

ALASKA LEGISLATURE COMMITTEE FILES 2007-2008 RES 12693

1 Management Board is authorized by law, the department shall issue a cash refund to  
 2 the Alaska Retirement Management Board for a transferable tax credit originally  
 3 issued to a person under (d) of this section and purchased by the Alaska Retirement  
 4 Management Board. (f) An entity that is exempt from taxation under this chapter may  
 5 not apply for a transferable tax credit certificate. MLP

6 \* **Sec. 2930**, AS 43.55.025(a) is amended to read:

7 (a) Subject to the terms and conditions of this section, a credit against the  
 8 production tax **levied by** [DUE UNDER] AS 43.55.011(e) ~~or~~ **[OR (f)]** is allowed for  
 9 exploration expenditures that qualify under (b) of this section in an amount equal to  
 10 one of the following:

11 (1) ~~30~~ **[20]** percent of the total exploration expenditures that qualify  
 12 only under (b) and (c) of this section;

13 (2) ~~30~~ **[20]** ~~PERCENT~~ percent of the total exploration expenditures  
 14 [FOR WORK PERFORMED BEFORE JULY 1, 2007, AND] that qualify only under  
 15 (b) and (d) of this section;

16 (3) 40 percent of the total exploration expenditures that qualify under  
 17 (b), (c), and (d) of this section; or

18 (4) 40 percent of the total exploration expenditures that qualify only  
 19 under (b) and (e) of this section.

20 \* **Sec. 3031**, AS 43.55.025(b) is amended to read:

21 (b) To qualify for the production tax credit under (a) of this section, an  
 22 exploration expenditure must be incurred for work performed [ON OR] after  
 23 **December 31, 2006** ~~2007~~ [JULY 1, 2003], and before July 1, 2016, [EXCEPT THAT  
 24 AN EXPLORATION EXPENDITURE FOR A COOK INLET PROSPECT MUST  
 25 BE INCURRED FOR WORK PERFORMED ON OR AFTER JULY 1, 2005.] and

26 (1) may be for seismic or **other** geophysical exploration costs not  
 27 connected with a specific well;

28 (2) if for an exploration well,

29 (A) must be incurred by an explorer that holds an interest in  
 30 the exploration well for which the production tax credit is claimed;

31 (B) may be for either **a** [AN OIL OR GAS DISCOVERY]

1 well that encounters an oil or gas deposit or a dry hole; [AND]

2 (C) must be for a well that has been completed, suspended,  
 3 or abandoned under AS 31.05.030 at the time the explorer claims the tax  
 4 credit under (f) of this section; and

5 (D) must be for goods, services, or rentals of personal  
 6 property reasonably required for the surface preparation, drilling, casing,  
 7 cementing, and logging of an exploration well, and, in the case of a dry hole,  
 8 for the expenses required for abandonment if the well is abandoned within 18  
 9 months after the date the well was spudded;

10 (3) may not be for [TESTING, STIMULATION, OR COMPLETION  
 11 COSTS;] administration, supervision, engineering, or lease operating costs;  
 12 geological or management costs; community relations or environmental costs;  
 13 bonuses, taxes, or other payments to governments related to the well; costs, including  
 14 repairs and replacements, arising from or associated with fraud, wilful  
 15 misconduct, gross negligence, criminal negligence, or violation of law, including  
 16 a violation of 33 U.S.C. 1319(c)(1) health, safety, or environmental statutes or  
 17 1321(b)(3) (Clean Water Act), regulations; or other costs that are generally  
 18 recognized as indirect costs or financing costs; and

19 (4) may not be incurred for an exploration well or seismic exploration  
 20 that is included in a plan of exploration or a plan of development for any unit  
 21 ~~on~~ before May 14, 2003 [ON MAY 13, 2003].

22 \* ~~Sec. 31.32.~~ AS 43.55.025(c) is repealed and reenacted to read:

23 (c) To be eligible for the ~~30~~20 percent production tax credit authorized by  
 24 (a)(1) of this section or the 40 percent production tax credit authorized by (a)(3) of  
 25 this section, exploration expenditures must

26 (1) qualify under (b) of this section; and

27 (2) be for an exploration well, subject to the following:

28 (A) before spudding the well.

29 (i) the explorer shall submit to the commissioner of  
 30 natural resources the information necessary to determine whether the  
 31 geological objective of the well is a potential oil or gas trap that is

1 distinctly separate from any trap that has been tested by a preexisting  
2 well; and

3 (ii) ~~at the time of the request for a determination under~~  
4 ~~(i), the commissioner of natural resources may request from the~~  
5 ~~explorer that specific data sets, ancillary data, and reports including all~~  
6 ~~results, and copies of data collected and data analyses for the well be~~  
7 ~~provided to the Department of Natural Resources upon completion of~~  
8 ~~the well; in this subparagraph, well data includes all analyses~~  
9 ~~conducted on physical material, and well logs collected from the well~~  
10 ~~and sample analyses; testing geophysical and velocity data including~~  
11 ~~vertical seismic profiles and check shot surveys; testing data and~~  
12 ~~analyses; age data; geochemical analyses; and access to tangible~~  
13 ~~material; and~~

14 (iii) ~~the commissioner of natural resources must make~~  
15 ~~an affirmative determination on whether the geological objective of~~  
16 ~~the well is a potential oil or gas trap that is distinctly separate from any~~  
17 ~~trap that has been tested by a preexisting well and what information~~  
18 ~~under (ii) must be submitted after completion, abandonment, or~~  
19 ~~suspension under AS 31.05.030~~question: the commissioner of natural  
20 resources shall decide whether to make that determination within 60  
21 days after receiving all the necessary information from the explorer  
22 and based on the information received and on other information the  
23 commissioner of natural resources may consider relevant;

24 (B) for an exploration well other than a well to explore a Cook  
25 Inlet prospect, the well must be located and drilled in such a manner that the  
26 bottom hole is located not less than three miles away from the bottom hole of  
27 a preexisting well drilled for oil or gas, irrespective of whether the preexisting  
28 well has been completed, suspended, or abandoned;

29 (C) after completion, suspension, or abandonment ~~or~~  
30 ~~suspension under AS 31.05.030~~ of the exploration well, the commissioner of  
31 natural resources must determine that the well was ~~consistent with~~

1           ~~achieving~~adequately achieved the explorer's stated geological objective.

2   \* ~~Sec. 32.33.~~ AS 43.55.025(f) is amended to read:

3           (f) For a production tax credit under this section,

4                   (1) an explorer shall, in a form prescribed by the department and,  
5           except for a credit under (f) of this section, within six months of the completion of  
6           the exploration activity, claim the credit and submit information sufficient to  
7           demonstrate to the department's satisfaction that the claimed exploration expenditures  
8           qualify under this section: ~~in addition, the explorer shall submit information~~  
9           ~~necessary for the commissioner of natural resources to evaluate the validity of~~  
10           ~~the explorer's compliance with the requirements of this section;~~

11                   (2) an explorer shall agree, in writing,

12                           (A) to notify the Department of Natural Resources, within 30  
13           days after completion of seismic or geophysical data processing, completion  
14           of [A] well drilling, or filing of a claim for credit, whichever is the latest, for  
15           which exploration costs are claimed, of the date of completion and submit a  
16           report to that department describing the processing sequence and providing a  
17           list of data sets available: [IF, UNDER (c)(2)(B) OF THIS SECTION, AN  
18           EXPLORER SUBMITS A CLAIM FOR A CREDIT FOR EXPENDITURES  
19           FOR AN EXPLORATION WELL THAT IS LOCATED WITHIN THREE  
20           MILES OF A WELL ALREADY DRILLED FOR OIL AND GAS, IN  
21           ADDITION TO THE SUBMISSIONS REQUIRED UNDER (1) OF THIS  
22           SUBSECTION, THE EXPLORER SHALL SUBMIT THE INFORMATION  
23           NECESSARY FOR THE COMMISSIONER OF NATURAL RESOURCES  
24           TO EVALUATE THE VALIDITY OF THE EXPLORER'S CLAIM THAT  
25           THE WELL IS DIRECTED AT A DISTINCTLY SEPARATE  
26           EXPLORATION TARGET, AND THE COMMISSIONER OF NATURAL  
27           RESOURCES SHALL, UPON RECEIPT OF ALL EVIDENCE  
28           SUFFICIENT FOR THE COMMISSIONER TO EVALUATE THE  
29           EXPLORER'S CLAIM, MAKE THAT DETERMINATION WITHIN 60  
30           DAYS:]

31                           (B) to provide to the Department of Natural Resources, within

1 30 days after the date of a request, unless a longer period is provided by the  
 2 Department of Natural Resources, specific data sets, ancillary data, and  
 3 reports identified in (A) of this paragraph; in this subparagraph.

4 (i) a seismic or geophysical data set includes the  
 5 data for an entire seismic survey, irrespective of whether the  
 6 survey areas cover area covers nonstate land in addition to state  
 7 land or land in a unit in addition to land outside a unit;

8 (ii) well data include all derivative products, results,  
 9 and copies of data collected and data analyses for the well, well  
 10 logs; sample analyses; geophysical and velocity data including  
 11 vertical seismic profiles and check shot surveys; and tangible  
 12 material including, for each whole core collected, a lengthwise cut  
 13 slab that is at least 1/3 of the whole core volume, and  
 14 representative samples, as specified by the Department of Natural  
 15 Resources, of other gaseous, liquid, or solid material collected  
 16 from drilling or testing the well;

17 (C) that, notwithstanding any provision of AS 38, information  
 18 provided under this paragraph will be held confidential by the Department of  
 19 Natural Resources

20 (i) in the case of well data, until the expiration of the  
 21 24-month period of confidentiality described in AS 31.05.035(c),  
 22 without extension, after which the Department of Natural  
 23 Resources [FOR 10 YEARS FOLLOWING THE COMPLETION  
 24 DATE], at which time the Department of Natural Resources [, AT  
 25 WHICH TIME THAT DEPARTMENT] will release the information  
 26 after 30 days' public notice unless, in the discretion of the  
 27 commissioner of natural resources, it is necessary to  
 28 protect/withhold the well data in order to avoid disclosing  
 29 information relating to the valuation of unleased acreage in the  
 30 same vicinity, or unless the well is on private land and the owner,  
 31 including the lessor but not the lessee, of the oil and gas resources

1 has not given permission to release the well data;

2 (ii) in the case of seismic or other geophysical data,  
3 other than seismic data acquired by seismic exploration subject to  
4 (f) of this section, for 10 years following the completion date, at  
5 which time the Department of Natural Resources will release the  
6 information after 30 days' public notice, except as to seismic or  
7 other geophysical data acquired from private land, unless the  
8 owner, including a lessor but not a lessee, of the oil and gas  
9 resources in the private land gives permission to release the  
10 seismic or other geophysical data associated with the private land;

11 (iii) in the case of seismic data obtained by seismic  
12 exploration subject to (f) of this section, only until the expiration of  
13 30 days' public notice issued on or after the date the production  
14 tax credit certificate is issued under (5) of this subsection;

15 (3) if more than one explorer holds an interest in a well or seismic  
16 exploration, each explorer may claim an amount of credit that is proportional to the  
17 explorer's cost incurred;

18 (4) the department may exercise the full extent of its powers as though  
19 the explorer were a taxpayer under this title, in order to verify that the claimed  
20 expenditures are qualified exploration expenditures under this section; and

21 (5) if the department is satisfied that the explorer's claimed  
22 expenditures are qualified under this section and that all data required to be  
23 submitted under this section have been submitted, the department shall issue to the  
24 explorer a production tax credit certificate for the amount of credit to be allowed  
25 against production taxes levied by AS 43.55.011(e) or (f); the credit is available for  
26 immediate use; notwithstanding any contrary provision of AS 38, AS 40.25.100,  
27 or AS 43.05.230, the following information is not confidential:

28 (A) the explorer's name;

29 (B) the date of the application;

30 (C) the location of the well or seismic exploration;

31 (D) the date of the department's issuance of the certificate;

1 and

2 (E) the date on which the information required to be  
3 submitted under this section will be released [DUE UNDER  
4 AS 43.55.011(e) OR (f)].

5 \* Sec. 33.34. AS 43.55.025(g) is amended to read:

6 (g) An explorer, other than an entity that is exempt from taxation under  
7 this chapter, may transfer, convey, or sell its production tax credit certificate to any  
8 person, and any person who receives a production tax credit certificate may also  
9 transfer, convey, or sell the certificate.

10 \* Sec. 35. AS 43.55.025(h) is amended to read:

11 (h) A producer that purchases a production tax credit certificate may apply  
12 the credits against its production tax levied by [LIABILITY UNDER]  
13 AS 43.55.011(e) [OR (f)]. Regardless of the price the producer paid for the  
14 certificate, the producer may receive a credit against its production tax liability for the  
15 full amount of the credit, but for not more than the amount for which the certificate is  
16 issued. A production tax credit allowed under this section may not be applied more  
17 than once.

18 \* Sec. 36. AS 43.55.025(i) is repealed and reenacted to read:

19 (i) For a production tax credit under this section,

20 (1) a credit may not be applied to reduce a taxpayer's tax liability  
21 under AS 43.55.011(e) ~~or (f)~~ below zero for a calendar year; and

22 (2) an amount of the production tax credit in excess of the amount that  
23 may be applied for a calendar year under this subsection may be carried forward and  
24 applied against the taxpayer's tax liability under AS 43.55.011(e) ~~or (f)~~ in one or more  
25 later calendar years.

26 \* Sec. 34.37. AS 43.55.025(k) is amended by adding a new paragraph to read:

27 (4) "preexisting well" means a well that was spudded more than 540  
28 days but less than 35 years before the date on which the exploration well to which it  
29 is compared is spudded.

30 \* Sec. 35.38. AS 43.55.025 is amended by adding a new ~~subsection~~ subsection to read:

31 (l) Subject to the terms and conditions of this section, if a claim is filed under

1 (f)(1) of this section before January 1, 2016, a credit against the production tax levied  
 2 by AS 43.55.011(e) ~~or (f)~~ is allowed in an amount equal to five percent of an eligible  
 3 expenditure under this subsection incurred for seismic exploration performed before  
 4 July 1, 2003. To be eligible under this subsection, an expenditure must

5 (1) have been for seismic exploration that

6 (A) obtained data that the commissioner of natural resources  
 7 considers to be in the best interest of the state to acquire for public  
 8 distribution; and

9 (B) was conducted outside the boundaries of a production unit;  
 10 however, the amount of the expenditure that is otherwise eligible under this  
 11 section is reduced proportionately by the portion of the seismic exploration  
 12 activity that crossed into a production unit; and

13 (2) qualify under (b)(3) of this section.

14 ~~(m) Subject to appropriations made by law, if and to the extent that purchase~~  
 15 ~~of transferable tax credits by the Alaska Retirement Management Board is authorized~~  
 16 ~~by law, the department shall issue a cash refund to the Alaska Retirement~~  
 17 ~~Management Board for a transferable tax credit originally issued to an explorer under~~  
 18 ~~(f) of this section and purchased by the Alaska Retirement Management Board.~~

19 \* ~~Sec. 36.39.~~ AS 43.55.030(a) is amended to read:

20 (a) A producer that produces oil or gas from a lease or property in the  
 21 state during a calendar year, whether or not any tax payment is due under  
 22 AS 43.55.020(a) for that oil or gas, [THE PERSON PAYING THE TAX] shall file  
 23 with the department on March 31 of the following year [FOLLOWING THE  
 24 CALENDAR YEAR FOR WHICH THE TAX WAS LEVIED] a statement, under  
 25 oath, in a form prescribed by the department, giving, with other information required,  
 26 the following:

27 (1) a description of each lease or property from which [THE] oil or  
 28 [AND] gas was [WERE] produced, by name, legal description, lease number, or  
 29 accounting codes assigned by the department;

30 (2) the names of the producer and, if different, the person paying the  
 31 tax, if any:

1 (3) the gross amount of oil and the gross amount of gas produced from  
2 each lease or property, and the percentage of the gross amount of oil and gas owned  
3 by the [EACH] producer [FOR WHOM THE TAX IS PAID];

4 (4) the gross value at the point of production of the oil and of the gas  
5 produced from each lease or property owned by the [EACH] producer and the costs  
6 of transportation of the oil and gas [FOR WHOM THE TAX IS PAID];

7 (5) the name of the first purchaser and the price received for the oil  
8 and for the gas, unless relieved from this requirement in whole or in part by the  
9 department; [AND]

10 (6) the producer's qualified capital expenditures, as defined in  
11 AS 43.55.023, other lease expenditures [AND ADJUSTMENTS AS  
12 CALCULATED] under AS 43.55.165, and adjustments or other payments or  
13 credits under AS 43.55.170;

14 (7) the production tax values of the oil and gas under  
15 AS 43.55.160;

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

17 (9) calculations showing the amounts, if any, that were or are due  
18 under AS 43.55.020(a) and interest on any underpayment or overpayment  
19 [AS 43.55.160 - 43.55.170].

20 \* ~~Sec. 37.40~~, AS 43.55.030(d) is amended to read:

21 (d) Reports required under this section [BY OR ON BEHALF OF THE  
22 PRODUCER] are delinquent the first day following the day the report is due. The  
23 person required to file the report is liable for a penalty, as determined by the  
24 department under standards adopted in regulation by the department, of not  
25 more than \$1,000 for each day the person fails to file the report at the time  
26 required. The penalty is in addition to the penalties in AS 43.05.220 and  
27 43.05.290 and is assessed, collected, and paid in the same manner as a tax  
28 deficiency under this title. In this subsection, "report" includes a statement.

29 \* ~~Sec. 38.41~~, AS 43.55.030 is amended by adding new subsections to read:

30 (e) An explorer or producer that incurs a lease expenditure under  
31 AS 43.55.165 or receives a payment or credit under AS 43.55.170 during a calendar

1 year but does not produce oil or gas from a lease or property in the state during the  
2 calendar year shall file with the department on March 31 of the following year a  
3 statement, under oath, in a form prescribed by the department, giving, with other  
4 information required, the following:

5 (1) the producer's qualified capital expenditures, as defined in  
6 AS 43.55.023, other lease expenditures under AS 43.55.165, and adjustments or other  
7 payments or credits under AS 43.55.170; and

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

11 (f) The department may require a producer, an explorer, or an operator of a  
12 lease or property to file monthly reports, as applicable, of

13 (1) the amounts and gross value at the point of production of oil and  
14 gas produced;

15 (2) transportation costs of the oil and gas;

16 (3) any unscheduled interruption of, or reduction in the rate of, oil or  
17 gas production;

18 (4) lease expenditures and adjustments under AS 43.55.165 and  
19 43.55.170;

20 (5) joint interest billings;

21 (6) contracts for the sale or transportation of oil or gas;

22 (7) information and calculations used in determining monthly  
23 installment payments of estimated tax under AS 43.55.020(a); and

24 (8) other records and information the department considers necessary  
25 for the administration of this chapter.

26 \* ~~Sec. 39.42.~~ AS 43.55.040 is amended to read:

27 **Sec. 43.55.040. Powers of Department of Revenue.** Except as provided in  
28 AS 43.05.405 - 43.05.499, the department may

29 (1) require a person engaged in production and the agent or employee  
30 of the person, and the purchaser of oil or gas, or the owner of a royalty interest in oil  
31 or gas to furnish, whether by the filing of regular statements or reports or otherwise,

1 additional information that is considered by the department as necessary to compute  
2 the amount of the tax; notwithstanding any contrary provision of law, the disclosure  
3 of additional information under this paragraph to the producer obligated to pay the tax  
4 does not violate AS 40.25.100(a) or AS 43.05.230(a); before disclosing information  
5 under this paragraph that is otherwise required to be held confidential under  
6 AS 40.25.100(a) or AS 43.05.230(a), the department shall

7 (A) provide the person that furnished the information a  
8 reasonable opportunity to be heard regarding the proposed disclosure and the  
9 conditions to be imposed under (B) of this paragraph: and

10 (B) impose appropriate conditions limiting

11 (i) access to the information to those legal counsel,  
12 consultants, employees, officers, and agents of the producer who have  
13 a need to know that information for the purpose of determining or  
14 contesting the producer's tax obligation; and

15 (ii) the use of the information to use for that purpose:

16 (2) examine the books, records, and files of the [SUCH A] person;

17 (3) conduct hearings and compel the attendance of witnesses and the  
18 production of books, records, and papers of any person; [AND]

19 (4) make an investigation or hold an inquiry that is considered  
20 necessary to a disclosure of the facts as to

21 (A) the amount of production from any oil or gas location, or  
22 of a company or other producer of oil or gas; and

23 (B) the rendition of the oil and gas for taxing purposes;

24 **(5) require a producer, an explorer, or an operator of a lease or**  
25 **property to file reports and copies of records that the department considers**  
26 **necessary to forecast state revenue under this chapter; in the case of reports and**  
27 **copies of records relating to proposed, expected, or approved unit expenditures**  
28 **for a unit for which one or more working interest owners other than the**  
29 **operator have authority to approve unit expenditures, the required reports and**  
30 **copies of records are limited to those reports or copies of records that constitute**  
31 **or disclose communications between the operator and the working interest**

1 owners relating to unit budget matters; and

2 (6) require a producer that has an average total production in the  
 3 state of more than 100,000 barrels a day for a calendar year to report the gross  
 4 value at the point of production of the producer's taxable oil and gas in the state  
 5 for a calendar year and the total amount of lease expenditures in the state for  
 6 that calendar year; and

7 (7) assess against a person required under this section to file a  
 8 report, statement, or other document a penalty, as determined by the  
 9 department under standards adopted in regulation by the department, of not  
 10 more than \$1,000 for each day the person fails to file the report, statement, or  
 11 other document after notice by the department; the penalty is in addition to any  
 12 penalties under AS 43.05.220 and 43.05.290 and is assessed, collected, and paid  
 13 in the same manner as a tax deficiency under this title; the penalty shall bear  
 14 interest at the rate specified under AS 43.05.225(1).

15 \* Sec. 40.43. AS 43.55 is amended by adding a new section to read:

16 Sec. 43.55.055. Penalty for understatement of tax. (a) In addition to other  
 17 penalties prescribed by law, if there is a substantial understatement of tax required to  
 18 be shown on a statement required under AS 43.55.030(a), there shall be added to the  
 19 tax an amount equal to 10 percent of the substantial understatement of tax.

20 (b) In addition to other penalties prescribed by law, if there is a gross  
 21 understatement of tax required to be shown on a statement required under  
 22 AS 43.55.030(a), there shall be added to the tax an amount equal to 20 percent of the  
 23 gross understatement of tax.

24 (c) In addition to the penalties imposed under (a) or (b) of this section, a  
 25 person who has made a substantial or gross understatement of tax is liable to the state  
 26 for the reasonable costs of the state's enforcement action, including auditing costs.

27 (d) For purposes of this section,

28 (1) a substantial understatement of tax for any calendar year exists if  
 29 the amount of the understatement for the calendar year exceeds the lesser of 10  
 30 percent of the tax required to be shown on the statement for the calendar year or  
 31 \$10,000,000;

1                   ~~(2) a gross understatement of tax for any calendar year exists if the~~  
2                   ~~amount of the understatement for the calendar year exceeds the lesser of 20 percent of~~  
3                   ~~the tax required to be shown on the statement for the calendar year or \$20,000,000;~~

4                   ~~(3) "understatement" means the amount by which the tax required to~~  
5                   ~~be shown on the statement for the calendar year exceeds the amount of the tax~~  
6                   ~~reported as due by the taxpayer as shown on the statement.~~

7                   \* ~~Sec. 41. AS 43.55~~ is amended by adding new sections to read:

8                   **Sec. 43.55.075. Limitation on assessment and amended returns.** (a) Except  
9                   as provided in AS 43.05.260(c), the amount of a tax imposed by this chapter must be  
10                  assessed within ~~six~~four years after the latest return was filed.

11                  (b) A decision of a regulatory agency, court, or other body with authority to  
12                  resolve disputes that results in a retroactive change to a lease expenditure, to an  
13                  adjustment to a lease expenditure, to costs of transportation, to sale price, to  
14                  prevailing value, or to consideration of quality differentials relating to the  
15                  commingling of oils has a corresponding effect, either an increase or decrease, as  
16                  applicable, on the production tax value of oil or gas or the amount or availability of a  
17                  tax credit as determined under this chapter. For purposes of this section, a change to a  
18                  lease expenditure includes a change in the categorization of a lease expenditure as a  
19                  qualified capital expenditure or as not a qualified capital expenditure. The producer  
20                  shall

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

22                  and

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

27                  (c) If an alteration in or modification of a producer's federal income tax return  
28                  or a recomputation of the producer's federal income tax or determination of  
29                  deficiency occurs that affects the amount of a tax imposed on the producer under this  
30                  chapter, the producer shall

31                         (1) within 60 days after the final determination of the alteration,

1 modification, recomputation, or deficiency, notify the department in writing; and  
2 (2) within 120 days after the final determination of the alteration,  
3 modification, recomputation, or deficiency, file amended returns covering all affected  
4 periods.

5 (d) In this section.

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

8 (2) "return" includes a report, a statement, and an amended return,  
9 report, or statement.

10 ~~\* Sec. 43.55.078. Exceptions to tax credits. (a) For a calendar year after~~  
11 ~~2007, a producer or explorer may not take a tax credit under AS 43.55.023,~~  
12 ~~43.55.024, or 43.55.025 against a tax levied under this chapter if a state court or~~  
13 ~~administrative agency or federal court that has subject matter jurisdiction has entered~~  
14 ~~a judgment in favor of the state or a political subdivision of the state in an amount~~  
15 ~~greater than \$100,000 against the producer or explorer, the producer or explorer has~~  
16 ~~not satisfied the judgment, and the judgment concerns a matter having connections~~  
17 ~~with this state that are sufficient to satisfy constitutional jurisdictional requirements.~~

18 (b) Notwithstanding (a) of this section, the producer or explorer may receive  
19 a tax credit described in (a) of this section if

20 (1) the judgment is appealed but the appeal has not been decided; and

21 (2) the producer or explorer deposits in the court where the judgment  
22 was entered or the appeal is pending, in the form of cash, bond, or other security,

23 (A) the full amount of the judgment; and

24 (B) post-judgment interest on the judgment amount described  
25 in (A) of this paragraph; notwithstanding another provision of law, the post-  
26 judgment interest rate compounded quarterly on a judgment the amount of  
27 which is deposited under (a) of this paragraph is equal to the greater of

28 (i) the applicable statutory rate; or

29 (ii) the rate of return on the producer's or explorer's  
30 equity as shown on the producer's or explorer's most recent quarterly  
31 earnings report as of the date of the notice of appeal.

1 ~~(e) In this section:~~

2 ~~(1) "judgment" means any final administrative determination or~~  
3 ~~judgment in favor of the state or a political subdivision of the state;~~

4 ~~(2) "producer or explorer" includes an affiliate of a producer or~~  
5 ~~explorer.~~

6 ~~\* Sec. 42.44.~~ AS 43.55.110 is amended by adding new subsections to read:

7 (e) The department may require that returns, statements, reports, notifications,  
8 and applications filed under this chapter be filed electronically in a form and manner  
9 approved or prescribed by the department.

10 (f) The department may require that payments required under this chapter be  
11 made electronically in a form and manner approved or prescribed by the department.

12 (g) Notwithstanding AS 44.62, the department may issue, for the information  
13 and guidance of producers, explorers, and other interested persons, advisory bulletins  
14 stating the department's interpretation of provisions of this chapter and of regulations  
15 adopted under this chapter. Unless otherwise provided by the department by  
16 regulation, interpretations stated in the advisory bulletins are not binding on the  
17 department or others.

18 (h) Subject to legislative appropriation, the department may compensate a  
19 person who provides information to the department about noncompliance with the  
20 provisions of this chapter by an explorer or a producer of oil or gas if that information  
21 leads to the collection of additional taxes, penalties, or interest from the producer.  
22 The amount of compensation under this subsection may not exceed the lesser of  
23 \$~~400,000~~500,000 or 10 percent of the additional tax, penalty, or interest collected as a  
24 result of the information. A state employee or an agent of the state is not eligible for  
25 compensation under this subsection.

26 ~~(i) A person who, under ( ) of this section, provides, in~~  
27 ~~bad faith, to the department erroneous information about~~  
28 ~~noncompliance with the provisions of this chapter by an explorer or~~  
29 ~~producer of oil or gas shall pay to the~~  
30 ~~( ) department all expenses related to the department's investigation~~  
31 ~~of the alleged noncompliance; and~~

1                   ~~(2) explorer or producer about whom the noncompliance was alleged~~  
2                   ~~all expenses that are incurred by the explorer or producer relating to the department's~~  
3                   ~~investigation of the alleged noncompliance.~~

4 \* **Sec. 43.45.** AS 43.55.150 is amended to read:

5                   **Sec. 43.55.150. Determination of gross value at the point of production.**

6                   (a) For the purposes of AS 43.55.011 - 43.55.180, the gross value at the point of  
7                   production is calculated using the actual [REASONABLE] costs of transportation of  
8                   the oil or gas [ ~~THE REASONABLE COSTS OF TRANSPORTATION ARE THE~~  
9                   ~~ACTUAL COSTS~~], except when the

10                   (1) shipper [PARTIES TO THE TRANSPORTATION] of oil or gas  
11                   is [ARE] affiliated with the transportation carrier or with a person that owns an  
12                   interest in the transportation facility:

13                   (2) contract for the transportation of oil or gas is not an arm's length  
14                   transaction [OR IS NOT REPRESENTATIVE OF THE MARKET VALUE OF  
15                   THAT TRANSPORTATION]; or [AND]

16                   (3) method or terms of transportation of oil or gas are [IS] not  
17                   reasonable in view of existing alternative [METHODS OF] transportation options.

18                   (b) If the department finds that a condition [THE CONDITIONS] in (a)(1),  
19                   (2), or [AND] (3) of this section is [ARE] present, the gross value at the point of  
20                   production is calculated using the actual costs of transportation, or the  
21                   reasonable costs of transportation as determined under this subsection,  
22                   whichever is lower. The [THE] department shall determine the reasonable costs of  
23                   transportation, using the fair market value of like transportation, the fair market value  
24                   of equally efficient and available alternative modes of transportation, or other  
25                   reasonable methods. Transportation costs fixed by tariff rates that have been  
26                   adjudicated as just and reasonable by [PROPERLY ON FILE WITH] the  
27                   Regulatory Commission of Alaska or another [OTHER] regulatory agency and  
28                   transportation costs in an arm's length transaction paid by parties not affiliated  
29                   with an owner of the method of transportation shall be considered prima facie  
30                   reasonable.

31                   (c) In determining the gross value of oil under [(a) OF] this section, the

1 department may not allow as reasonable costs of transportation

2 (1) the amount of loss of or damage to, or of expense incurred due to  
3 the loss of or damage to, a vessel used to transport oil if the loss, damage, or expense  
4 is incurred in connection with a catastrophic oil discharge from the vessel into the  
5 marine or inland waters of the state;

6 (2) the incremental costs of transportation of the oil that are  
7 attributable to temporary use of or chartered or substituted service provided by  
8 another vessel due to the loss of or damage to a vessel regularly used to transport oil  
9 and that are incurred in connection with a catastrophic oil discharge into the marine or  
10 inland waters of the state; and

11 (3) the costs incurred to charter, contract, or hire vessels and  
12 equipment used to contain or clean up a catastrophic oil discharge.

13 \* ~~Sec. 44.46.~~ AS 43.55.160(a) is amended to read:

14 (a) Except as provided in (b) of this section, for the purposes of

15 [(1)] AS 43.55.011(e), the ~~{ANNUAL}~~ annual production tax value of  
16 the taxable

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

25 (2) [(B)] oil and gas produced during a calendar year from leases or  
26 properties in the state outside the Cook Inlet sedimentary basin, no part of which is  
27 north of 68 degrees North latitude, is the gross value at the point of production of the  
28 oil and gas taxable under AS 43.55.011(e) and produced by the producer from those  
29 leases or properties, less the producer's lease expenditures under AS 43.55.165 for the  
30 calendar year applicable to the oil and gas produced by the producer from those leases  
31 or properties, as adjusted under AS 43.55.170; ~~this subparagraph does not apply to~~

1 ~~gas subject to AS 43.55.011(o):~~

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

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

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

21 (2) AS 43.55.011(g). THE MONTHLY PRODUCTION TAX  
22 VALUE OF THE TAXABLE

23 (A) OIL AND GAS PRODUCED DURING A MONTH  
24 FROM LEASES OR PROPERTIES IN THE STATE THAT INCLUDE  
25 LAND NORTH OF 68 DEGREES NORTH LATITUDE IS THE GROSS  
26 VALUE AT THE POINT OF PRODUCTION OF THE OIL AND GAS  
27 TAXABLE UNDER AS 43.55.011(g) AND PRODUCED BY THE  
28 PRODUCER FROM THOSE LEASES OR PROPERTIES, LESS 1/12 OF  
29 THE PRODUCER'S LEASE EXPENDITURES UNDER AS 43.55.165 FOR  
30 THE CALENDAR YEAR APPLICABLE TO THE OIL AND GAS  
31 PRODUCED BY THE PRODUCER FROM THOSE LEASES OR

1 PROPERTIES, AS ADJUSTED UNDER AS 43.55.170;

2 (B) OIL AND GAS PRODUCED DURING A MONTH  
3 FROM LEASES OR PROPERTIES IN THE STATE OUTSIDE THE COOK  
4 INLET SEDIMENTARY BASIN, NO PART OF WHICH IS NORTH OF 68  
5 DEGREES NORTH LATITUDE, IS THE GROSS VALUE AT THE POINT  
6 OF PRODUCTION OF THE OIL AND GAS TAXABLE UNDER  
7 AS 43.55.011(g) AND PRODUCED BY THE PRODUCER FROM THOSE  
8 LEASES OR PROPERTIES, LESS 1/12 OF THE PRODUCER'S LEASE  
9 EXPENDITURES UNDER AS 43.55.165 FOR THE CALENDAR YEAR  
10 APPLICABLE TO THE OIL AND GAS PRODUCED BY THE PRODUCER  
11 FROM THOSE LEASES OR PROPERTIES, AS ADJUSTED UNDER  
12 AS 43.55.170;

13 (C) OIL PRODUCED DURING A MONTH FROM A  
14 LEASE OR PROPERTY IN THE COOK INLET SEDIMENTARY BASIN  
15 IS THE GROSS VALUE AT THE POINT OF PRODUCTION OF THE OIL  
16 TAXABLE UNDER AS 43.55.011(g) AND PRODUCED BY THE  
17 PRODUCER FROM THAT LEASE OR PROPERTY, LESS 1/12 OF THE  
18 PRODUCER'S LEASE EXPENDITURES UNDER AS 43.55.165 FOR THE  
19 CALENDAR YEAR APPLICABLE TO THE OIL PRODUCED BY THE  
20 PRODUCER FROM THAT LEASE OR PROPERTY, AS ADJUSTED  
21 UNDER AS 43.55.170;

22 (D) GAS PRODUCED DURING A MONTH FROM A  
23 LEASE OR PROPERTY IN THE COOK INLET SEDIMENTARY BASIN  
24 IS THE GROSS VALUE AT THE POINT OF PRODUCTION OF THE GAS  
25 TAXABLE UNDER AS 43.55.011(g) AND PRODUCED BY THE  
26 PRODUCER FROM THAT LEASE OR PROPERTY, LESS 1/12 OF THE  
27 PRODUCER'S LEASE EXPENDITURES UNDER AS 43.55.165 FOR THE  
28 CALENDAR YEAR APPLICABLE TO THE GAS PRODUCED BY THE  
29 PRODUCER FROM THAT LEASE OR PROPERTY, AS ADJUSTED  
30 UNDER AS 43.55.170].

31 \* ~~Sec. 45.47.~~ AS 43.55.160(b) is amended to read:

1           (b) A production tax value calculated under [(a) OF] this section may not be  
2           less than zero.

3       \* Sec. 48. AS 43.55.160(e) is amended to read:

4           (e) Any adjusted lease expenditures under AS 43.55.165 and 43.55.170 that  
5           would otherwise be deductible by a producer in a calendar year but whose deduction  
6           would cause a a [AN ANNUAL] production tax value calculated under (a) [(a)(1)] of  
7           this section of taxable oil or gas produced during the calendar year to be less than  
8           zero may be used to establish a carried-forward annual loss under AS 43.55.023(b).  
9           However, the department shall provide by regulation a method to ensure that,  
10          for a period for which a producer's tax liability is limited by AS 43.55.011(i) or  
11          (k), any adjusted lease expenditures under AS 43.55.165 and 43.55.170 that  
12          would otherwise be deductible by a producer for that period but whose  
13          deduction would cause a production tax value calculated under (a)(3) or (4) of  
14          this section to be less than zero are accounted for as though the adjusted lease  
15          expenditures had first been used as deductions in calculating the production tax  
16          values of oil or gas subject to any of the limitations under AS 43.55.011(i) or (k)  
17          that have positive production tax values so as to reduce the tax liability  
18          calculated without regard to the limitation to the maximum amount provided for  
19          under the applicable provision of AS 43.55.011(i) or (k). Only the amount of  
20          those adjusted lease expenditures remaining after the accounting provided for  
21          under this subsection may be used to establish a carried-forward annual loss  
22          under AS 43.55.023(b). In this subsection, "producer" includes "explorer."

23       \* Sec. 46.49. AS 43.55.165(a) is repealed and reenacted to read:

24           (a) Except as provided in ~~(k) and (h)~~ of this section for For purposes of this  
25           chapter, a producer's lease expenditures for a calendar year are

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

27                           (A) incurred ~~in the state~~ by the producer during the calendar  
28                           year after March 31, 2006, to explore for, develop, or produce oil or gas  
29                           deposits located within the producer's leases or properties in the state or, in the  
30                           case of land in which the producer does not own an operating right, operating  
31                           interest, or working interest, to explore for oil or gas deposits within other

1 land in the state; and

2 (B) allowed by the department by regulation, based on the  
3 department's determination that the costs satisfy the following three  
4 requirements:

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

7 (ii) the costs must be ordinary and necessary costs of  
8 exploring for, developing, or producing, as applicable, oil or gas  
9 deposits; and

10 (iii) the costs must be direct costs of exploring for,  
11 developing, or producing, as applicable, oil or gas deposits; and

12 (2) a reasonable allowance for that calendar year, as determined under  
13 regulations adopted by the department, for overhead expenses that are directly related  
14 to exploring for, developing, or producing, as applicable, the oil or gas deposits.

15 \* Sec. 47.50. AS 43.55.165(b) is amended to read:

16 (b) For purposes of (a) of this section,

17 (1) direct costs include

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

22 (B) payments of or in lieu of property taxes, sales and use  
23 taxes, motor fuel taxes, and excise taxes;

24 [(C) A REASONABLE ALLOWANCE, AS DETERMINED  
25 UNDER REGULATIONS ADOPTED BY THE DEPARTMENT, FOR  
26 OVERHEAD EXPENSES DIRECTLY RELATED TO EXPLORING FOR,  
27 DEVELOPING, AND PRODUCING OIL OR GAS DEPOSITS LOCATED  
28 WITHIN LEASES OR PROPERTIES OR OTHER LAND IN THE STATE;]

29 (2) an activity does not need to be physically located on, near, or  
30 within the premises of the lease or property within which an oil or gas deposit being  
31 explored for, developed, or produced is located in order for the cost of the activity to

1 be a cost upstream of the point of production of the oil or gas;

2 (3) in determining whether costs are lease expenditures, the  
3 department may shall consider, among other factors, the

4 (A) typical industry practices and standards in the state  
5 that determine the costs, other than items listed in (e) of this section, that  
6 an operator is allowed to bill a producer that is not the operator, under  
7 unit operating agreements or similar operating agreements that were in  
8 effect before December 2, 2005, and were subject to negotiation with at  
9 least one producer with substantial bargaining power, other than the  
10 operator; and

11 (B) standards adopted by the Department of Natural  
12 Resources that determine the costs, other than items listed in (e) of this  
13 section, that a lessee is allowed to deduct from revenue in calculating net  
14 profits under a lease issued under AS 38.05.180(f)(3)(B), (D), or (E).

15 \* Sec. 48.51. AS 43.55.165(c) is repealed and reenacted to read:

16 (c) Subject to (g) and (h) of this section, if the department finds that the  
17 pertinent provisions of a unit operating agreement or similar operating agreement are  
18 substantially consistent with the department's determinations and standards under (a)  
19 and (b) of this section concerning whether costs are lease expenditures and, in  
20 addition, finds that at least one working interest owner party to the agreement, other  
21 than the operator, with substantial incentive and ability to effectively audit billings  
22 under the agreement, in fact is effectively auditing billings under the agreement, the  
23 department may authorize or require a producer, subject to conditions prescribed  
24 under regulations adopted by the department, to treat as that portion of its lease  
25 expenditures for a calendar year applicable to oil and gas produced from a lease or  
26 property in the state only

27 (1) the costs, other than items listed in (e) of this section, that are  
28 incurred by the operator during the calendar year and that

29 (A) are billed to the producer by the operator under the  
30 agreement to which that lease or property is subject and are either not disputed  
31 by a working interest owner party to the agreement or are finally determined

1 to be properly billable as a result of dispute resolution; or

2 (B) for a producer that is the operator, would be billable to the  
 3 producer by the operator in accordance with the terms of the agreement to  
 4 which that lease or property is subject if the producer were not the operator;  
 5 and

6 (2) a reasonable percentage, as determined under regulations adopted  
 7 by the department, of the costs that are billed under (1) of this subsection as an  
 8 allowance for overhead expenses directly related to exploring for, developing, and  
 9 producing oil or gas deposits located within the lease or property.

10 \* Sec. 52. AS 43.55.165(e) is amended to read:

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

12 (1) depreciation, depletion, or amortization;

13 (2) oil or gas royalty payments, production payments, lease profit  
 14 shares, or other payments or distributions of a share of oil or gas production, profit, or  
 15 revenue, except that a producer's lease expenditures applicable to oil and gas  
 16 produced from a lease issued under AS 38.05.180(f)(3)(B), (D), or (E) include the  
 17 share of net profit paid to the state under that lease.

18 (3) taxes based on or measured by net income;

19 (4) interest or other financing charges or costs of raising equity or  
 20 debt capital;

21 (5) acquisition costs for a lease or property or exploration license;

22 (6) costs, ~~including repairs and replacements,~~ arising from ~~or~~  
 23 ~~associated with~~ fraud, wilful misconduct, [OR] gross negligence, ~~criminal~~  
 24 ~~negligence, or violation of law, including or failure to comply with an obligation~~  
 25 ~~under a violation of 33 U.S.C. 1319(e)(1) lease, permit, or license issued by the~~  
 26 ~~state or 1321(b)(3) (Clean Water Act) federal government:~~

27 (7) fines or penalties imposed by law;

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

31 (9) costs incurred in organizing a partnership, joint venture, or other

1 business entity or arrangement;

2 (10) amounts paid to indemnify the state; the exclusion provided by  
3 this paragraph does not apply to the costs of obtaining insurance or a surety bond  
4 from a third-party insurer or surety;

5 (11) surcharges levied under AS 43.55.201 or 43.55.300;

6 (12) ~~an expenditure incurred~~ for a transaction that is an internal  
7 transfer or is otherwise not an arm's length transaction, ~~unless the producer~~  
8 ~~establishes to the satisfaction of the department expenditures incurred that the~~  
9 ~~expenditure is not~~ EXPENDITURES INCURRED THAT ARE ~~are~~ in excess of fair  
10 market value;

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

15 (14) a tax levied under AS 43.55.011;

16 (15) [THE PORTION OF] costs incurred for dismantlement, removal,  
17 surrender, or abandonment of a facility, pipeline, well pad, platform, or other  
18 structure, or for the restoration of a lease, field, unit, area, tract of land, body of  
19 water, or right-of-way in conjunction with dismantlement, removal, surrender, or  
20 abandonment [, THAT IS ATTRIBUTABLE TO PRODUCTION OF OIL OR GAS  
21 OCCURRING BEFORE APRIL 1, 2006; THE PORTION IS CALCULATED AS A  
22 RATIO OF THE AMOUNT OF OIL AND GAS PRODUCTION, IN BARRELS OF  
23 OIL EQUIVALENT, ASSOCIATED WITH THE FACILITY, PIPELINE, WELL  
24 PAD, PLATFORM, OTHER STRUCTURE, LEASE, FIELD, UNIT, AREA, BODY  
25 OF WATER, OR RIGHT-OF-WAY OCCURRING BEFORE APRIL 1, 2006, TO  
26 THE TOTAL AMOUNT OF OIL AND GAS PRODUCTION, IN BARRELS OF  
27 OIL EQUIVALENT, ASSOCIATED WITH THAT FACILITY, PIPELINE, WELL  
28 PAD, PLATFORM, OTHER STRUCTURE, LEASE, FIELD, UNIT, AREA, BODY  
29 OF WATER, OR RIGHT-OF-WAY THROUGH THE END OF THE CALENDAR  
30 MONTH BEFORE COMMENCEMENT OF THE DISMANTLEMENT,  
31 REMOVAL, SURRENDER, OR ABANDONMENT]; a cost is not excluded under

1 this paragraph if the dismantlement, removal, surrender, or abandonment for which  
2 the cost is incurred is undertaken for the purpose of replacing, renovating, or  
3 improving the facility, pipeline, well pad, platform, or other structure; [FOR THE  
4 PURPOSES OF THIS PARAGRAPH, "BARREL OF OIL EQUIVALENT" MEANS

5 (A) IN THE CASE OF OIL, ONE BARREL;

6 (B) IN THE CASE OF GAS, 6,000 CUBIC FEET;]

7 (16) costs incurred for containment, control, cleanup, or removal in  
8 connection with any unpermitted release of oil or a hazardous substance and any  
9 liability for damages imposed on the producer or explorer for that unpermitted  
10 release: this paragraph does not apply to the cost of developing and maintaining an oil  
11 discharge prevention and contingency plan under AS 46.04.030;

12 (17) costs incurred to satisfy a work commitment under an exploration  
13 license under AS 38.05.132;

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

20 (19) costs incurred for repair, replacement, or deferred  
21 maintenance of a facility, a pipeline, a structure, or equipment, other than a well,  
22 that results in or is undertaken in response to a failure, problem, or event that  
23 results in an unscheduled interruption of, or reduction in the rate of, oil or gas  
24 production; or costs incurred for repair, replacement, or deferred maintenance  
25 of a facility, a pipeline, a structure, or equipment, other than a well, that is  
26 undertaken in response to, or is otherwise associated with, an unpermitted  
27 release of a hazardous substance or of gas; however, costs under this paragraph  
28 that would otherwise constitute lease expenditures under (a) and (b) of this  
29 section may be treated as lease expenditures if the department determines that  
30 the repair or replacement is solely necessitated by an act of war, by an  
31 unanticipated grave natural disaster or other natural phenomenon of an

1 exceptional, inevitable, and irresistible character, the effects of which could not  
2 have been prevented or avoided by the exercise of due care or foresight, or by an  
3 intentional or negligent act or omission of a third party, other than a party or its  
4 agents in privity of contract with, or employed by, the producer or an operator  
5 acting for the producer, but only if the producer or operator, as applicable,  
6 exercised due care in operating and maintaining the facility, pipeline, structure,  
7 or equipment, and took reasonable precautions against the act or omission of the  
8 third party and against the consequences of the act or omission; in this  
9 paragraph,

10 (A) "costs incurred for repair, replacement, or deferred  
11 maintenance of a facility, a pipeline, a structure, or equipment" includes  
12 costs to dismantle and remove the facility, pipeline, structure, or  
13 equipment that is being replaced;

14 (B) "hazardous substance" has the meaning given in  
15 AS 46.03.826;

16 (C) "replacement" includes renovation or improvement;

17 (20) costs incurred to construct, acquire, or operate a refinery or  
18 crude oil topping plant, regardless of whether the products of the refinery or  
19 topping plant are used in oil or gas exploration, development, or production  
20 operations; however, if a producer owns a refinery or crude oil topping plant  
21 that is located on or near the premises of the producer's lease or property in the  
22 state and that processes the producer's oil produced from that lease or property  
23 into a product that the producer uses in the operation of the lease or property in  
24 drilling for or producing oil or gas, the producer's lease expenditures include the  
25 amount calculated by subtracting from the fair market value of the product used  
26 the prevailing value, as determined under AS 43.55.020(f), of the oil that is  
27 processed;

28 ~~(2021)~~ costs of lobbying, public relations, public relations  
29 advertising, or policy advocacy.

30 \* ~~Sec. 49.53~~, AS 43.55.165(h) is amended to read:

31 (h) The department shall adopt regulations that provide for reasonable

1 methods of allocating costs between oil and gas, ~~between gas subject to~~  
2 ~~AS 43.55.011(e) and other gas,~~ and between leases or properties in those  
3 circumstances where an allocation of costs is required to determine [THE  
4 DETERMINATION OF THE] lease expenditures that are costs of exploring for,  
5 developing, or producing oil deposits or costs of exploring for, developing, or  
6 producing gas deposits [APPLICABLE TO OIL OR TO GAS], or that are costs of  
7 exploring for, developing, or producing oil or gas deposits located within  
8 [APPLICABLE TO OIL AND GAS PRODUCED FROM] different leases or  
9 properties [, REQUIRES AN ALLOCATION OF COSTS].

10 \* ~~Sec. 50.54.~~ AS 43.55.165~~170(a)~~ is amended by adding new subsections to read:

11 (k) ~~For purposes of AS 43.55.160, for a calendar year after 2006, a producer's~~  
12 ~~total lease expenditures, before adjustment under AS 43.55.170, that are applicable to~~  
13 ~~oil and gas produced by the producer from all leases or properties within a unit from~~  
14 ~~which 1,000,000,000 BTU equivalent barrels of oil or gas have been cumulatively~~  
15 ~~produced by the close of the most recent calendar year and from which the average~~  
16 ~~daily oil and gas production during the most recent calendar year exceeded 100,000~~  
17 ~~BTU equivalent barrels are determined under this subsection and (l) of this section.~~  
18 ~~Except as otherwise provided(a) Unless the payment or credit has already been~~  
19 ~~subtracted in calculating billable or billed costs under (l) of this section, the~~  
20 ~~producer's total lease expenditures, other than qualified capital expenditures, (1) for~~  
21 ~~calendar year 2007, are equal to the product of 1.37 multiplied by the total lease~~  
22 ~~expenditures for calendar year 2006, other than qualified capital expenditures, that are~~  
23 ~~applicable to oil and gas produced by the producer from all leases or properties within~~  
24 ~~the unit, as reported on the producer's statement under AS 43.55.030(a) for calendar~~  
25 ~~year 2006, and (2) for a calendar year after 2007, are equal to the product of 1.03~~  
26 ~~multiplied by the total lease expenditures, other than qualified capital expenditures,~~  
27 ~~determined for the previous calendar year under this subsection. The producer's total~~  
28 ~~lease expenditures for a calendar year after 2006 that are applicable to oil and gas~~  
29 ~~produced by the producer from all leases or properties within a unit subject to this~~  
30 ~~subsection are the sum of the producer's qualified capital expenditures incurred~~  
31 ~~during the calendar year that are applicable to that oil and gas plus the lease~~

1 expenditures, other than qualified capital expenditures, that are applicable to that oil  
2 and gas as determined under this subsection and (f) of this section. If a producer  
3 whose lease expenditures for 2006 are used to determine lease expenditures for a later  
4 calendar year under this subsection transfers an interest in an affected lease or  
5 property to a different producer, the transferee's lease expenditures applicable to oil  
6 and gas produced by the transferee from the lease or property continue to be  
7 determined under this subsection using those 2006 lease expenditures. In this  
8 subsection, "qualified capital expenditures" has the meaning given in AS 43.55.023.

9 (f) If, after audit by the department of a producer's statement or amended  
10 statement under AS 43.55.030(a) for calendar year 2006, the department finally  
11 determines that the reported amount of total lease expenditures, other than qualified  
12 capital expenditures, for calendar year 2006 applicable to oil and gas produced by the  
13 producer from all leases or properties within a unit subject to (k) of this section  
14 exceeds by more than 10 percent the actual amount of those lease expenditures, other  
15 than qualified capital expenditures, the producer or transferee, as applicable, shall (1)  
16 substitute the actual amount of those lease expenditures, other than qualified capital  
17 expenditures, for purposes of the calculations set out in (k) of this section, and (2) file  
18 amended statements for affected past tax periods within 60 days after the final  
19 determination.

20 \* ~~Sec. 51. AS 43.55.170(a) is amended to read:~~

21 (a) ~~A [UNLESS THE PAYMENT OR CREDIT HAS ALREADY BEEN~~  
22 ~~SUBTRACTED IN CALCULATING BILLABLE OR BILLED COSTS UNDER~~  
23 ~~AS 43.55.165(c) [OR (d), (A)]],~~ a producer's lease expenditures under AS 43.55.165  
24 must be adjusted by subtracting payments or credits, other than tax credits, received  
25 by the producer or by an operator acting for the producer for

26 (1) the use by another person of a production facility in which the  
27 producer has an ownership interest or the management by the producer of a  
28 production facility under a management agreement providing for the producer to  
29 receive a management fee;

30 (2) a reimbursement or similar payment that offsets the producer's  
31 lease expenditures, including an insurance recovery from a third-party insurer and a

1 payment from the state or federal government for reimbursement of the producer's  
2 upstream costs, including costs for gathering, separating, cleaning, dehydration,  
3 compressing, or other field handling associated with the production of oil or gas  
4 upstream of the point of production;

5 (3) the sale or other transfer of

6 (A) an asset, including geological, geophysical, or well data or  
7 interpretations, acquired by the producer as a result of a lease expenditure or  
8 an expenditure that would be a lease expenditure if it were incurred after  
9 March 31, 2006; for purposes of this subparagraph,

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

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

18 (B) oil or gas

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

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

23 \* ~~Sec. 52.55.~~ AS 43.55 is amended by adding a new section to article 4 to read:

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

30 (1) the amount of oil or gas production;

31 (2) the amount of taxes levied under this chapter or paid under this

1 chapter;

- 2 (3) the effective tax rates under this chapter;
- 3 (4) the gross value of oil or gas at the point of production;
- 4 (5) the transportation costs for oil or gas;
- 5 (6) qualified capital expenditures, as defined in AS 43.55.023;
- 6 (7) exploration expenditures under AS 43.55.025;
- 7 (8) production tax values of oil or gas under AS 43.55.160;
- 8 (9) lease expenditures under AS 43.55.165;
- 9 (10) adjustments to lease expenditures under AS 43.55.170;
- 10 (11) tax credits applicable or potentially applicable against taxes

11 levied by this chapter.

12 \* Sec. 53.56, AS 43.55.900 is amended by adding new paragraphs to read:

13 (22) "producer" means an owner of an operating right, operating  
14 interest, or working interest in a mineral interest in oil or gas;

15 (23) "~~progressivity tax rate~~" means ~~that part of the tax rate in~~  
16 ~~AS 43.55.011(g) that exceeds 25 percent;~~

17 ~~(24)~~ "unit" means a group of tracts of land that is

18 (A) subject to a cooperative or a unit plan of development or  
19 operation that has been certified by the commissioner of natural resources  
20 under AS 38.05.180(p);

21 (B) subject to a cooperative or a unit plan of development or  
22 operation that has been certified by the United States Secretary of the Interior  
23 under 30 U.S.C. 226(m);

24 (C) subject to an agreement of the owners of interests in the  
25 tracts of land to validly integrate their interests to provide for the unitized  
26 management, development, and operation of the tracts of land as a unit, within  
27 the meaning of AS 31.05.110(a); or

28 (D) within the unit area of a unit created by order of the  
29 Alaska Oil and Gas Conservation Commission under AS 31.05.110(b\*);

30 ~~(25) "used in the state" means delivered for consumption as fuel in the~~  
31 ~~state, including as fuel consumed to generate electricity.~~

1 ~~\* Sec. 54. AS 43.55.160(e), 43.55.165(e), 43.55.165(d), and 43.55.180 are repealed.~~

2 ~~\* Sec. 55. The uncodified law of the State of Alaska is amended by adding a new section to~~  
3 ~~read:~~

4 ~~APPLICABILITY. (a) Sections 15, 36, 38, 44, 51, and 54 of this Act apply to oil~~  
5 ~~and gas produced after December 31, 2007.~~

6 ~~(b) Sections 36 and 38 of this Act apply to statements and reports under~~  
7 ~~AS 43.55.030(a), as amended by sec. 36 of this Act, and AS 43.55.030(e) and (f), as added~~  
8 ~~by sec. 38 of this Act, required to be filed after December 31, 2007.~~

9 ~~(c) Sections 29, 32 and 34 of this Act apply to exploration expenditures incurred for~~  
10 ~~work performed after December 31, 2006, that are the basis of tax credits that may be~~  
11 ~~claimed against taxes levied for oil and gas produced after December 31, 2007.~~

12 ~~(d) AS 43.55.055, enacted by sec. 40 of this Act, applies to understatements made~~  
13 ~~after the effective date of sec. 40 of this Act.~~

14 ~~(e) AS 43.55.075(a), enacted by sec. 41 of this Act, applies to any tax liability under~~  
15 ~~AS 43.55 with respect to which the period of limitations on assessment under AS 43.05.260~~  
16 ~~had not expired before the effective date of secs. 44 and 41 of this Act.~~

17 ~~(f) The penalty in AS 43.55.030(d), enacted by the amendment to AS 43.55.030(d) in~~  
18 ~~sec. 37 of this Act, applies to any report required to be filed after the effective date of sec. 37~~  
19 ~~of this Act that is not filed timely.~~

20 ~~(g) The penalty in AS 43.55.040(6), enacted by the amendment to AS 43.55.040 in~~  
21 ~~sec. 39 of this Act, applies to any report, statement, or other document required to be filed~~  
22 ~~after the effective date of sec. 39 of this Act.~~

23 ~~\* Sec. 56. The uncodified law of the State of Alaska is amended by adding new sections to~~  
24 ~~read:~~

25 ~~OIL AND GAS REVENUE AUDIT MASTER POSITIONS: LEGISLATIVE~~  
26 ~~INTENT. It is the intent of the legislature that the commissioner of administration shall~~  
27 ~~cause not more than four oil and gas revenue audit master positions to be created in the~~  
28 ~~Department of Revenue and not more than two oil and gas revenue audit master positions to~~  
29 ~~be created in the Department of Natural Resources. Oil and gas revenue audit masters shall~~  
30 ~~be employed in a professional capacity to collect oil and gas revenue by developing policy,~~  
31 ~~conducting studies, drafting proposed regulations, enforcing regulations, and directing audits~~

1 ~~by oil and gas auditors.~~

2 ~~OIL AND GAS AUDITORS: CLASSIFICATION AND PAY PLANS.~~

3 ~~Notwithstanding AS 39.25.150(2), the Department of Administration shall develop and~~  
 4 ~~implement a distinct position classification plan and a distinct pay plan for oil and gas~~  
 5 ~~auditors and their immediate supervisors that perform~~

6 ~~(1) production tax audits in the Department of Revenue;~~

7 ~~(2) royalty audits, including net profit share audits, in the Department of~~  
 8 ~~Natural Resources.~~

9 ~~\* Sec. 57. The uncodified law of the State of Alaska is amended by adding a new section to~~  
 10 ~~read:~~

11 ~~TRANSITION: DEPARTMENT OF NATURAL RESOURCES REGULATIONS.~~

12 ~~Notwithstanding any contrary provision of AS 44.62.240, a regulation adopted by the~~  
 13 ~~Department of Natural Resources to implement, interpret, make specific, or otherwise carry~~  
 14 ~~out statutory provisions for the administration of oil and gas leases issued under~~  
 15 ~~AS 38.05.180(F)(3)(B), (D), or (E), to the extent the regulation deals with the treatment of oil~~  
 16 ~~and gas production taxes in determining net profits under those leases, may apply~~  
 17 ~~retroactively to April 1, 2006, if the Department of Natural Resources expressly designates in~~  
 18 ~~the regulation that the regulation applies retroactively to that date. \* Sec. 57,~~

19 ~~AS 43.55.011(h), 43.55.011(i), 43.55.011(n), 43.55.160(c), and 43.55.165(d) are repealed.~~

20 ~~\* Sec. 58. The uncodified law of the State of Alaska is amended by adding a new section to~~  
 21 ~~read:~~

22 ~~APPLICABILITY. (a) Sections 15 - 27, 29 - 38, and 45 - 57 of this Act apply to oil~~  
 23 ~~and gas produced after June 30, 2007.~~

24 ~~(b) Sections 39 and 41 of this Act apply to statements and reports under~~  
 25 ~~AS 43.55.030(a), as amended by sec. 39 of this Act, and AS 43.55.030(e) and (f), as added~~  
 26 ~~by sec. 41 of this Act, required to be filed after the effective date of secs. 39 and 41 of this~~  
 27 ~~Act.~~

28 ~~(c) Sections 30 - 33, 35, and 37 of this Act apply to exploration expenditures incurred~~  
 29 ~~for work performed after December 31, 2007, that are the basis of tax credits that may be~~  
 30 ~~claimed against taxes levied for oil and gas produced after December 31, 2007.~~

31 ~~(d) AS 43.55.075(a), enacted by sec. 43 of this Act, applies to any tax liability under~~

1 AS 43.55 with respect to which the period of limitations on assessment under AS 43.05.260  
2 had not expired before the effective date of secs. 14 and 43 of this Act.

3 (e) The penalty in AS 43.55.030(d), enacted by the amendment to AS 43.55.030(d)  
4 in sec. 40 of this Act, applies to any report required to be filed after the effective date of sec.  
5 40 of this Act that is not filed timely.

6 (f) The penalty in AS 43.55.040(7), enacted by the amendment to AS 43.55.040 in  
7 sec. 42 of this Act, applies to any report, statement, or other document required to be filed  
8 after the effective date of sec. 42 of this Act.

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

11 OIL AND GAS REVENUE AUDIT MASTER POSITIONS: LEGISLATIVE  
12 INTENT. It is the intent of the legislature that the commissioner of administration shall cause  
13 not more than four oil and gas revenue audit master positions to be created in the Department  
14 of Revenue and not more than two oil and gas revenue audit master positions to be created in  
15 the Department of natural Resources. Oil and gas revenue audit masters shall be employed in  
16 a professional capacity to collect oil and gas revenue by developing policy, conducting  
17 studies, drafting proposed regulations, enforcing regulations, and directing audits by oil and  
18 gas auditors.

19 \* Sec. 60. The uncodified law of the State of Alaska is amended by adding a new section to  
20 read:

21 OIL AND GAS AUDITORS: CLASSIFICATION AND PAY PLANS.  
22 Notwithstanding AS 39.25.150(2), the Department of Administration shall develop and  
23 implement a distinct position classification plan and a distinct pay plan for oil and gas  
24 auditors and their immediate supervisors, other than revenue audit masters, that perform

25 (1) oil and gas tax audits in the Department of Revenue under the direction of  
26 an oil and gas revenue audit master;

27 (2) royalty audits, including net profit share audits, in the Department of  
28 Natural Resources under the direction of an oil and gas revenue audit master.

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

31 TRANSITION: PAYMENT OF TAX. A person subject to tax under AS 43.55 that is

1 required to make one or more installment payments of estimated tax or other payment of tax  
2 under AS 43.55.020(a), as amended by sec. 21 of this Act, for the production of oil or gas  
3 during a month after June 30, 2007, and before the effective date of sec. 21 of this Act but  
4 that failed to pay the full amount of the installment payments or other payment of tax  
5 required under AS 43.55.020(a) because of the retroactive application of secs. 15 - 27, 29 -  
6 38, and 45 - 57 of this Act under sec. 64 of this Act, shall pay before April 1, 2008, the  
7 balance of any tax due under AS 43.55 for the period after June 30, 2007, and before the  
8 effective date of this section.

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

11 TRANSITION: RETROACTIVITY OF REGULATIONS. Notwithstanding any  
12 contrary provision of AS 44.62.240,

13 (1) if the Department of Revenue expressly designates in the regulation that  
14 the regulation applies retroactively to that date, a regulation adopted by the Department of  
15 Revenue to implement, interpret, make specific, or otherwise carry out secs. 15 - 27, 29 - 38,  
16 and 45 - 57 of this Act may apply retroactively to July 1, 2007;

17 (2) a regulation adopted by the Department of Natural Resources to  
18 implement, interpret, make specific, or otherwise carry out statutory provisions for the  
19 administration of oil and gas leases issued under AS 38.05.180(f)(3)(B), (D), or (E), to the  
20 extent the regulation deals with the treatment of oil and gas production taxes in determining  
21 net profits under those leases, may apply retroactively to April 1, 2006, if the Department of  
22 Natural Resources expressly designates in the regulation that the regulation applies  
23 retroactively to that date.

24 \* Sec. 63. The uncodified law of the State of Alaska is amended by adding a new section to  
25 read:

26 TRANSITION: REGULATIONS. The Department of Natural Resources and the  
27 Department of Revenue may proceed to adopt regulations to implement this Act. The  
28 regulations take effect under AS 44.62 (Administrative Procedure Act), but not before the  
29 effective date of the law implemented by the regulation.

30 \* Sec. ~~59.64~~. The uncodified law of the State of Alaska is amended by adding a new  
31 section to read:

1 REVISOR'S INSTRUCTION. In the following statute sections, the revisor of statutes  
2 shall substitute the spanned reference

3 (1) ~~AS 43.55.011 - 43.55.170~~ for the spanned reference "~~AS 43.55.011 -~~  
4 ~~43.55.180~~"; ~~AS 43.55.020(e), 43.55.080, 43.55.135, 43.55.150(a), 43.55.201(e), and~~  
5 ~~43.55.300(e)~~;

6 (2) "~~AS 43.55.017 - 43.55.170~~" for the spanned reference "~~AS 43.55.017 -~~  
7 ~~43.55.180~~"; ~~AS 43.55.023(g)~~.

8 \* ~~Sec. 60.~~ RETROACTIVITY OF CERTAIN PROVISIONS OF THIS ACT. (a)  
9 Sections 29 and 34 of this Act are retroactive to July 1, 2003.

10 (b) Sections 15 - ~~36~~ 27, 29 - 38, ~~44~~ 51, and ~~54~~ 45 - 57 of this Act take are retroactive  
11 to July 1, 2007.

12 \* Sec. 65. Section 28 of this Act takes effect January 1, 2008.

13 \* Sec. ~~61-66~~. Except as provided in sec. ~~60~~ 65 of this Act, this Act takes effect immediately  
14 under AS 01.10.070(c).

*Sections 29-34  
repealed by  
"Reg. 10"*  
*Galun about  
half that"*

L

**SB**

**2001**

**(FILE 7)**

**PPT**

**BACKGR'D**

**(SEE ALSO PEDRO VAN MEURES  
PRESENTTION TO LB&A 10/18/07)**

**Petroleum Profits Tax (PPT)  
Implementation Status Report**

**Alaska Department of Revenue  
August 3, 2007**

## PPT IMPLEMENTATION STATUS REPORT

### I. Purpose of the Report and Conclusions:

In August 2006, the Alaska Legislature passed HB 3001 containing a new oil and gas production tax system called the Petroleum Profits Tax (PPT). The new profits-based tax replaced the previous production tax based on gross value, generally referred to as the "Economic Limit Factor" (ELF) tax system. Debate and passage of HB 3001 was contentious, with questions raised on the propriety of a profits-based tax and on the appropriate tax rate. The controversy escalated earlier this year with the handing down of federal indictments against several legislators that centered on potential corruption involving the PPT deliberations and votes.

The Governor tasked the Commissioner of Revenue with evaluating whether the PPT was meeting expectations with respect to state revenues and industry's reinvestment in Alaska. The Commissioner of Revenue formed a Production Tax Team, staffed with members from the Department of Revenue, Division of Tax and the Department of Natural Resources, Division of Oil and Gas to review various aspects of PPT implementation. Based on the information provided by the Production Tax Team, the initial conclusions of the Department of Revenue are:

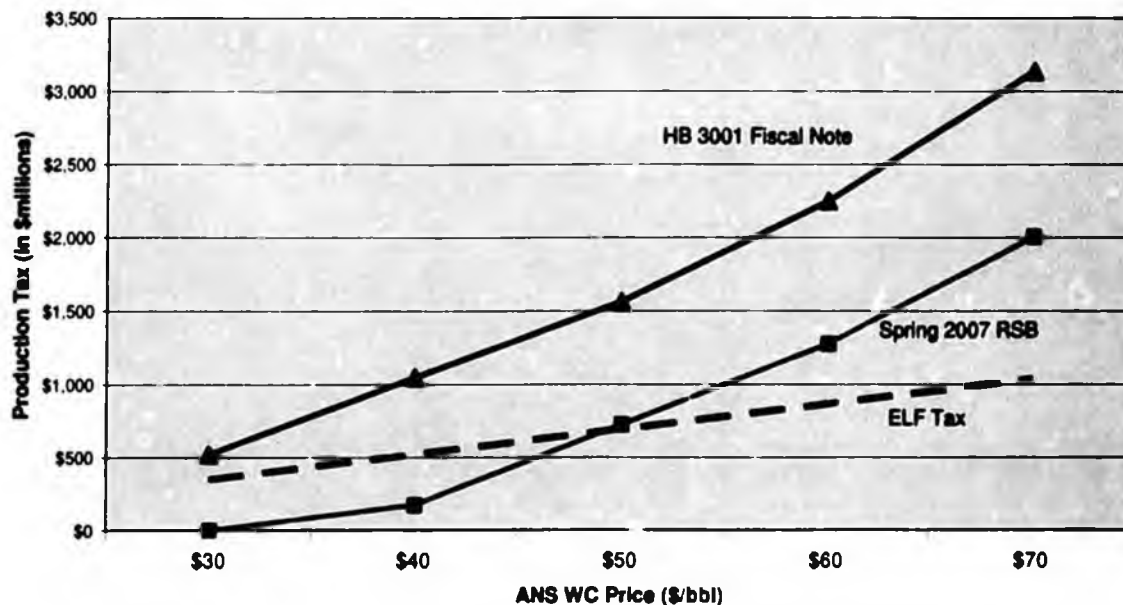
- 1) At current prices, the state is collecting more production tax revenues under PPT than it would have under the ELF system. However, those revenues are falling far short of what was expected when PPT was passed.
- 2) Operating and capita. costs are substantially higher than were forecasted in the PPT fiscal note provided to the legislature.
- 3) The value of PPT credits may not be fully realized for exploration companies new to Alaska, given the small market for resale among "producers."
- 4) The crossover oil price point where the state receives more revenue under the PPT than under the ELF system has moved from the \$26/barrel predicted in the PPT fiscal note to \$48/barrel.
- 5) The activation of the progressive surcharge has shifted from a market price of \$55 to over \$60 a barrel.
- 6) DOR faces significant challenges in implementing the PPT as currently structured.

## II. Discussion:

1) Production tax revenues are falling far short of expectations. The following graph shows the differences in modeling results for FY 2008 production tax revenues; this graph compares initial modeling for FY 2008<sup>1</sup>, as prepared for the House Bill 3001 (PPT) fiscal note [SCS HB3001(NGD)], with current modeling, as prepared for the *Spring 2007 Revenue Sources Book*, and with the tax revenue that would have been generated under the ELF system. The tax revenue expectations for FY 2008 are significantly lower than the revenue forecasted when the fiscal note was drafted. This is primarily due to the significantly higher costs being reported as compared to what was estimated in the fiscal note, as noted below.

In FY 2008, based on forecasted price and production levels, the PPT is expected to generate about \$250 million over that which would have been generated under the ELF system. However, this is more than \$800 million less than what was predicted in the PPT fiscal note.

**FY 2008 Production Tax Estimates: HB 3001 (24th Legislature) Fiscal Note and Spring 2007 Revenue Sources Book PPT Forecasts; and ELF Tax**



Note: Above estimates are based on most current taxpayer submitted expenditure forecasts and do not reflect any changes in spending due to increases or decreases in oil price

<sup>1</sup> Because of the unexpected disruptions to revenues and costs caused by the gathering line failures in the Prudhoe Bay Unit in FY 2007, the Department is using FY 2008 as the comparison year to eliminate one-time aberrations. In addition, the HB 3001<sup>1</sup> Fiscal Note and ELF Tax models have been adjusted to reflect current production estimates.

2) Operating and capital costs are substantially higher than were forecasted in the PPT fiscal note. The substantial and unanticipated increase in costs is the primary reason revenues are falling short of expectations. Throughout the latter half of 2004 and 2005, DOR officials gathered information from confidential tax documents, annual reports, private consultant analyses, and the industry about the costs of producing petroleum on the North Slope. DOR modeled the PPT revenue forecasts using these cost data and the results of this modeling were provided to the legislature to aid their consideration of the PPT.

Based on the cost data received by the Department for 2006 and 2007 since passage of PPT, the Department has increased by almost 100% taxpayer operating and capital cost estimates for FY 2008 in its Spring 2007 Revenue Source Book revenue projections. In discussions with taxpayers, DOR has been told that these higher costs levels for 2006 and 2007 are not aberrations caused by unique events, such as the Prudhoe Bay shutdown, and that we should anticipate costs remaining at these levels for the foreseeable future.

**North Slope Production and Costs FY 2008,  
per HB 3001 Fiscal Note and Spring 2007 Forecast**

	HB 3001 Fiscal Note	Spring 2007 Forecast
<b>FY 2008</b>		
<b>Production</b> (barrels per day)	802,000	764,000
<b>Costs</b>		
Operating costs (\$millions)	\$1,076	\$2,160
Capital costs (\$millions)	\$1,052	\$1,900
<b>Total Costs</b>	<b><u>\$2,128</u></b>	<b><u>\$4,060</u></b>
Total Costs per Barrel	\$7.27	\$14.56
Operating costs per barrel	\$3.68	\$7.75
Capital costs per barrel	\$3.59	\$6.81

High oil and gas prices since 2005 are frequently cited as the cause of these cost increases. Projects around the world that were once only marginally economic, are now considered very viable, and are now placing increased demands on limited supplies of engineering, procurement and construction services and on raw construction materials. The Upstream Capital Costs Index, developed by Cambridge Energy Research Associates (CERA), shows that costs for oil and gas production equipment, facilities, construction materials and personnel have increased 53% since 2005. CERA expects cost escalation to continue through 2007, although at a slower pace. Fluor Corporation estimates that prices for fabricated structural steel have increased 60-70% from 2003 to 2006, and that delivery times for these materials increased by 18-20 weeks from their previous levels. The same company reports that prices for seamless and welded pipe used in petroleum production have increased 80-160% from 2003 to 2006, and expects increases of another 15-50% by 2009.

It is too early to tell whether all of the costs reported under PPT thus far are properly deductible. Also, it is too early to know whether the increase in reported industry spending in the state will result in increased future production, or whether the increase in spending can be attributed to changed behavior as a result of the incentives included in PPT. What we do know is that the costs used in the modeling for the PPT fiscal note have proven inaccurate.

**3) The value of PPT credits may not be fully realized for exploration companies new to Alaska given the small market for resale among "producers."**

Under PPT, tax credits earned by investors and explorers may be transferred and sold to other taxpayers who have a production tax liability. Companies that have been issued credit certificates above and beyond the \$25 million that can be refunded by the state would presumably sell their certificates to the highest bidder. In the first year that the PPT has been in place, however, companies holding credit certificates report that there have been few buyers for the certificates, and that those offering to buy them are doing so at large discounts.

**4) The oil price crossover point where the state receives more revenue under the PPT than under the prior ELF system has moved from \$26/barrel to \$48/barrel.**

The ELF system "crossover point"—that is, the Alaska North Slope - West Coast (ANS WC) oil price whereby the PPT generates more revenue than the ELF system—was the focus of some attention during the 2006 legislative session. Primarily due to the increase in the cost estimate, the currently estimated crossover point is substantially higher than was projected in 2006.

**5) The activation of the progressive surcharge has shifted from a market price of \$55 to \$60-63 a barrel.** Because the surcharge is not activated until the taxpayer's net income per barrel exceeds \$40, higher costs have depressed taxpayer net income, thus delaying the price at which the surcharge kicks in. In addition, as production declines, the price at which the progressive surcharge is activated will move higher as costs are spread over fewer barrels. Although the level differs for each individual taxpayer, the North Slope average progressivity trigger is now estimated to be somewhere between \$60 and \$63 per barrel.

**6) DOR faces significant challenges in administering the PPT as currently structured.**

a) **Regulations-** The second phase of PPT regulations has been delayed as a result of the challenge of accurately describing the allowed and disallowed lease expenditure deductions.

b) **Revenue Forecasts-** The Department has been severely hampered in its ability to provide the administration and the legislature with accurate revenue forecasts because the department lacks future capital and operating expenditure information. The Department is in the process of rectifying this problem by requiring operators to provide forward-looking cost data, when and as provided to the unit working interest owners.

Statutory changes may be required to fortify and focus these requests for unit cost information.

c) Audits- With the passage of PPT, the department was authorized to hire eight auditors and one tax technician to assist with the additional audit requirements of the new tax structure. To date, the department has successfully filled the three most senior auditor positions, and has reduced the skills requirements for the remaining junior level auditor positions in light of the challenges of matching competitive pay with the more senior level skill sets.

The complexity of auditing production tax has increased several fold under the PPT, and the PPT increased the number of determinations an auditor must make. The provisions in the PPT which are intended to simplify and streamline these determinations through reliance upon unit owners' auditing of unit operators may assist this process, but we have not yet been through an audit cycle to assess the efficacy of this approach.

### III. Conclusion

The state's experience with PPT puts a spotlight on the risks associated with a net profit-based tax system. The new system introduced the added variable of costs into the oil revenue equation. While it is a risk that is inherent in the decision to approve a net profit-based tax, the question is whether the magnitude of the risk was fully understood by the legislature given the information provided to them. While costs would be expected to increase, the dramatic difference between what was predicted and what has actually been experienced brings into question whether the legislature made its decisions based upon appropriate information.

Another aspect of PPT, the tax credits given for capital expenditures, has been significantly reduced in value due to the lack of an efficient market for those new exploration companies looking to sell their credits to those who have current production. This deficiency is particularly troubling because these new exploration companies are the ones that provide the state with the greatest opportunity to encourage new production that might not otherwise occur.

Clearly, there are aspects to PPT that should be re-examined by the legislature. In particular, the legislature should reassess whether the state is getting its fair share of oil and gas revenues, and whether the credits are designed optimally to provide the maximum impact on the state's goal of encouraging investment that leads to more oil and gas production.

**SB 2001**

**(FILE 8)**

**INSTATE**

**GAS**

**& COOK INLET**

**TAX**

**STRUCTURE**

## **TAX EQUITY FOR GAS PRODUCTION FROM BASINS OUTSIDE OF COOK INLET AND SOUTH OF NORTH SLOPE**

**Need:** Several basins south of the Brooks Range could provide natural gas for which would (1) help alleviate large, looming gas production shortfalls in South Central, (2) result in delivery of local gas to Interior communities, and (3) provide gas for local uses in rural areas. In particular focus is gas exploration activity in the Nenana basin which is stalled in large measure due to gas tax changes made by PPT in 2006. Discovery of gas at Nenana could result in gas delivery to the entire Railbelt, including South Central.

**Remedy:** Changes to current PPT or pending ACES changes which would extend Cook Inlet gas production tax treatment for in state uses of gas that could be produced from basins south of the Brooks Range such as Nenana, Copper River, Healy, Yukon Flats, Wulik, Holitna and onshore Bristol Bay. There would be no change to the tax on any possible oil production from these areas.

**Background:** Prior to the enactment of PPT in 2006 several million dollars were spent by Andex Resources, Usibelli Energy, Doyon, Limited and Arctic Slope Regional Corporation gathering over 200 miles of seismic and performing other work related to conventional natural gas exploration, mostly on State lands in the Nenana basin under an exploration license. The Nenana basin is located along the Railbelt southwest of Fairbanks and to the immediate west of the community of Nenana. Earlier exploration programs and work under the current exploration license indicate the potential for gas in amounts that could provide pipeline gas and gas fired power to Railbelt communities from Fairbanks to Anchorage. There are no discoveries of oil or gas in this basin.

Pending is a decision to drill a 10,000 foot exploration well. However, Andex, the majority partner and operator in the venture, has declined to invest further due in major part to the 22.5 % PPT tax rate on any gas produced at Nenana. In contrast, Cook Inlet gas is taxed until 2022 at a much lower rate. The project has been suspended for soon to be three winter drilling seasons: first in anticipation of tax changes in 2006, the fallout from PPT enactment in 2007, and now the pending ACES proposal which because of timing precludes a drilling decision for 2008.

Nenana is the only pending gas exploration project designed to serve South Central and Interior Railbelt communities with pipeline gas and new gas-fired power which would be taxed at 22.5%. Moreover, Department of Revenue officials acknowledge that North Slope export gas will need to be taxed at a rate of perhaps 10% or lower before a large diameter pipeline could be sanctioned.

The potential of the Nenana basin is substantial. Experts note that as much as 6 trillion cubic feet of conventional natural gas could be recovered there. Cook Inlet has produced about 7 trillion cubic feet since the early 1960s. Yet, the Nenana gas project has a very high exploration risk profile because it is in a "wildcat" basin. There has been no discovery or production. There is no pipeline or other gas related infrastructure and services in the area. These elements, when combined with existing tax treatment, have resulted in the loss of the project's majority partner. Efforts to attract new participants to the venture have been unsuccessful.

## Questions heard from Legislators, staff and the Administration

**Why expand Cook Inlet tax coverage to all areas south of the Brooks Range, rather than to Nenana only?**

Basins such as Copper River and Yukon Flats also could provide gas to the Railbelt. The Brooks Range and the southern boundary of the North Slope Borough are demarcation lines separating the North Slope from the rest of the state. Expansion of Cook Inlet treatment up to either of these lines addresses the accepted principle that North Slope gas will need specific tax treatment, leaving the rest of the state with a different approach focused primarily on in state uses. Other basins south of the Brooks Range could provide gas to local communities and rural development for heating and power, such as Red Dog Mine (Wulik basin) and the pending Donlin Creek Mine (Holitna basin).

**Would extension of Cook Inlet tax coverage be good tax policy if a "big" gas find with export potential was made in one of these basins?**

Current Cook Inlet tax treatment has a limited life; it will sunset at the end of 2021. First drilling at Nenana could not start in all likelihood until January 2009. Exploration and development, if successful, would take several years, probably until 2013-2015, to find enough gas to justify a pipeline to serve a portion of Railbelt needs. Even if larger quantities were found, that gas would likely go to South Central to make up for accelerating production declines in Cook Inlet. The North Slope gas line would not be in place until 2016 or later, and space in that line will likely be taken up by North Slope gas for many years before there would be expansion possibilities—all after the 2021 sunset of the special Cook Inlet tax provisions. And, the Legislature can always change laws.

Regardless, the Nenana gas project, for example, is intended to provide gas to Alaskans. We believe this would be the case for anyone trying to develop gas in these other basins south of the Brooks Range and outside of Cook Inlet. There are at least two solutions to lingering concerns about a "big find" which might be exported out of state. They are: incorporation of a production "ceiling" provision at which each new basin would lose Cook Inlet tax treatment, or a simpler provision which grants Cook Inlet tax treatment solely to in state uses.

**Didn't "new area" basins outside of Cook Inlet and the North Slope get an additional PPT benefit last year?**

Yes. An additional \$6 million/year credit is available for oil and gas. However, in most financial models the PPT rules of general application, including the extra \$6 million credit, are not competitive with identical projects in Cook Inlet. To assure that the areas south of the Brooks Range are treated identically to Cook Inlet, the \$6 million credit as applied to gas should be eliminated if Cook Inlet gas provisions are granted.

It is important to note that the \$6 million credit is still a very valuable tool to attract investors to explore for oil in remote, unexplored places such as the Yukon Flats north of Fairbanks. The \$6 million credit as it applies to oil should not be repealed.

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October 30, 2007

Representative Mike Doogan  
716 W. 4<sup>th</sup> Avenue, Suite 320  
Anchorage, AK 99501-2133

Re: FNG's regulatory status  
Our File No. : 2102

Dear Representative Doogan:

I represent Fairbanks Natural Gas (FNG) in regulatory matters, including matters before the Regulatory Commission of Alaska (RCA). My client wishes to thank you for your interest and questions during the recent House Oil and Gas hearing on HB2001, and has asked me to provide additional information regarding FNG's regulatory status. You asked Rep. Ramras whether or not FNG is a regulated utility. His response was not entirely correct.

FNG is subject to RCA regulation, and operates pursuant to RCA Certificate of Public Convenience #514 in designated areas of Fairbanks. In 2003 the RCA approved a conditional exemption from rate regulation based on AS 42.05.711(d), which states, "The commission may exempt a utility, a class of utilities, or a utility service from all or a portion of this chapter if the commission finds that the exemption is in the public interest."

RCA Order No. U-02-048 determined that "FNG operates in a competitive market, and it is in the public interest to grant its petition for exemption. Economic regulation is not necessary under these circumstances." The RCA further stated, "We do not see the need to impress a rate cap on FNG, given the ease with which its customers can change fuels. We grant FNG's petition in Docket U-02-48 for exemption from rate regulation with conditions."

The conditions imposed on FNG by the RCA include:

- FNG is required to file informational tariffs with RCA before making any changes in rates.

Representative Mike Doogan  
October 30, 2007  
Page 2  
FNG/2102

- FNG cannot discriminate against customers who cannot switch fuels. These customers must be included in the same rate class with others who can easily switch, and must be charged the same rate.
- FNG must maintain a current tariff with the RCA through its informational tariff filings.
- FNG must notify its customers, at least one billing cycle in advance, of any rate changes. FNG's customers have considerably better and earlier actual notice of rate changes than customers of most other utilities.
- RCA will review filings for unreasonable discrimination between rate classes. The RCA staff does not "rubber stamp" FNG's filings, and has rejected tariff changes sought by FNG.
- FNG must file annual reports with the RCA.

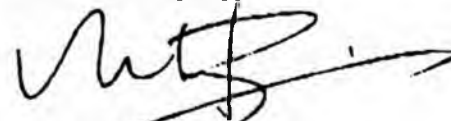
The RCA has recently determined not to reconsider FNG's conditional exemption, but has made it clear that it may reconsider the exemption in the future.

This regulation issue is relevant to FNG's effort to deliver an alternative fuel source to Fairbanks and its intent to pass along to Interior ratepayers the benefits of the tax ceiling currently enjoyed by residents of Southcentral Alaska.

Again, thank you for taking the time to raise these issues. Given your extremely busy schedule in deliberating the complex DPT, we appreciate your attention to this critical matter for FNG and Fairbanks natural gas users. Please do not hesitate to contact us with any further questions.

Sincerely,

ROSE & FIGURA



Mark L. Figura

MLF/blc

cc: House Oil & Gas Committee; Interior Delegation

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October 30, 2007

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Anchorage, AK 99501-2133

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Representative Mike Doogan  
October 30, 2007  
Page 2  
FNG/2102

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Sincerely,

ROSE & FIGURA



Mark L. Figura

MLF/blc

cc: House Oil & Gas Committee; Interior Delegation

**SB**

**2001**

**(FILE 9)**

**10/19/07**

# ALASKA STATE LEGISLATURE

Sen. Charlie Huggins, Chair  
Sen. Bert Stedman, Vice Chair  
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Sen. Gary Stevens  
Sen. Lesil McGuire  
Sen. Bill Wielechowski  
Sen. Thomas Wagoner



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800-862-3878

## Senate Resources Committee

Butrovich Rm 205

Friday, October 19, 2007

9:00 a.m. - 2:00 p.m.

## AGENDA

### Production Tax on Oil and Gas

Sponsor Presentation: Governor's Production Tax Team

Patrick Galvin, Commissioner Dept. of Revenue

Marcia Davis, Deputy Commissioner Dept. of Revenue

Jon Iverson, Dir. Tax Div., Dept of Revenue

Bob George, Gaffney, Cline & Associates

Rich Ruggiero, Gaffney, Cline & Associates



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RAR/jlm/C1492.00/gcah.292.07

October 19, 2007

## MEMORANDUM

**RE: Oil and Gas Reporting and Disclosure in Selected Countries**

As part of the review of its oil and gas fiscal system, the State of Alaska is exploring ways to improve the administration of its 'net' based taxes. Many believe the State is at a disadvantage to the oil companies in auditing their compliance as little data are routinely provided to the State. As such, Gaffney, Cline and Associates (GCA) has been asked to prepare a brief overview of how the acquisition, distribution and publication of oil company data are handled in other oil and gas producing regimes.

### SUMMARY

Provision by oil companies to host governments of detailed information pertaining to petroleum licenses and activities thereunder is routine around the world, usually as a condition of the license or contract under which the petroleum rights are granted. Certain data, including costs, may also be required (or covered, as well) by fiscal regulations governing different forms of taxation beyond general income tax provisions.

The information normally required to be provided encompasses the range from physical samples to activity plans and operating and financial data. The form of provision may vary, but formats consistent with electronic data exchange are developed for certain information. Where provided, data are generally at a well or field level of granularity.

Data provision is governed by various different confidentiality provisions, although sharing between different state/government entities appears more the standard than the exception. Basic geologic data are held confidential for periods of 2-5 years; although in some circumstances this may be as long as 10 years.

Data on fields under development and producing fields tend to either be released straight away, or are only released in aggregate form. For the most part, detailed data are only released on historical field or well production. Historical capital and operating cost data tend to be aggregated by country for disclosure, on an annual historical basis.

Limited amounts of data are also provided on a forecast basis. This is mixed between aggregated data and field-level data. Most of the field data so offered is reserves, but Denmark actually reports capital expenditure forecasts by field. No published forecast operating cost data has been identified.

Field data are typically submitted pursuant to two time-based criteria: at the time field exploration, appraisal or development plans are submitted, or a major revision to those plans is

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incorporated, and on an annual basis for tracking and monitoring. Typically both situations will include production, capital and operating costs.

In its overview of reporting, GCA focused its efforts on reviewing practice in the petroleum producing countries of the North Sea, Canada, and Timor-Leste (where GCA recently assisted in the drafting of the Petroleum Act, the Petroleum Fiscal Act and associated regulations, drawing on "best practice" from around the world), although selected other examples are also included.

Considerable additional detail is available from websites and publications that go beyond the overview here, and should be studied further before detailed laws and regulations are drafted in Alaska.

## DISCUSSION

### Ownership of Data

Bar very minor exceptions, it is only in the United States that private entities own mineral rights. In Alaska, the state owns the rights to minerals making it similar to all other international locations.

States then lease or grant those rights to petroleum companies for a period of time either via a license, concession, service agreement or production sharing agreement. In exchange for receiving the rights to exploit (the state's) hydrocarbon resources, the oil companies are routinely obligated to provide the state with most, if not all, of the data related to their petroleum operations. The legislation, regulations and contracts in most countries specify quite clearly that the state owns all data obtained or produced as part of petroleum operations.

*Timor-Leste shall have title to all data and information, whether raw, derived, processed, interpreted or analysed, obtained pursuant to any Authorisation.*

Some countries even go so far as to require that physical data, such as reservoir cores, are kept in-country at a state controlled facility.

*Data and information acquired during the course of Petroleum Operations may be freely exported by Authorised Persons provided that the Ministry may require that an original, or in the case of a core, rock, fluid or other physical sample, a usable portion of the original, of all data and information, both physical and electronic, be kept in Timor-Leste.*

### Submission of Data

A variety of regulations usually stipulate the manner in which data are to be transmitted to the state. Physical data, such as cores or fluid samples, are packaged and labeled for long term storage. These are shipped to a facility designated by the state.

Other data, such as seismic, logs, production and costs, are supplied in two forms. First, the data are generally presented in the form of a routine report required by regulation. Reports are generally submitted in a non-editable format to ensure their integrity. Second, all data are