

SCOMM

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ALASKA STATE LEGISLATURE



Official Business

HOUSE SPECIAL COMMITTEE ON OIL AND GAS

Representative Kurt Olson, Chair
State Capitol, Room 408
Juneau, AK 99801-1182
Phone 907-465-2693 Fax 907-465-3835

Wednesday, October 24, 2007

House Finance Committee Room 519

9am – noon

1:30pm – 3pm if required

5:30pm – until complete

AGENDA

HB 2001 - Oil and Gas Production Tax Amendments

9 am

- Steve Porter - Consultant on contract to LB&A

5:30 pm

- Public Testimony – (Individual testimony time may be limited.)

SB 2001/HB 2001
October 20, 2007
Supplement to the Sectional Analysis of October 1 2007
Authors: Dan Dickinson & Steve Porter

Approximately 50 sections of the bills submitted on the first day of the special session were changed from the October 1 work draft. Where those changes were only punctuation, style, word, or grammar edits that do not affect the original analysis they are merely listed as "minor changes."

Minor changes – Section 1

Section 2 – Expands "data" that must be provided by DNR to DOR to "reports, files and other information."

Section 8 – Although this section adds approximately 5 pages of text to the bill, it merely restates the entire existing text of AS 38.05.180 (j) in order to make a change to AS 38.05.180(j) (6) (B). Section 8 was originally just the text of AS 38.05.180(j) (6) (B).

Section 10 – Adds Department of Natural Resource royalty auditors to the list of exempt employees.

Minor changes – Sections 15 – 22; 24 – 26

Section 26 also incorporates two substantive changes.

1. If more than one explorer holds an interest in a well, to obtain a .023 credit for exploration, that explorer, and any others holding an interest in the exploration, have to agree in writing not to invoke their rights to have information held confidential by DNR longer than 2 years.
2. The two legacy fields – Prudhoe and Kuparuk are "combined." Credits still cannot be applied against taxes from other non-legacy fields. However, unlike the October 1 work draft of the bill, credits from one legacy field can be applied against taxes from the other.

Minor changes – Sections 27 – 29; 36 – 39

Section 39 also incorporates two substantive changes

1. If more than one explorer holds an interest in a well, to obtain a .025 credit for exploration, that explorer, and any others holding an interest in the exploration, have to agree in writing not to invoke their rights to have information held confidential by DNR longer than 2 years.
2. The 30 day period that an explorer has to provide certain data to DNR may be extended to "a period provided by the Department of Natural Resources."

Supplemental Sectional Analysis of SB/HB 2001

Minor changes – Sections 42, 44 – 46

Section 47 - Makes clear that the \$1,000 a day reporting penalty applies to both “reports” and “statements.”

Minor changes – Sections 48 – 50

Section 51 – Authorizes the DOR to issue non-binding “advisory” opinions. The opinion is not binding on the DOR, meaning that if a taxpayer relies on the opinion and the department subsequently changes its mind, merely having followed the advisory opinion does not shield the taxpayer from interest and penalties.

Minor changes – Sections 42, 54, 55, 56

Section 58 – Adds any costs arising from “violations of law, or failure to comply with an obligation under a lease, permit or license issued by the federal government” to the list of costs which must be excluded from qualified lease expenditures.

Minor changes – Sections 59, 60 and 62

Section 63 (a), (b) and (c) are now section 63, 64 and 65, and subsequent sections 64 – 71 are renumbered 66 – 73.

In the new Section 67, DNR auditors are given (as DOR auditors were in the original bill) 90 days to opt to either become exempt or to retain their status in a union position.

Title: **FY2005 to FY 2008 Petroleum Revenue**

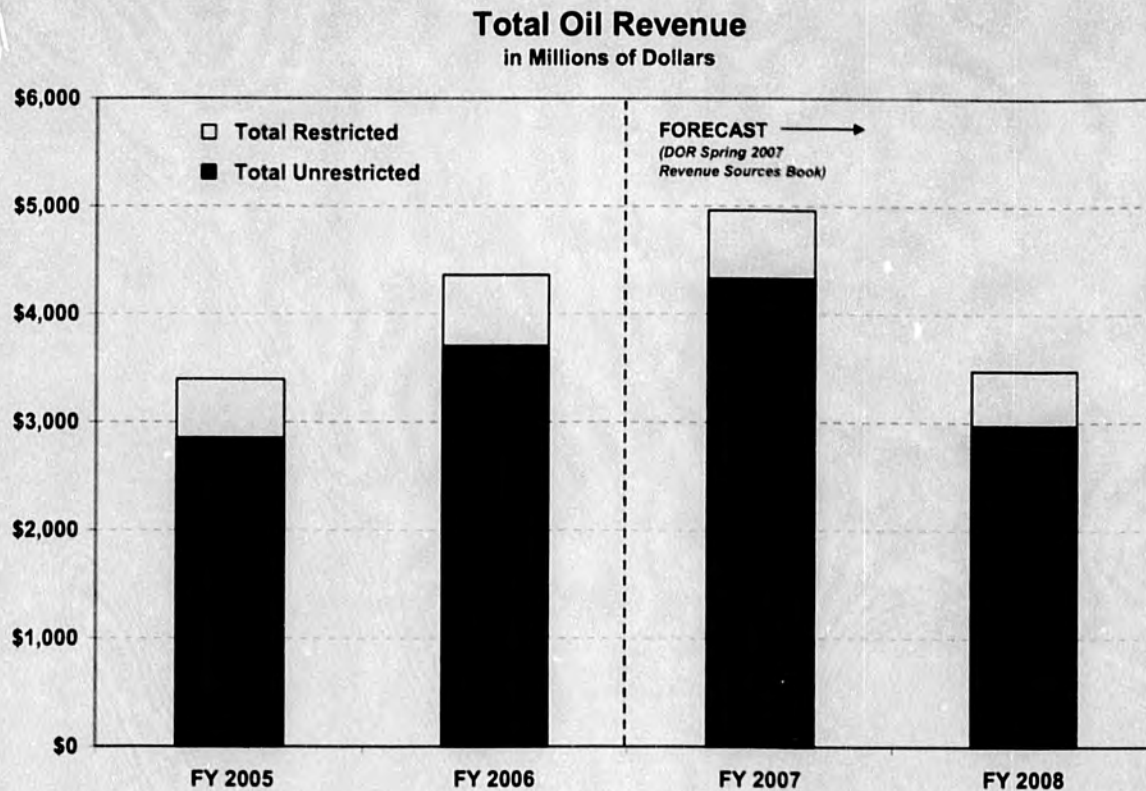
Data Sources: Alaska Department of Revenue, Tax Division
FY 2005 & FY 2006 from DOR historical database
FY 2007 Preliminary estimates
FY 2008 forecast from the Spring 2007 *Revenue Sources Book*

Prepared by: Jennifer Duval, Economist
jennifer.duval@alaska.gov

Date: October 23, 2007

Purpose: Request by Senator Huggins

Notes: Dollar amounts are millions of nominal dollars



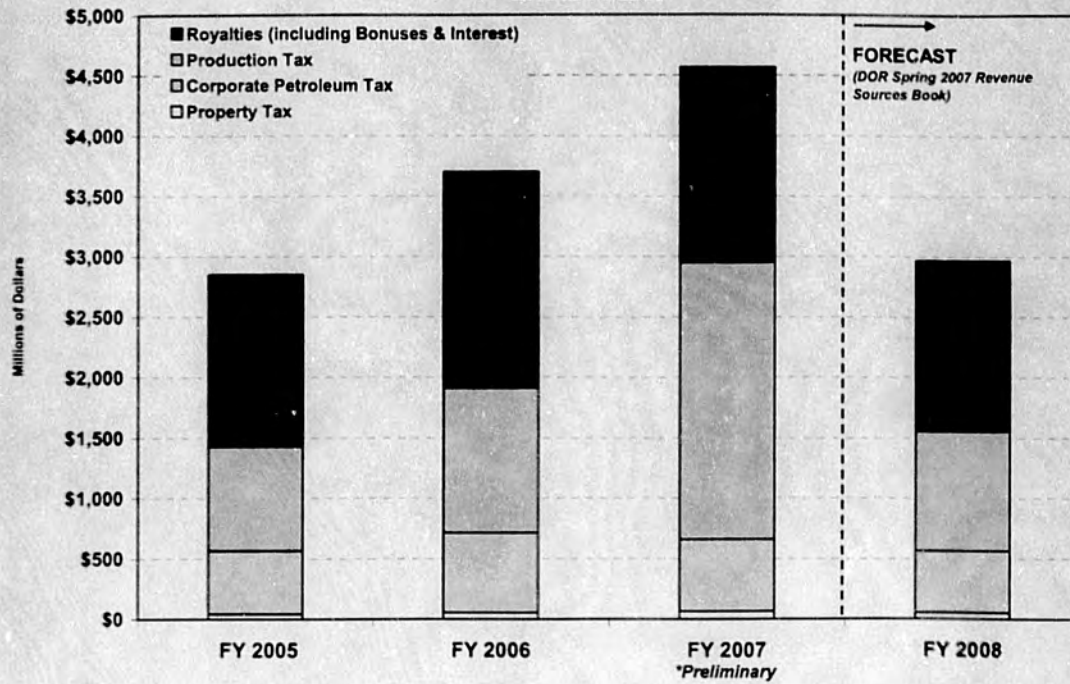
Historical and Forecast Oil Revenues FY 2005 - FY 2008

Source: DOR Spring 2007 Revenue Sources Book

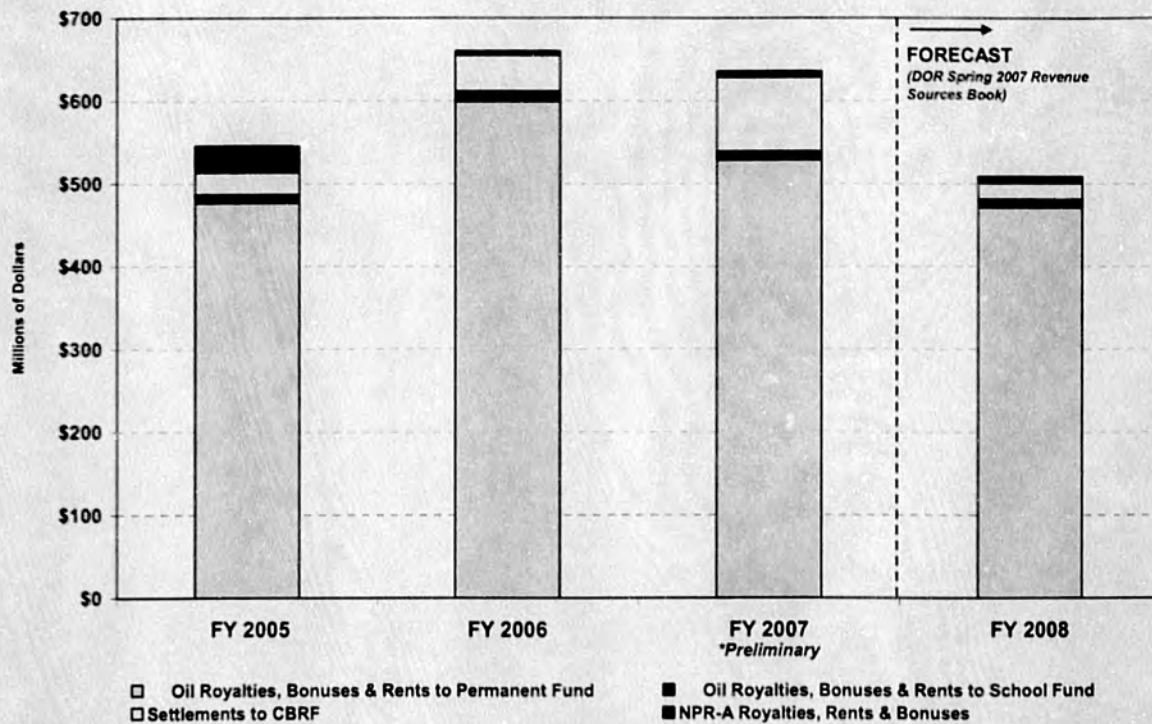
<i>in Millions of Dollars</i>	ACTUAL FY 2005	ACTUAL FY 2006	PRELIM ACTUAL FY 2007 (10/22/07)	SPR 07 FORECAST FY 2008
Unrestricted				
Property Tax	42.5	54.5	65.6	53.2
Corporate Petroleum Tax	524.0	661.1	594.4	512.1
Oil & Gas Production	854.9	1,191.7	2,282.2	983.1
Oil & Gas Hazardous Release	8.3	7.8	10.1	12.3
Production Tax	863.2	1,199.5	2,292.3	995.4
Mineral Bonuses & Rents	17.4	11.6	22.2	14.8
Oil and Gas Royalties	1401.1	1772.2	1,583.8	1,390.3
Interest	1.4	0.3	7.0	1.4
Royalties (including Bonuses & Interest)	1419.9	1784.1	1,613.0	1406.4
Total Unrestricted	2,849.6	3,699.2	4,565.3	2,967.10
Year-over-Year change	795.5	849.6	866.1	-1,598.2
Year-over-Year % change	38.7%	29.8%	23.4%	-35.0%
Restricted				
Oil Royalties, Bonuses & Rents to Permanent Fund	476.9	599.5	535.0	471.5
Oil Royalties, Bonuses & Rents to School Fund	9.6	12	10.6	9.4
Royalties to Permanent Fund & School Fund + Bonuses & Interest	486.5	611.5	545.7	480.9
Settlements to CBRF	27.4	43.7	113.6	20
NPR-A Royalties, Rents & Bonuses	31.6	4.5	12.8	7.6
Total Restricted	545.5	659.7	672.1	508.5
Total Oil	3,395.1	4,358.9	5,237.4	3,475.6

Percent of Total Oil	FY 2005	FY 2006	FY 2007	FY 2008
Property Tax	1.3%	1.3%	1.3%	1.5%
Corporate Petroleum Tax	15.4%	15.2%	11.3%	14.7%
Oil & Gas Production	25.2%	27.3%	43.6%	28.3%
Oil & Gas Hazardous Release	0.2%	0.2%	0.2%	0.4%
Production Tax	25.4%	27.5%	43.8%	28.6%
Mineral Bonuses & Rents	0.5%	0.3%	0.4%	0.4%
Oil and Gas Royalties	41.3%	40.7%	30.2%	40.0%
Interest	0.0%	0.0%	0.1%	0.0%
Royalties (including Bonuses & Interest)	41.8%	40.9%	30.8%	40.5%
Total Unrestricted	83.9%	84.9%	87.2%	85.4%
Restricted				
Oil Royalties, Bonuses & Rents to Permanent Fund	14.0%	13.8%	10.2%	13.6%
Oil Royalties, Bonuses & Rents to School Fund	0.3%	0.3%	0.2%	0.3%
Royalties to Permanent Fund & School Fund + Bonuses & Interest	14.3%	14.0%	10.4%	13.8%
Settlements to CBRF	0.8%	1.0%	2.2%	0.6%
NPR-A Royalties, Rents & Bonuses	0.9%	0.1%	0.2%	0.2%
Total Restricted	16.1%	15.1%	12.8%	14.6%
Total Oil	100%	100%	100%	100%

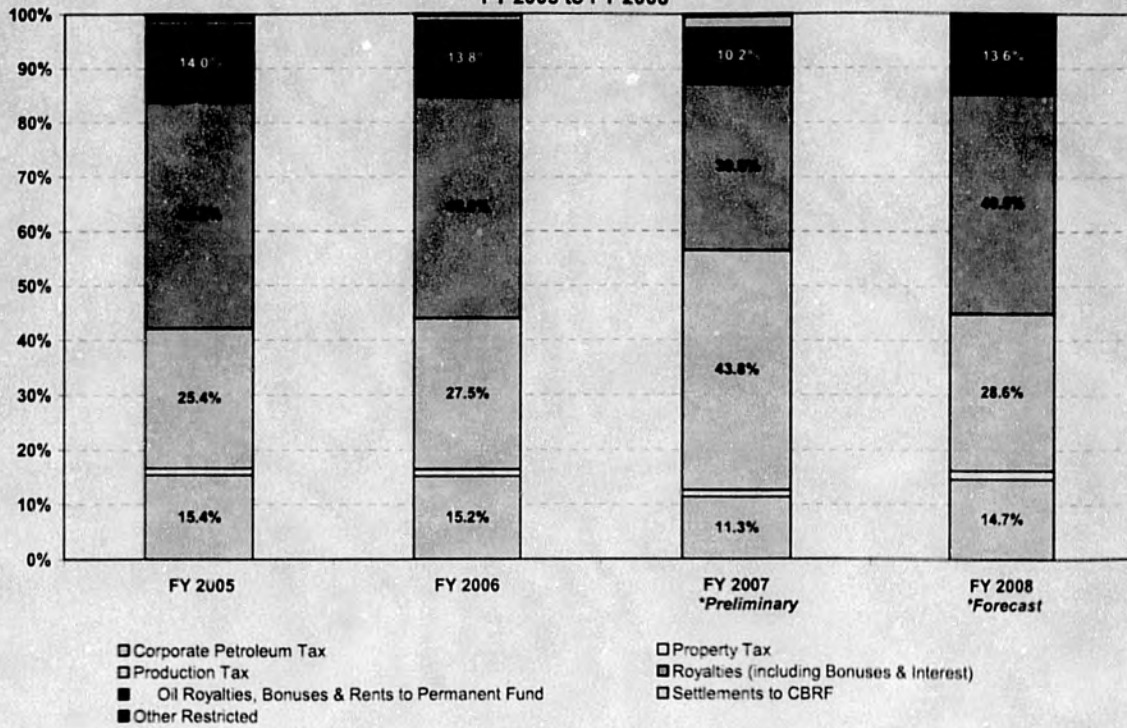
Unrestricted Oil Revenue by Category FY 2005 to FY 2008



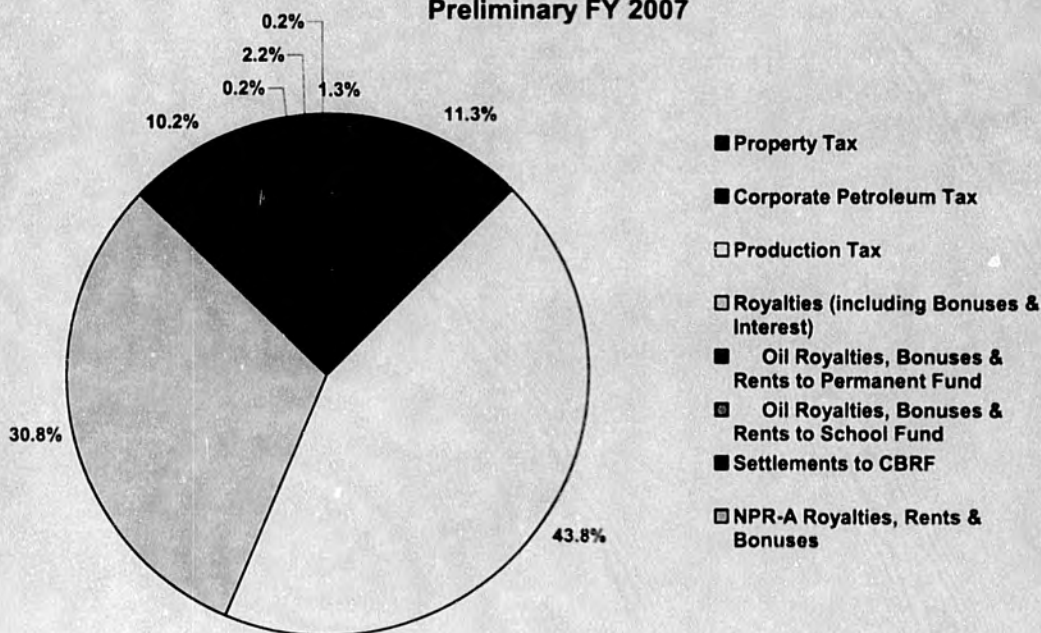
Restricted Oil Revenue FY 2005 to FY 2008



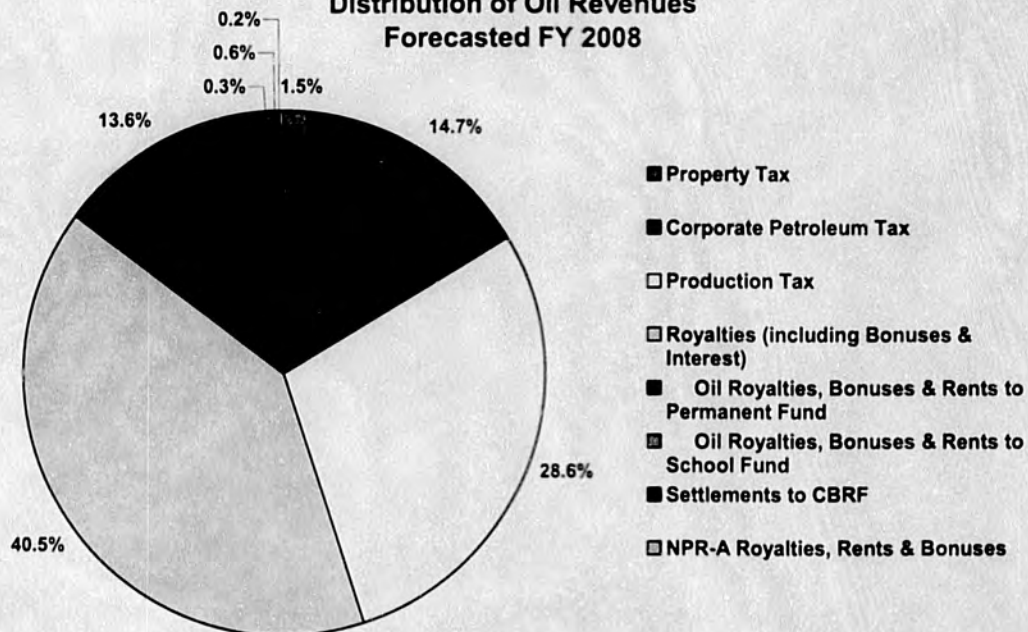
Percent Distribution of Total Oil Revenues by Year
FY 2005 to FY 2008



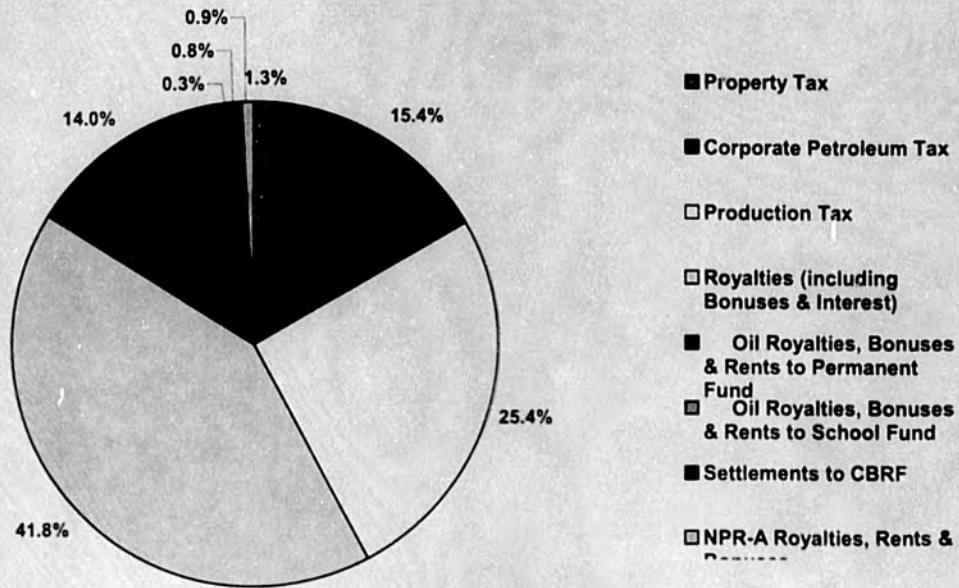
**Distribution of Oil Revenues
Preliminary FY 2007**



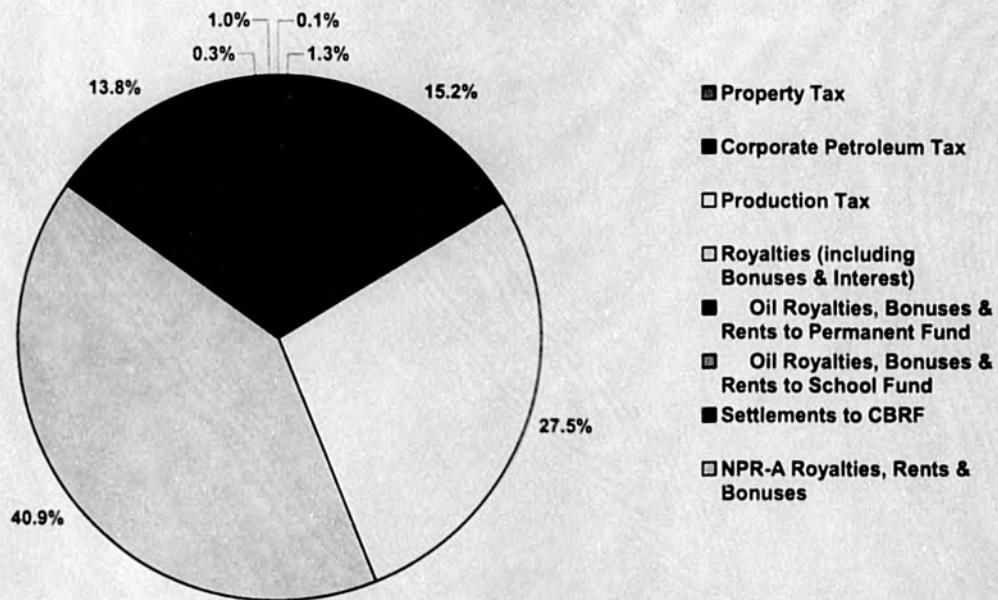
**Distribution of Oil Revenues
Forecasted FY 2008**



**Distribution of Oil Revenues
FY 2005**



**Distribution of Oil Revenues
FY 2006**



Senate Resources

Comments on Governor's ACES Proposal

Steven B Porter

10/22/2007

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Stability

- 1) Decision on Prudhoe Bay Satellites - Borealis, Midnight Sun, Orion, Polaris, Point McIntyre, and Aurora are integrated and collectively managed. Merely implemented the intent of the statute. When you consolidate wells with PBU facilities the regulations contemplate consolidation for tax purposes.
- 2) PPT tax. The producers have generally opposed any changes to the ELF prior to the SGDA negotiations. They liked the economics of ELF but knew they were going to have to agree to some change in order to get
 - a. Fiscal certainty under their contract
 - b. They were also hoping for contract approval if they agreed to the change
 - c. They lost on all counts.
 - i. They did not get the tax they "agreed to"
 - ii. They did not get any type of certainty on the tax
 - iii. They did not get the contract
- 3) The governor has called you back to review the tax because of the "cloud" on the tax. I don't think this review will cause the world to see you as unstable. The industry will certainly say it is true, but anyone who really looks underneath their rhetoric will know the truth. They also know the truth. This is merely an evaluation of what was done - with a possible early mid-course correction.
- 4) If you change the tax now and change it again during the regular session, there may be a problem.

Alaska's Prospectivity

1) Oil

- a. State lands- less than 20% of the future potential are on state lands where we receive both royalty and tax.
 - i. Puddles
 - ii. Heavy Oil – will come back to this
- b. NPRA – around 30% of future potential is in NPRA
 - i. No royalty but $\frac{1}{2}$ the royalty comes back to the state first as impact aid, then to fund PCE then another fund before it has a possibility to get to the general fund. Of the millions of dollars that the state has received from NPRA I don't think any of it has reached the general fund.
 - ii. Taxes – you still get taxes. But high costs will result in high opex and capex.
- c. Offshore OCS – over 50% of future potential is in the OCS
 - i. No royalty
 - ii. No taxes
- d. What is the future vision for oil
 - i. Gov should go to **congress** and get us the same as the Gulf States have. They get a share of the **OCS** revenues because the feds recognize that the local state jurisdictions are impacted by OCS development – and they can oppose it and prevent it from proceeding forward
 - 1. This should be before shell drills any exploration wells

2. Should work with the NSB to make sure that the operations in the OCS minimize the impact to the environment and local communities and subsistence culture
- ii. **Heavy oil** should be encouraged because it has the greatest chance on state lands of contributing to the future revenue stream of the state
 1. One of the slides yesterday showed the industry doing stress case economics at \$40. Commissioner Galvin stated that heavy oil will be impacted around \$41 dollars from the implementation of the **10% gross tax** which means that we may actually create a situation where we have prevented or slowed one of the most prospective oil reservoirs on state lands by passing the gross minimum tax. The minimum tax looks like it was designed to penalize heavy oil not help it.

e. **Alaska competitiveness –**

- i. We are a mature (between Colville and canning) province as far as oil is concerned. Geology is king. Heavy oil and puddles
- ii. NPRA has larger potential in the Alpine type range
- iii. OCS still has the elephants but at great cost and high environmental/legal risk.

2) **Gas**

- a. Pedro said the gas pipeline was uneconomic
- b. I would call it indeterminate
 - i. Four things needed to say economic or uneconomic
 1. Costs of the pipeline
 2. Future price of gas
 3. Stability of the taxes and what they are
 4. Internal Rate of Return/Project evaluation criteria

- c. The submittal of the proposals will not change the above substantially unless the applicants accepts, transfers, or provides a way to handle some of the above risks to the state's and the shipper's satisfaction.
 - d. When the proposals come out at the end of November the state should review the proposals then evaluate how they can help the state move the project forward. The project is not a gasline through Canada or an LNG line to Valdez. It is monetizing the North Slope gas resource to the greatest benefit of the people of the State of Alaska. It may mean making adjustments to the law in January. It may mean taking a new course, it also may mean AGIA is working and all that needs to be done is to implement it.
- 3) Timing of development in general and gas pipeline development specifically.
- a. A reasonable timeline for gas pipeline development is at least 10 years. Anything less than that you need to examine the proposal closely to make sure they are not shortcutting process that may impact them and the state in the future.
 - b. A reasonable timeline for oil development depends on proximity to existing facilities. E.g.,
 - i. Tarn took around 2 years and was probably one of the fastest because it was near Kuparuk.
 - ii. 6 to 8 years is a better estimate for prospects that are within 25 miles of existing facilities.
 - iii. Around 10 years for projects that is more remote.
 - iv. These are rough rules of thumb that don't take in to consideration specific environmental, logistics, cultural and subsistence issues of a particular project - each of which could delay development for several years.

ACES incentives

1) Legacy fields and all other existing fields.

- a. Places a higher tax burden on them
- b. Takes away the TIE credits
- c. Ring fences certain credits.

2) Explorers

- a. Places a higher tax burden on them
- b. Gives them a guarantee of getting their tax credit giving them 2% to 3% extra on their transferrable credits
- c. Moves net operating losses to 25% carryover.
- d. The costs of the higher tax exceed the credit benefit.

Summary

Someone asked yesterday what the governor's economic policy should be regarding oil and gas.

I recommend a few things

- 1) Encourage heavy oil development; don't place penalties in front of it.
- 2) Work with Congress to get our fair share of OCS revenue before shell or any other oil company drills in the OCS.
- 3) Works with local communities to make sure their concerns are addressed before development proceeds and so that responsible development can proceed.

House Oil & Gas Committee

POMS received
electronically and via fax
as of
5:20pm October 24, 2007

These POMS are in addition to those
already distributed.

Konrad Jackson

From: Shay Wilson
Sent: Wednesday, October 24, 2007 1:55 PM
To: Konrad Jackson
Subject: New Pom:Fire Protection

Tomas Boutin
Po Box 35116

Juneau 99803-5116,
b0utin@alaska.net
789-7936

CA wildfires point to AK situation. State and feds spend \$60 million on AK wildfire suppression. State has suppression/protection responsibility on state, muni & private land but has no input into suburban expansion and growth of wildland-urban interface. One-time state oil revenue pays. \$100 million fire season easy to imagine.

Konrad Jackson

From: Ken Erickson [ken@alaskapolitics.com]
Sent: Wednesday, October 24, 2007 11:57 AM
To: Konrad Jackson
Cc: zawackvv@wellsfargo.com
Subject: Re: Oil and gas tax

Konrad,

This ended up in my e-news in-box. Please add her comments to the public written testimony.

K

zawackvv@wellsfargo.com wrote:

>
> Please pass on my comments:
>
> It's my position to leave well enough alone. No one has
> ever taxed himself into posterity; if this is the case,
> our state government cannot do so either. The resources of
> Alaska belong to the people and I AM one of them.
>
> Also, how much is enough? The more money in the coffers,
> the more that will be spent on pet projects rather than on
> the services that ARE TO BE provided by government.
>
> *//**/Thank you,/*
>
> */Vir/**/ginia/**/ Zawacki/*
>

Konrad Jackson

From: Shay Wilson
Sent: Tuesday, October 23, 2007 7:19 PM
To: Konrad Jackson
Subject: New Pom:Miscellaneous

William Harvey Jr
13720 Davis St

Anchorage 99516-3614, blueraven
bluedog@ak.net

The political control of this state is run by the oil companies.
It's promulgated by their contributions to candidates that need the health and retirement
benefits of the state.
Look at Lyda Green, Koehring, Cowdery, Kott, & Andersen. Are you in that pot?

Hypocrites All!!!

We KNOW!!!

Konrad Jackson

From: Shay Wilson
Sent: Tuesday, October 23, 2007 6:49 PM
To: Konrad Jackson
Subject: New Pom:Oil & Gas

Christopher West
12810 Monterey Cir

Anchorage 99516-2752,
westcc@gmail.net
9075644626
9073455429

An uneconomic gas line, drying up of federal "pork", and decreased North Slope investment
leading to premature shutdown of TAPS.
All of these outcomes are a distinct possibility. Please approach the special session with
care - don't sacrifice the future for short term gain.

Konrad Jackson

From: Shay Wilson
Sent: Tuesday, October 23, 2007 5:29 PM
To: Konrad Jackson
Subject: New Pom:Oil & Gas

Jerry Mccutcheon
Po Box 101838

Anchorage 99510-1838,
susitnahydronow@yahoo.com

Chairman Huggins your statement "How are we going to pull off power generation?" Simple construct Susitna. The \$158million EIS has already been accepted by FERC. As chairman of resources you can ask Stevens, Murkowski, Young to ask the army corps of engineers to restudy Susitna's finances and it is free.

Konrad Jackson

From: Shay Wilson
Sent: Tuesday, October 23, 2007 4:54 PM
To: Konrad Jackson
Subject: New Pom:Oil & Gas

Lisa Peger
3873 Peger Rd

Fairbanks 99709-5464,Lisa Peger
lisapeger2@hotmail.com
907-452-8397
same

Dear legislators who wish to be re-elected, \$5,000 ONE TIME, ENERGY OFFSET, PFD for those who built the pipeline before they die. Next generation gets gas to sell and a big fund. Politics has throttled development, raised costs and burgeoned government. We need a bridge.

Konrad Jackson

From: Shay Wilson
Sent: Tuesday, October 23, 2007 4:40 PM
To: Konrad Jackson
Subject: New Pom:SB2001 Oil & Gas Tax Amendments

Jerry Mccutcheon
Po Box 101838

Anchorage 99510-1838,
susitnahydronow@yahoo.com

Shivley took \$95,000 bribe to rig a bid and ratted out Sheffield. Building owner sued state to force the state to buy the building. The Supreme Court said no a crime had been committed. The Briber would like his \$95,000 back. Who keep \$95,000, Shivley or Sheffield?

Konrad Jackson

From: Shay Wilson
Sent: Tuesday, October 23, 2007 3:20 PM
To: Konrad Jackson
Subject: New Pom:Criminal Procedure

Verne Rupright
866 W Spruce Ave
322 main st
Wasilla 99654,
vbattrny@mtaonline.net
373-3215
373-3223

Since you folks are fond of mandatory minimum sentences especially the republicans why not a mandatory minimum of 20 years for those convicted of public corruption type offenses why not set the example you leave most of us here wondering about you so whats good for the goose ...

Konrad Jackson

From: Shay Wilson
Sent: Tuesday, October 23, 2007 3:01 PM
To: Konrad Jackson
Subject: New Pom:Oil & Gas

Lisa Peger
3873 Peger Rd

Fairbanks 99709-5464, Lisa Peger
lisapeger2@hotmail.com
907-452-8397
same

Attention CBC's and all other legislators: pass Sarah's plan untouched except keep the 2.5 progressivity instead of 2%. Soon we will know who has misplaced allegiances and you can be the tossed salad of the next election. We're not going to forget or let you forget.

Good evening, my name is Tom Maloney and I appreciate the opportunity to testify regarding oil taxation. My background is in accounting and finance and I hold the following professional designations:

Certified Public Accountant

Certified Management Accountant

Certified Financial Planner

I have worked on Alaskan projects for 30 years and am currently employed by CH2M Hill. This testimony is personal and not on behalf of my employer or any trade organization.

There is a lot of discussion around taxation levels at legacy oil fields, like Prudhoe Bay and Kuparuk. It is worth mentioning that one hundred percent of all capital costs needed for North Slope infrastructure, Trans-Alaska pipeline, etc. was paid for by private funds, by a variety of companies. The resource risk, example; oil, gas, etc. was also born by the private investor.

There have been fields developed that have been un-economical, example; Badami and new oil fields developed at exceptionally low oil prices, like North Star at under \$10/ per barrel. These field owners took on the full capital, operating, production and price risk associated with these fields. In some circumstances the economics of the fields could not have been justified at the low prices in existence at the time the investment was made.

Currently, at Prudhoe Bay, Kuparuk and other fields there are a known quantity of existing wells and existing production volumes. The vast majority of existing wells are continuously going down in volumes on a year over year basis. In order to stem a dramatic increase in overall production volumes at these legacy fields', new wells will be required in both light and heavy oil.

I believe, that to encourage new wells in legacy and other fields, there needs to be additional investments tax incentives particularly as it relates to heavy oil deposits that are contained in these fields.

The initial capital investment for heavy oil deposits is much more expensive than the light original crude that was discovered almost 40 years at Prudhoe Bay. If we want to tap heavy oil deposits, which are vast in number, we must recognize that the on going operating costs are higher than conventional oil and the production volumes are some times less than 10% of a conventional well. In other words, to encourage heavy oil development we all must recognize, capital costs are higher, operating costs are higher, and production volumes much smaller per well then what we are used to at the these legacy fields.

To encourage new investment and keep our production volumes at a level that will keep North Slope facilities and TAPS open for the next generation, we need clearly defined tax rules around new investment. We need to do everything possible to positively affect production volumes, as most of us know we can not control oil or natural gas prices in the long run.

I am personally asking each legislator to think about what is needed to stem the production decline. Please come up with a reasonable, understandable tax system that will encourage billions of dollars in new investment over the next 10 years. We also need to remember, that producer companies have expended over \$50 billion dollars in Alaska investment. They have paid around \$80 billion dollars in just State income tax.

I would like to see all of the existing producer companies continue to invest billions of dollars for new wells and existing fields, including heavy oil. We should all want to encourage any and all producers to bring more capital investment to Alaska.

In my opinion, the existing PPT structure would encourage needed new capital investment for both existing and new fields. However, I feel that additional strong targeted heavy oil investment tax credits are needed to stimulate this type of major research and development effort. How about we all work toward reducing the production decline by 2009?

My 15 year old son is currently a sophomore in high school and interested in technical trades. He wanted me to tell you all that he will need a job up here in the not to distant future.

Thanks for your consideration and all the hard work you are doing during this special session and being away from your friends and family.

Tom Maloney
3215 Legacy Drive
Anchorage, AK 99516

My understanding is that the oil industry paid over 5 billion dollars in tax and royalty payments for this fiscal year. At roughly a population base of 680 thousand Alaskans this would amount to a per capital tax payment of around 7,350 dollars.

The oil industry pays for roughly for 90% of our state government. Let's not go and change tax rules every year and chase them out of the state. I know my husband and I would not want to make up the tax differential .

Daphine Hatton
4993 East 6th Avenue
Anchorage, AK 99508