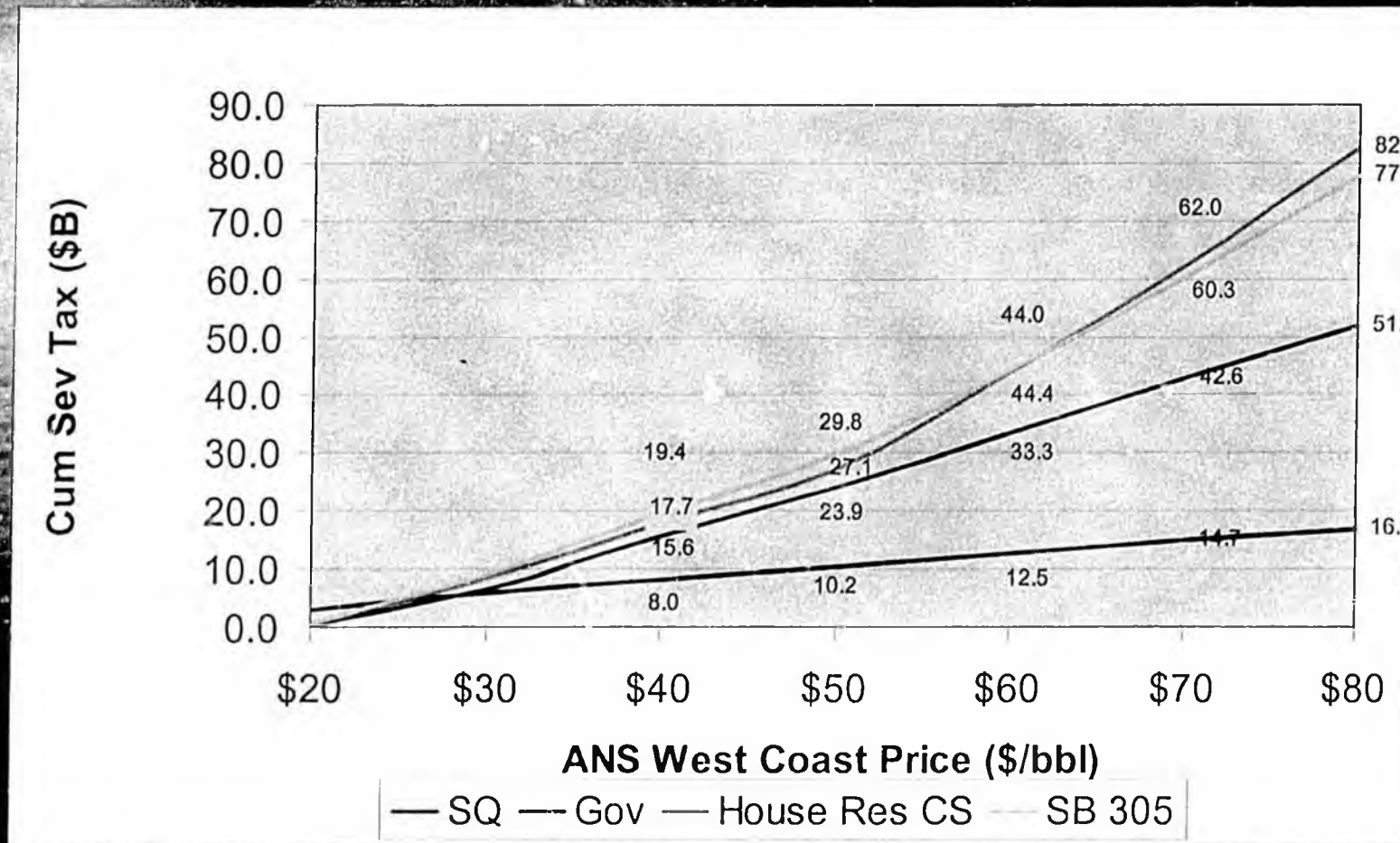
Before the House Finance
Committee

April 26, 2006

Robynn J. Wilson, CPA

Dan E. Dickinson, CPA

The Bottom Line: Cumulative Severance Tax (\$B) 2006-2030 Low Volume Scenario



2

Tax Rate:

CSHB 488(RES)

General rate: **20%**

Private royalty rate:
5% oil and gas

Cook Inlet oil: no
special provision

Gas: no special
treatment

SB 305

General rate: **22.5%**

Private royalty rate:
5% oil, 1.67% gas

Cook Inlet oil: 5% (net)

Gas: Special Revenue
(Value) exclusion

Gas Revenue (Value) Exclusion SB 305 (AS 43.55.160(a))

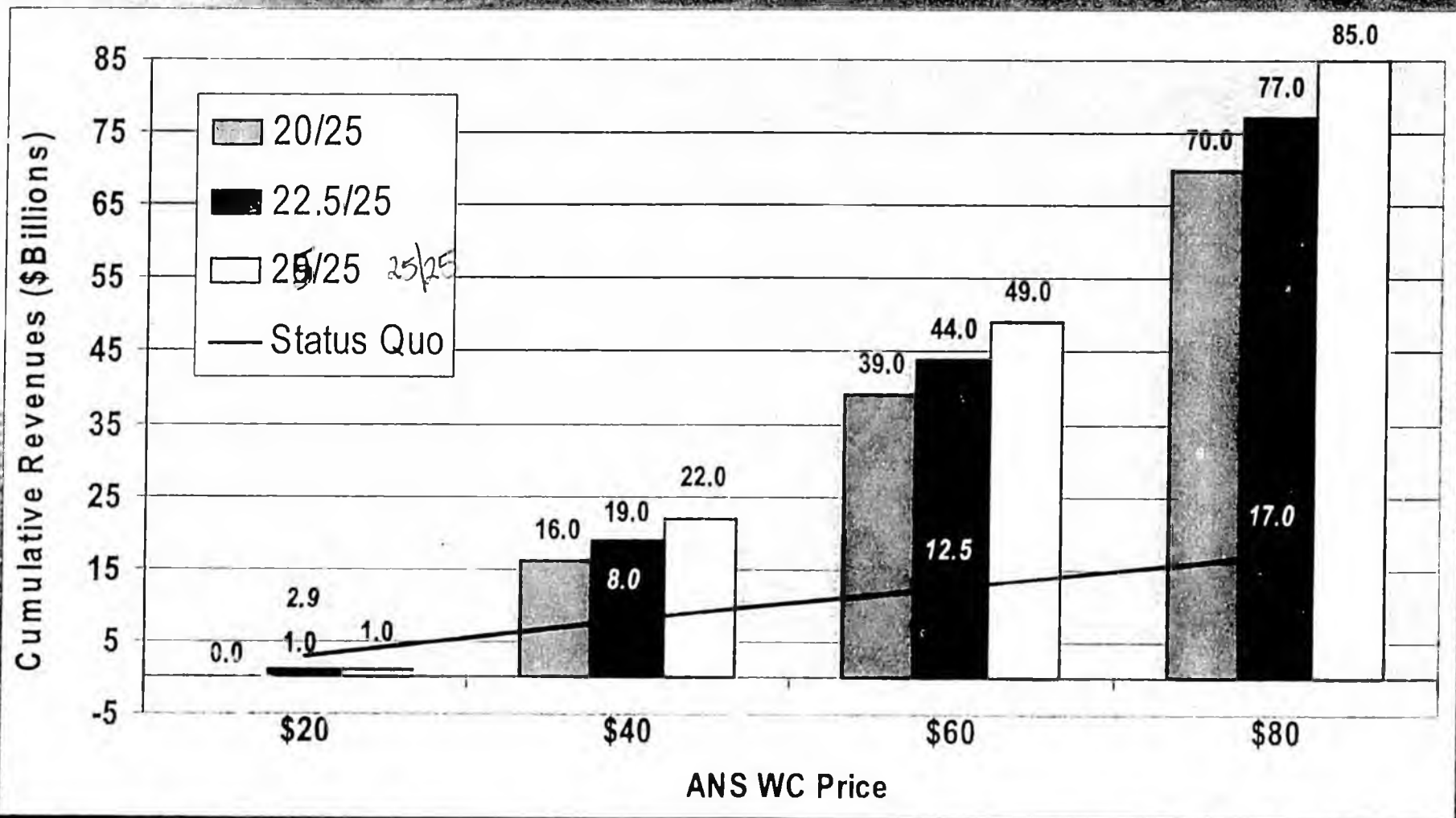
Gross value excludes 2/3 of the value of gas

- Yields an effective rate (before deductions) of 7.5%
- On a net value basis yields an effective tax rate of near 5%
- Obviates the need to allocate expenses

Applies statewide on all gas

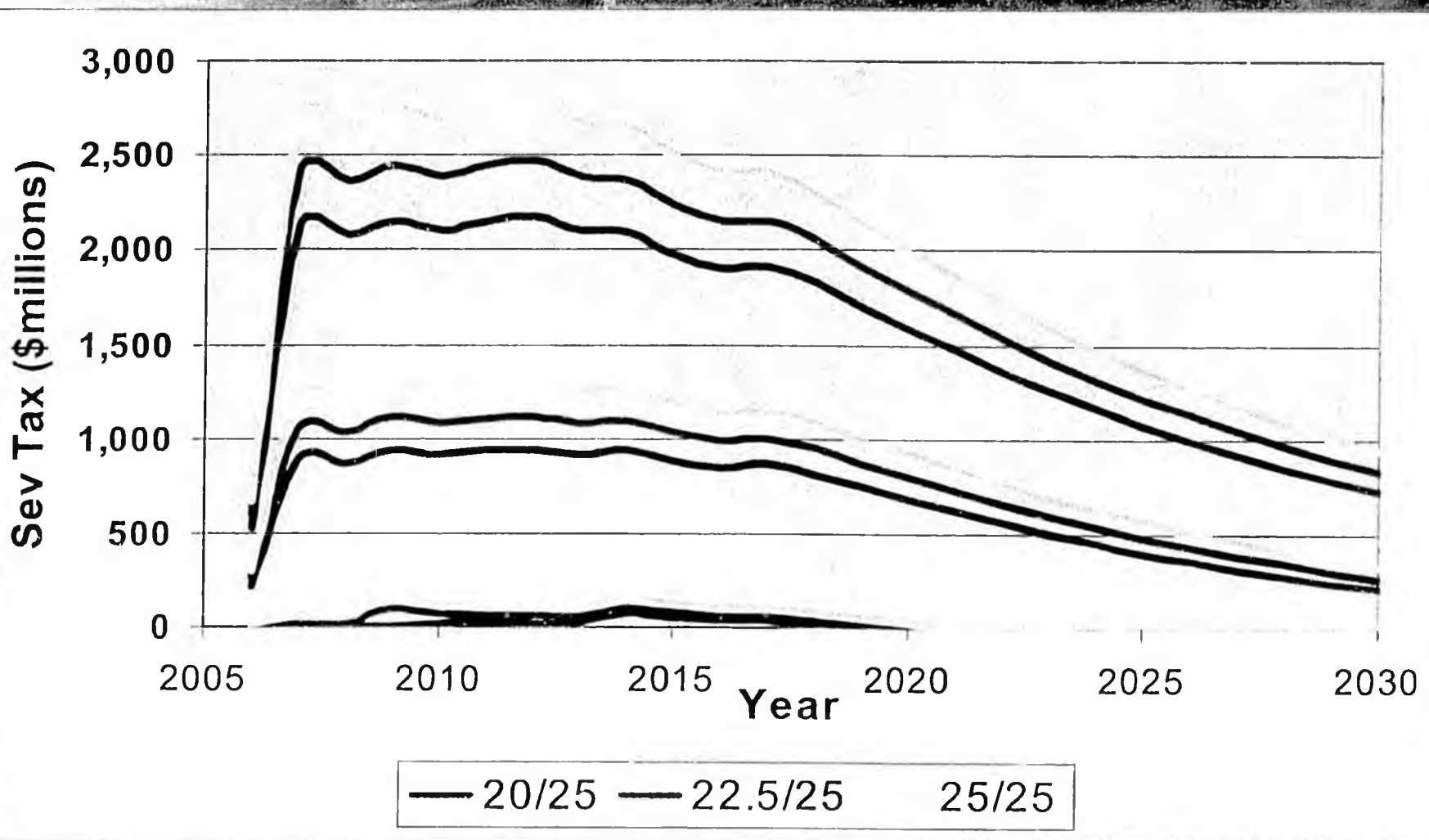
Effect of Tax Rate

Cumulative Severance Tax Revenues under SB 305 with 20%, 22.5%, and 25% Tax Rate, 2006-2030



Effect of Tax Rate

Annual Severance Tax under SB 305 with 20%, 22.5%, and 25% Tax Rate, 2006-2030 (\$millions)



Progressivity: CSHB 488(RES)

Progressivity on oil
Sec. 43.55.011(f), (g)

Triggered at \$50 WTI
slope factor .3%

$0.3\% \times (\text{WTI} - \$50)$
Jumps to 37.5% at
\$110

Progressivity on gas
Sec. 43.55.011(i), (j)

Triggered at \$8 HH
slope factor 2%

$2\% \times (\text{HH} - \$8)$
Jumps to 37.5% at \$18

Progressivity: SB 305

AS 43.55.011(g) & (h)

Applies to oil only

Triggered at \$50 ANSwc

Slope factor .00155

SB 305 progressivity formula

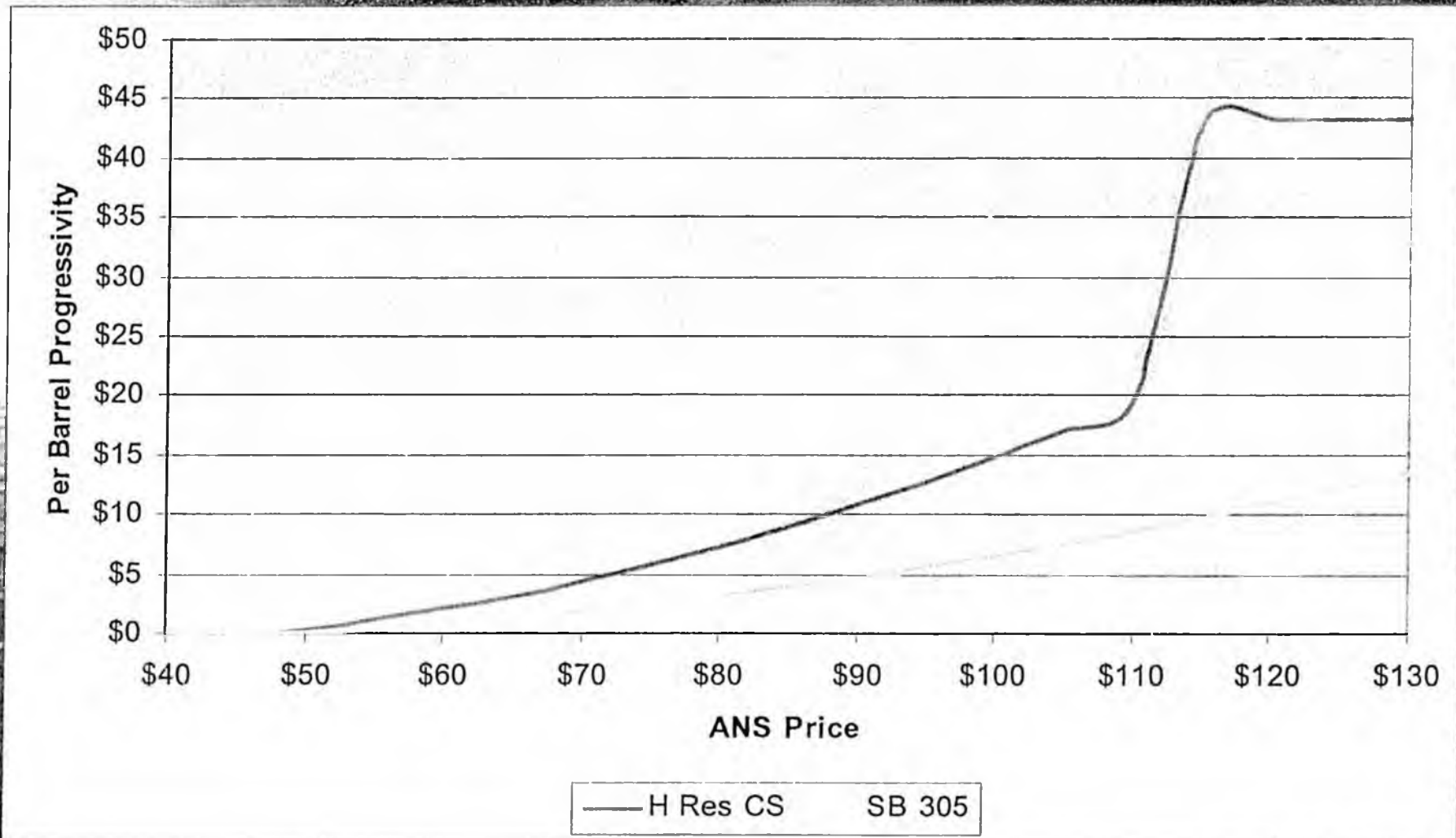
$(ANS_{wc} - \$50) \times .002) \times [ANS_{wh} \times (1 - PPT \text{ rate})]$ x (total taxable barrels of oil)
is the same as—

$(ANS_{wc} - \$50) \times .00155 \times ANS_{wh} \times$ (total taxable barrels of oil)

“ANS_{wh} price” means the **prevailing value** for oil produced in the Alaska ANS area

Effects of Progressivity

Progressive Surcharge per Barrel, 2010



Capital Investment Credit

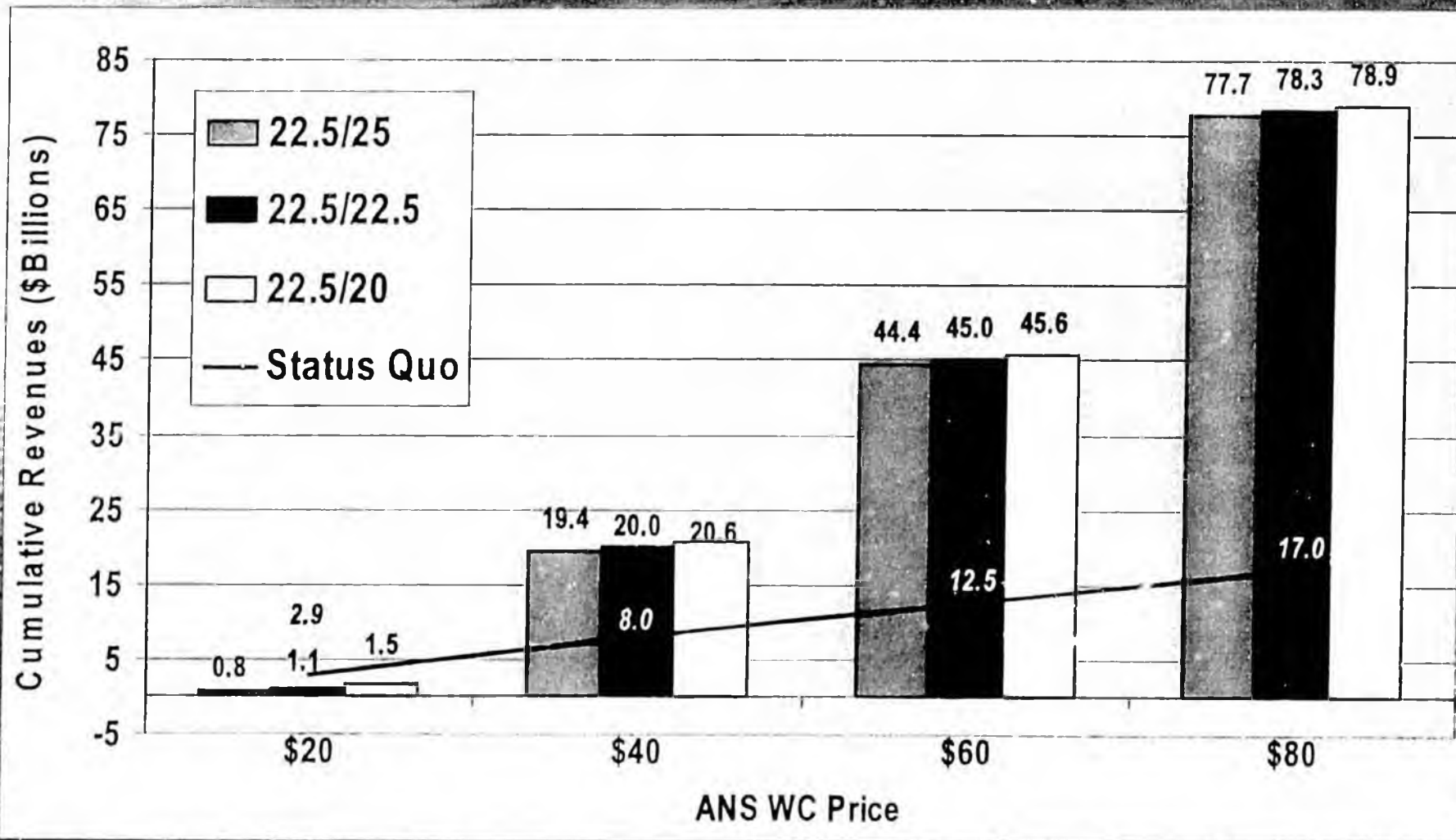
AS 43.55.024

CSHB 488(RES): **20%**

SB 305: **25%**

Effect of Credit Rate

Cumulative Severance Tax Revenues under SB 305 with
25%, 22.5%, and 20% Credit Rate, (2006—2030)



Capital Investment Credit (continued)

Both CSHB 488(RES) and SB 305:

Credit applies to PPT general tax only
(not against progressivity tax or spill
surcharges)

Credits are transferable—purchaser limited
to 20% tax shelter

Credits Refundable

CSHB 488(RES): up to \$10M depending
on current investment

SB 305: no provision

Carryforward of Loss

Both CSHB 488(RES) and SB 305:

Loss is carried forward to next month

At end of year, loss is converted to credit at
tax rate:

CSHB 488(RES)—20%

SB 305—22.5%

Treatment of Progressivity Tax

CSHB 488(RES)

AS 43.55.160(a)

Progressivity tax is
deductible like a lease
expenditure

SB 305

AS 43.55.160(d)(2)(O)

Progressivity tax is not
deductible

Transition: CSHB 488(RES)
AS 43.55.160(c)(1) & Sec. 42 uncodified

Deduction

Lookback: 3 months
Applies to: capex and opex
Deductible: over 9 months
Sunsets: No

Transition: SB 305
2 for 1 (AS 43.55.024(i))

Credit: 20%

Lookback: 5 years

Applies to: capex

Benefits: 7 years

Sunsets: 3/31/2013

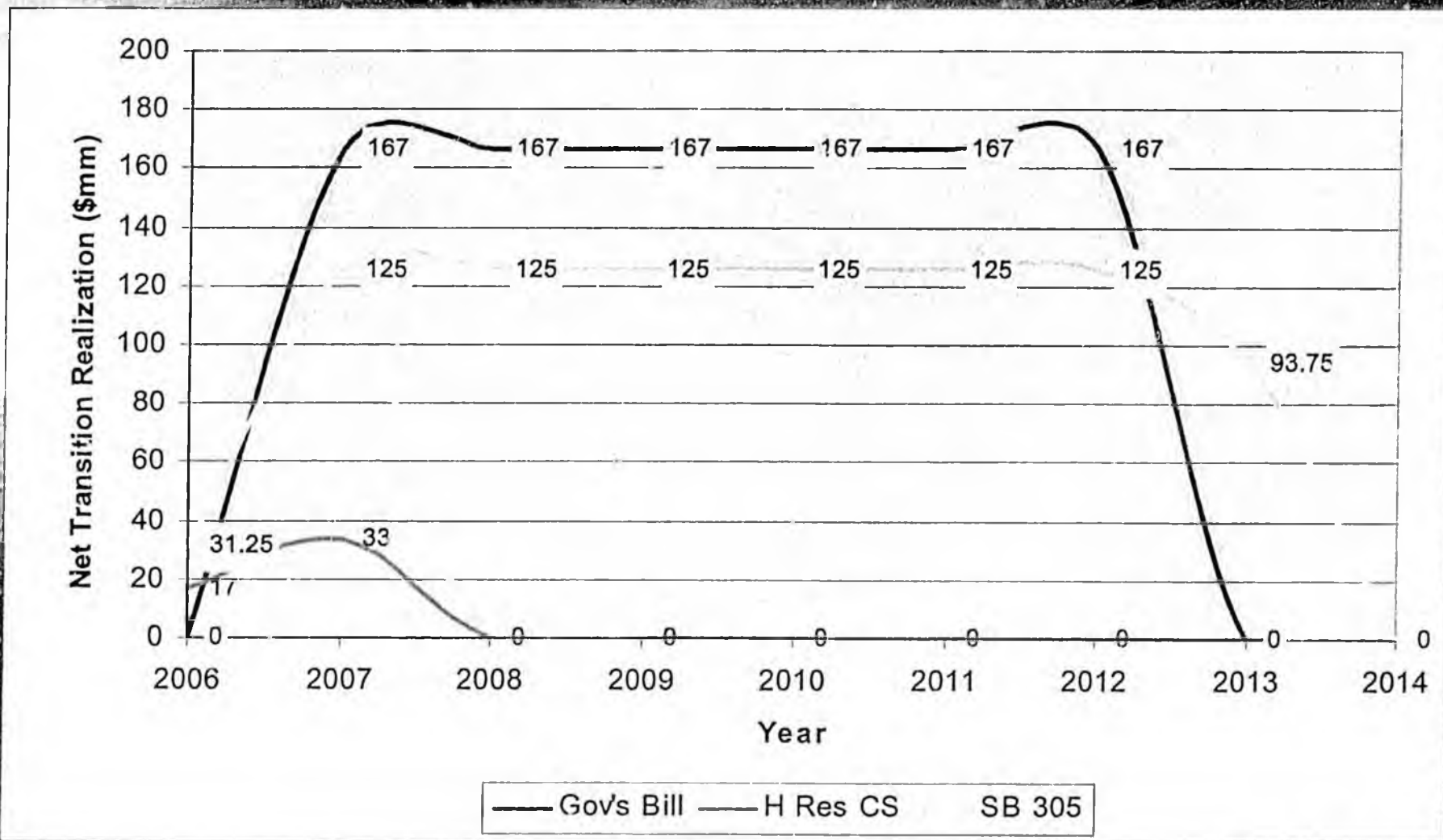
SB 305: 2 for 1

recoupment
5 yr 7 yr.

C	historic investment per year		35		35
D	years of lookback ¹		5		5
	total lookback	\$	175	\$	175
D	total credit available (20%)		35		35
E	recoupment time		5		7
F	claim available per year	\$	35	\$	25
G	current investment required	\$	70	\$	50
H	increase over historic		100%		43%

Effect of Transition

Net Transition Realizations, 2006-2014



Base Allowance: CSHB 488(RES)
Sec. 43.55.170(a)

Credit: \$12M per year per company

Sunsets: 3/31/2016

Base Allowance: SB 305
5000 barrel plan
AS 43.55.170(a)

Credit: based on production

Maximum: \$14M

Sunsets: 3/31/2016

Base Allowance: SB 305 (continued)

Under 5000 bpd

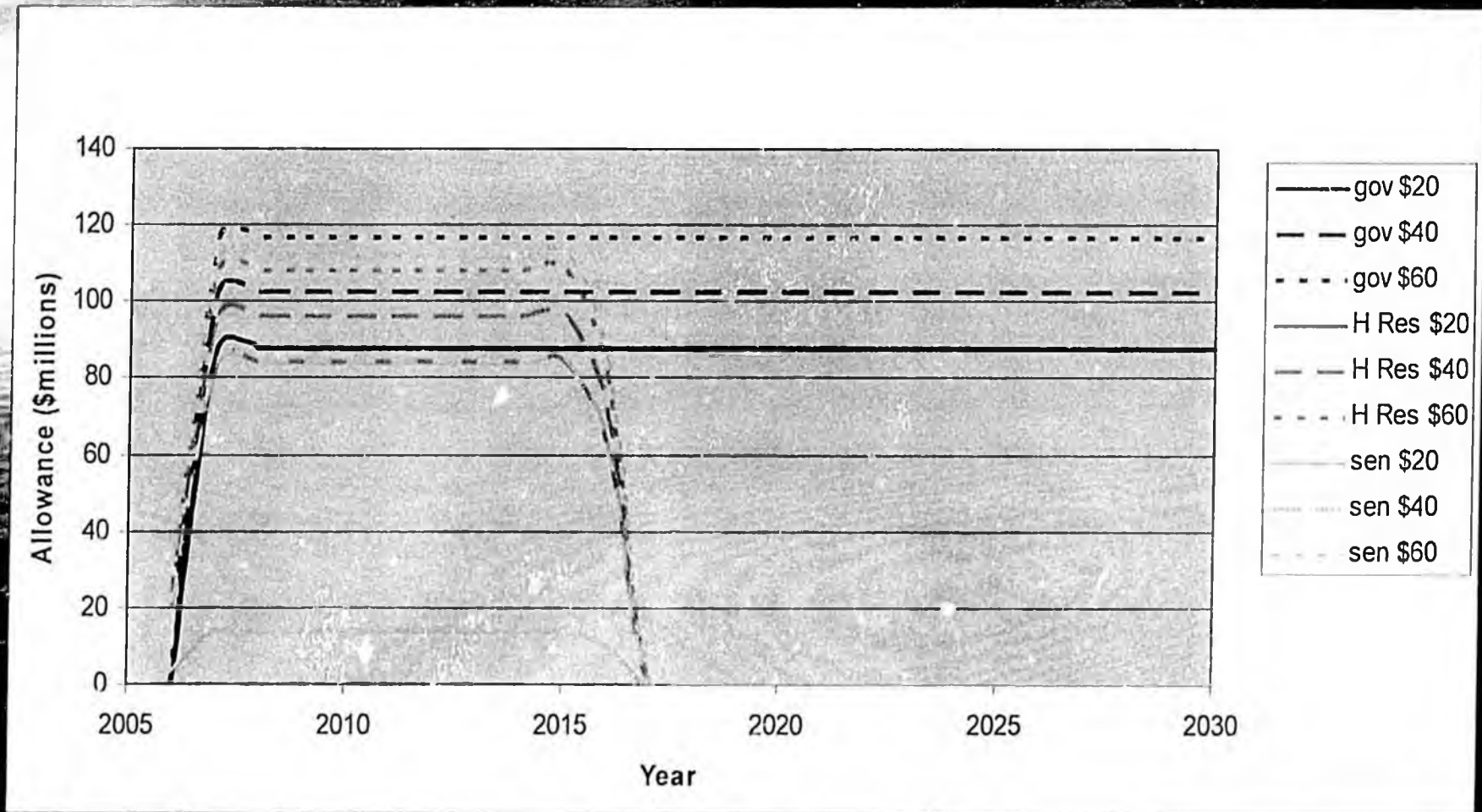
credit equal to 100% tax sheltered

Over 5000 bpd

percentage of tax sheltered

formula: $5000 / \text{total bpd} = \% \text{ shelter}$

Allowances 2006-2030 (\$millions)



Safe Harbor

CSHB 488(RES)

AS 43.55.020(h)

Safe harbor: 90%

If not met:

interest

penalty 5%

SB 305

AS 43.55.020(a)

Safe harbor: 95%

If not met:

interest on amount up

to 95%