Fiscal Impact
HCS CSSB21(RES)

For Presentation to the

House Finance Committee

April 6, 2013

Introduction

1. Key provisions analyzed
2. Total fiscal impact under Fall 2012 forecast
3. Hypothetical additional production scenarios
4. FY 2015 revenue sensitivity

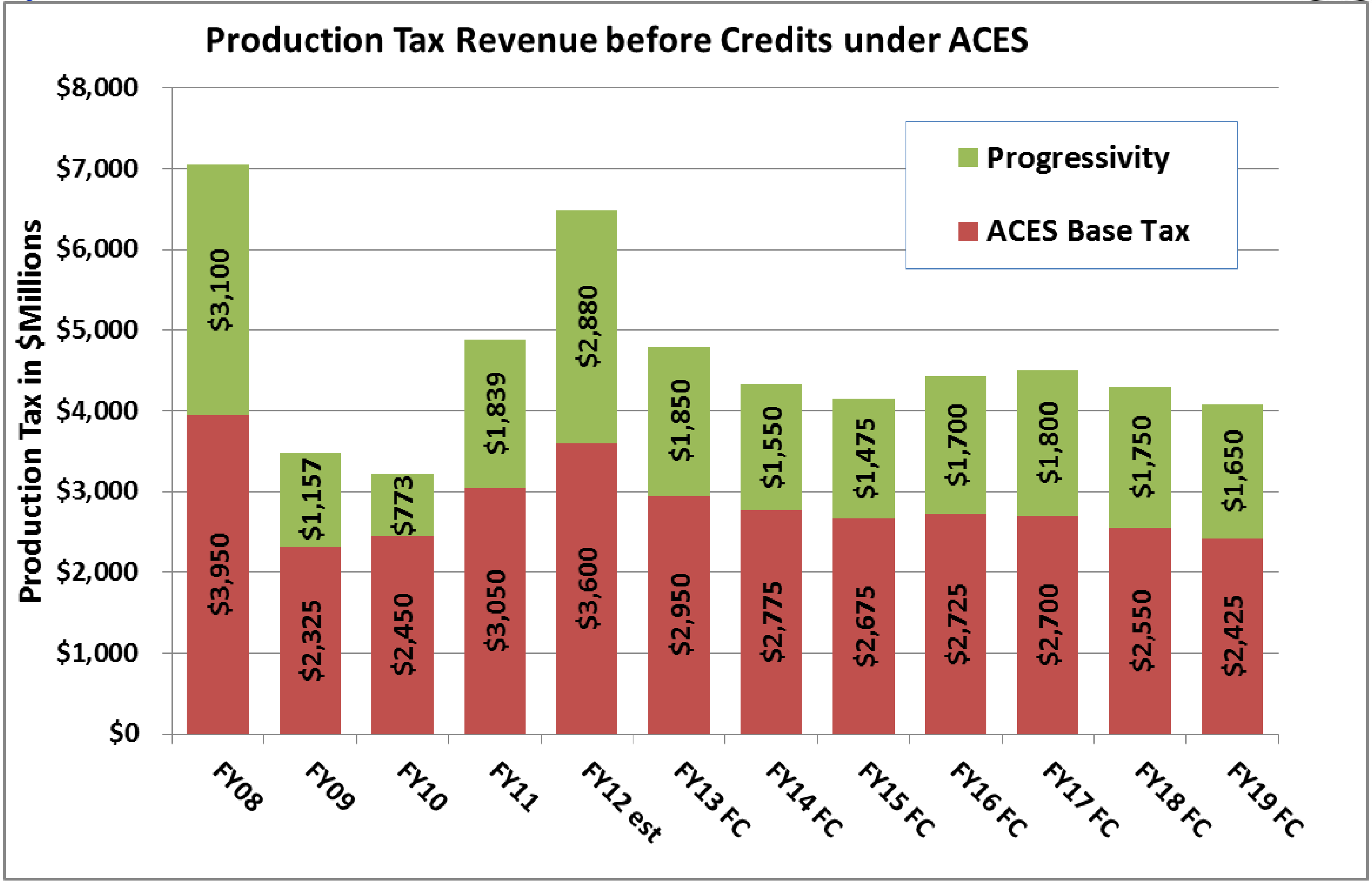
Note: presentation assumes an effective date of January 1, 2014 for most major provisions.

1. Repeals progressive surcharge

- Progressive surcharge at AS 43.55.011(g) repealed
- Progressive surcharge is an additional tax that is added to base tax
- Progressive surcharge increases tax rate at production tax values of greater than $30 / barrel
- Progressive surcharge may add up to 50% to the total tax rate at very high prices for a maximum total tax rate of 75%

- Fiscal Impact = varies by fiscal year, up to $1.8 billion per year under our Fall 2012 forecast

Impact of Progressive Surcharge



2. Increases base production tax rate

- Base tax rate increased to 33% from 25% under ACES; decreased from 35% from CS SB21
- Base tax rate of 33% applied to production tax value
- The higher base tax rate increases revenue from the base tax
- The higher base tax rate provides greater protection to the state at low oil prices

- Fiscal Impact = varies by fiscal year, up to $875 million per year under our Fall 2012 forecast

3. Limitations on capital credits

- Production tax credits under AS 43.55.023(a) for qualified capital expenditures are limited to expenditures incurred before January 1, 2014 for the North Slope
- 20% capital credit eliminated for North Slope after 1/1/2014 (replaced with new mechanisms that incentivize production, not spending).
- ACES provisions are unchanged for Cook Inlet and Middle Earth and they retain 20% capital credit

- Since capital credits are taken against liability or refunded, fiscal impact is on both revenue and budget
- Likely fiscal impact is summarized on following slide

Estimated Fiscal Impact for limitations on credits as compared to Fall 2012 Forecast ($millions)

	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018	FY 2019
NS capital credits against tax liability	$300	$700	$650	$550	$475	$400
NS credits for refund	$0	$150	$150	$150	$150	$150
Total Fiscal Impact	$300	$850	$800	$700	$625	$550

Note: these are positive fiscal impacts. NS credits for refund includes both capital and NOL credits refunded.

4. Changes to Net Operating Loss credit

- Companies that incur net losses from leases or properties on the North Slope will earn a credit of 33% of those losses, an 8% increase over the 25% credit provided in ACES.
  - Transferable credit.
  - Eligible for refund by the state.
- The revenue impact of this provision is -$30 million per year over the amount forecasted under ACES

5. Establishes Gross Revenue Exclusion

- Excludes 20% of gross value by reducing the gross value of the qualifying production in the determination of the production tax value.
- Qualifying production is any of the following:
  - **New Units** - Land was not in a unit on 1/1/2003
  - **New Participating Areas** - Produced within a PA established after 12/31/2011, in a unit formed before 1/1/2003, if participating area does not contain a reservoir that had been in a PA established before 12/31/2011
  - **Expansions of Participating Areas** - Produced from acreage that was added to an existing participating area by the Department of Natural Resources on or after 1/1/2014, and the producer demonstrates that the volume of oil or gas produced is from acreage added to an existing participating area.

- Fiscal Impact = Indeterminate, under $50 million / year under Fall 2012 forecast
- GRE benefit would apply almost entirely to “New Production” not currently included in our forecast. The fiscal impact that we are including in the analysis refers to production in our forecast that is likely to qualify.

6. Eliminates requirement that credits be taken over two years

- Capital credits and Net Operating Loss credits earned had to be split across two years under ACES
- This provision allows credits to be used in the year they were earned
- This provision aligns credit treatment on the North Slope with credit treatment in all other parts of the state
- Fiscal impact is neutral – simply shifts a future obligation to FY14.
- $400 million total obligation shifted to FY14: $250 million revenue impact; $150 million operating budget impact.

7. Changes funding source for community revenue sharing

- The community revenue sharing fund is amended to allow the legislature to make appropriations from the tax revenue collected under AS 43.20, as opposed to revenue collected under the provision that is proposed to be repealed - AS 43.55.011(g).
- Corporate income tax revenue under AS 43.20 is adequate to provide the maximum annual appropriation of $60 million or the amount to bring the fund up to $180 million.
  - Corporate income tax has exceeded $500 million every year for the last 8 years.
- Zero fiscal impact.

8. Establishes per oil barrel tax credit

- $5 credit per taxable barrel for oil production subject to GRE.
  - Must be applied against tax liability and cannot cause tax liability to be less than zero
- Sliding scale for Non-GRE eligible oil production.
  - Scale is progressive on GVPP (wellhead) value per barrel of oil starting at $8/barrel at wellhead prices up to $80/barrel down to $0/barrel at wellhead prices over $150/barrel
  - Sliding scale is at rate of $1 credit per $10 wellhead price
  - Adds a slightly progressive feature to the system
- Both credits tie incentives to production, not spending
- Credits can not be transferred, carried forward, or used to reduce the producer's tax liability to less than zero.
  - The credit for areas not eligible for a GRE may not reduce the producer's tax liability to less than the minimum tax established under AS 43.55.011(f).
- Likely fiscal impact is summarized on next slide

Estimated Fiscal Impact for $5 per taxable oil barrel and sliding scale credit* as compared to Fall 2012 Forecast ($millions)

FY 2014	FY 2015	FY 2016	FY 2017	FY 2018	FY 2019
-$425	-$825	-$775	-$750	-$700	-$675

* At forecast prices the per taxable barrel credit is $5 on the sliding scale.

9. Creates service industry expenditures credit

- New Corporate Income Tax Credit for oil and gas service companies
- Credit is 10% of qualifying in-state expenditures:
  - Manufacturing of oil and gas equipment
  - Modification of oil and gas equipment
  - For in-state spending only
- Maximum $10 million per taxpayer per year
- Non-transferable; Any amount of the credit that exceeds the taxpayer's liability under AS 43.20 may be carried forward for 5 years.

- Fiscal Impact = Indeterminate, less than $25 million / year
- Difficult to estimate due to lack of data

10. Interest rate on delinquent taxes changed

- Currently the higher of 5 percentage points above the annual rate of interest charged by the 12th Federal Reserve District or 11 percent.
- Changed to 3 percentage points above the annual rate of interest charged by the 12th Federal Reserve District.
- Change applied to interest charged on delinquent taxes and refunds and assessments for most taxes administered by DOR.

- Fiscal impacts include $100,000 for DOR accounting system changes.
- Fiscal impact is estimated to be up to -$25 million per year, increasing over time as more delinquent taxes are calculated under the new interest rates established with this provision.
- Our fiscal impact estimates do not take into account changes in taxpayer behavior as a result of this reduction in interest rate.

11. Removes 3-mile requirement for "Middle Earth" frontier basin credit

- Explanation:
  - Removes requirement that well be 3 miles from existing well to qualify for credit
  - Applies to frontier basin credit in AS 43.55.025(a)(6)
  - Credit is 80% of eligible drilling expenditures, up to $25 million, for first four eligible wells
    - Drilled before July 1, 2016 in qualifying frontier basin
    - Must be a new target pre-approved by DNR
    - Well data shared with DNR
  - Credit is transferable
  - Cannot take this credit along with NOL credit

- Fiscal Impact already accounted for in Fall 2012 forecast

12. The small producer credit

- **The small producer credit at AS 43.55.024 is extended to the later of 2022 or the ninth calendar year after the calendar year that the producer first has commercial production.**

- Fiscal impact:
  - Zero in FY 2014-2016
  - -$25 million in FY 2017-2018
  - -$50 million in FY 2019

13. DOR Production Tax Report to Legislature

- The Department of Revenue is required to provide a report to the legislature on or before the first day of the 2016 regular session.
  - This report will study various elements of the production tax system and recommend changes to the system.

- This report will be completed with existing professional staff and has no revenue impact.

14. Joint Interest Billings Consideration

- The Department of Revenue is required to consider Joint Interest Billings in the audit process for production tax and may rely on audits performed by joint interest owners in performing state audits of taxpayers.

- This provision may lead to slight changes in the department's audit process and has an indeterminate fiscal impact.
- Fiscal impacts include $50,000 for regulations review for this and other provisions.

15. AIDEA Bonding Authority

- AIDEA is given bonding authority to finance construction of oil and gas processing facilities.

- This provision does not have any fiscal impact on the Department of Revenue.

Provisions in HCS CSSB21(RES) and their Estimated Fiscal Impact as compared to Fall 2012 Forecast ($millions) [1]

Brief Description of Provision	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018	FY 2019
1. Elimination of progressive portion of tax	-$800	-$1,500	-$1,700	-$1,800	-$1,750	-$1,650
2. Base tax rate changed to 33% of production tax value	$450	$850	$875	$850	$800	$775
3. Limitation of credits for qualified capital expenditures for North Slope	$300	$700	$650	$550	$475	$400
4. Net operating loss credit rate increased to 33%; are transferable and refundable	Minimal revenue impact - see "Impact on Operating Budget"					
5. Gross revenue exclusion for oil production in new units and new or expanded participating areas	$0	-$25	-$25	-$50	-$25	-$50
6. Provision requiring credits be taken over 2 years eliminated [2]	-$250					
7. Amendment to the community revenue sharing fund	$0	$0	$0	$0	$0	$0
8. Credit of $5 per taxable barrel / Sliding scale credit per taxable barrel based on oil price	-$425	-$825	-$775	-$750	-$700	-$675
9. Credit under AS 43.20 for qualified oil and gas industry expenditures	Indeterminate (possibly up to -$25 million annually)					
10. Reduced interest rate for late payments and assessments on most taxes	Indeterminate (possibly up to -$25 million annually, increasing over time)					
11. Removal of 3-mile requirement for frontier basin tax credit	$0	$0	$0	$0	$0	$0
12. Small producer credit extended to 2022	$0	$0	$0	-$25	-$25	-$50
13. 2016 required report to legislature	No fiscal impact					
14. Requirement to consider Joint Interest Billings in audit process	Indeterminate					
15. AIDEA bonding authority to finance oil and gas processing facilities	No Department of Revenue fiscal impact					
Total Revenue Impact	**-$725 to -$775**	**-$800 to -$850**	**-$975 to -$1025**	**-$1200 to -$1250**	**-$1200 to -$1250**	**-$1200 to -$1250**
Impact on Operating Budget of provision requiring credits be taken over 2 years eliminated	-$150					
Impact on Operating Budget of limitation to Qualified Capital Expenditure credit		$150	$150	$150	$150	$150
Impact on Operating Budget of increase in Net Operating Loss credits		-$30	-$30	-$30	-$30	-$30
Total Fiscal Impact - does not include potential revenue impacts from potential increases in production [3]	**-$875 to -$925**	**-$680 to -$730**	**-$855 to -$905**	**-$1080 to -$1130**	**-$1080 to -$1130**	**-$1080 to -$1130**

[1] The impacts listed are based on production and prices as forecasted in our Fall 2012 revenue forecast. The forecasted oil prices are between $109.61 and $118.29.
All data here are estimates; all figures have been rounded to reflect the uncertainty in the estimates.

[2] Provision 6 above, which eliminates the requirement that credits be taken over 2 years is revenue neutral, and simply shifts the tax liability from future years to FY 2014. The total impact of that provision is $400 million, with $250 million taken against tax liability as a revenue impact and $150 million impacting the operating budget. The total fiscal impact consists of both revenue impacts and operating budget impacts of the bill.

[3] NOTE: "Total Fiscal Impact" includes best estimates of both revenue and operating budget impacts. Operating budget impact for FY 2014 represents additional refunded credits due to elimination of the provision requiring that credits be taken over 2 years. Operating budget impact for FY 2015 and beyond represents reduction in refunded credits due to limitation of credits for qualified capital expenditures for North Slope. This amount also includes increases in credit refunds paid through the operating budget for the increase in NOL credit rates.

Production Scenarios

Scenario A:

- New 50 Million barrel field developed by small producer without tax liability
- Peak production = 10,000 bbls/day
- Development costs = $500,000,000
- Qualifies for GRE and NOL

Production Scenarios

Scenario B:

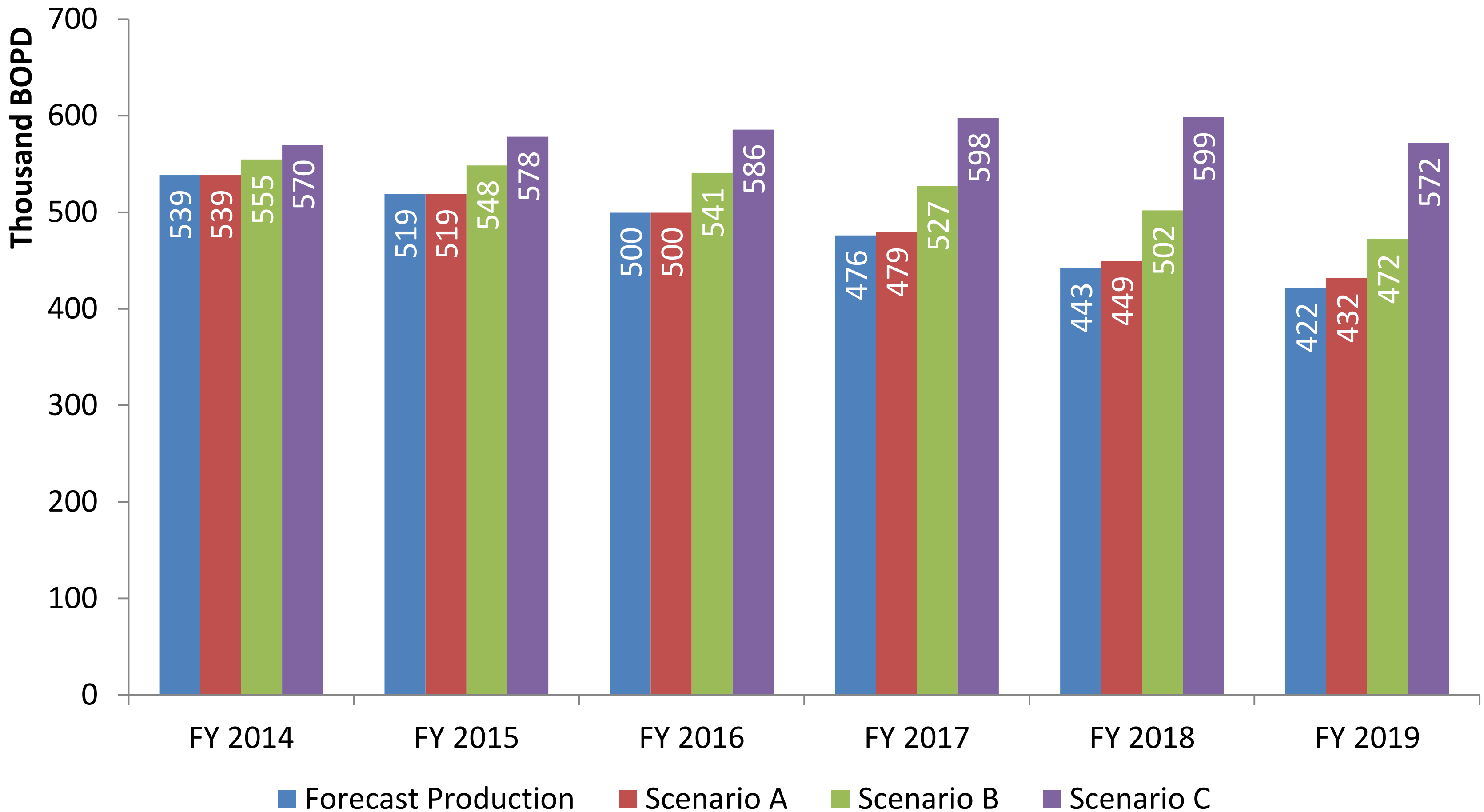
- Operators of existing units add 4 drill rigs to current plans
- Each rig adds 4,000 bbls/day in new production each year
  - Which each then decline at 15% per year
- Does not qualify for GRE

Production Scenarios

Scenario C:

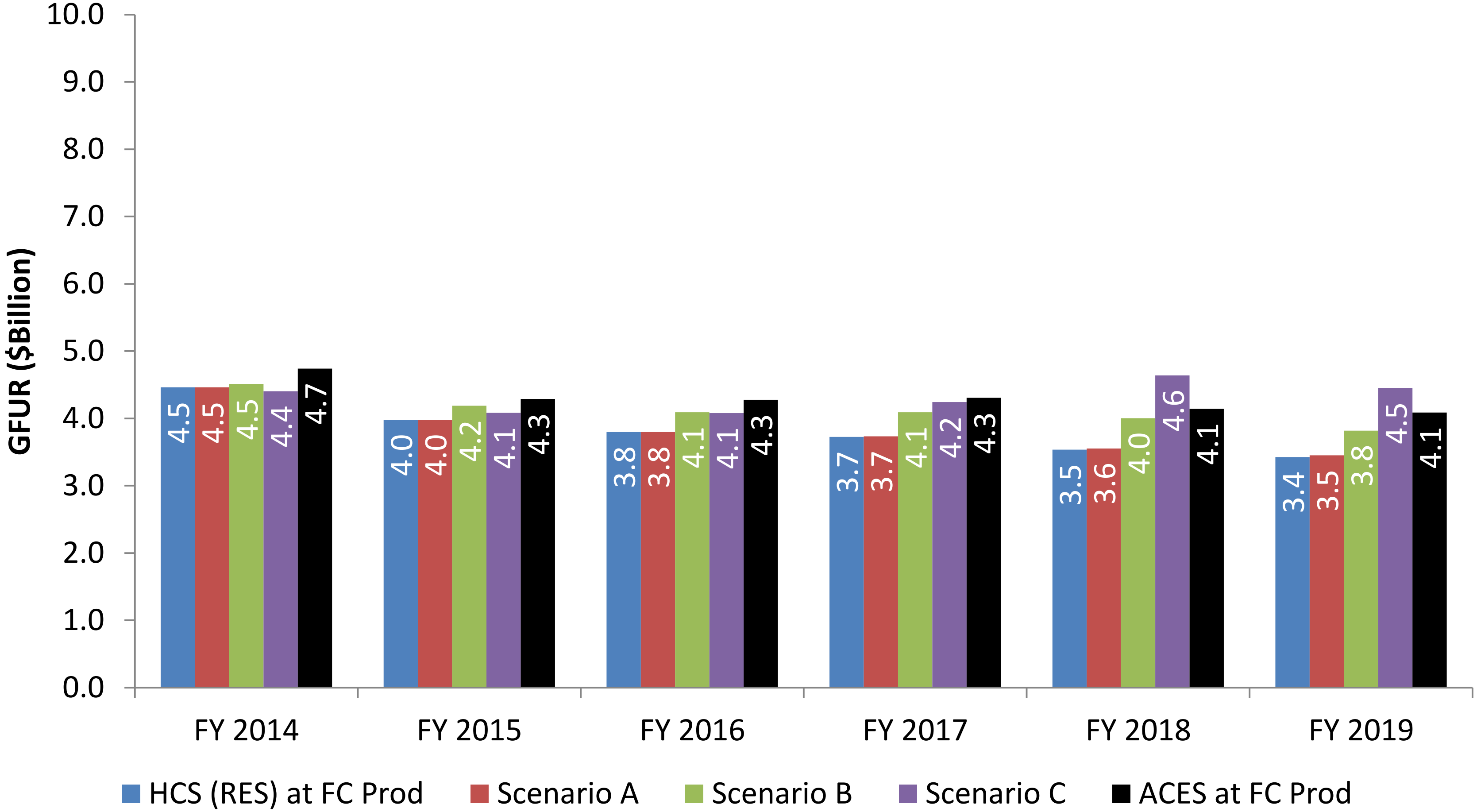
- Operator of existing legacy unit builds new drill pad
- Development cost = $5 billion
- Adds 15,000 bbls/day in 2014 increasing to peak rate of 90,000 bbls/day in 2018
- Does not qualify for GRE

Production Profiles of Production Scenarios



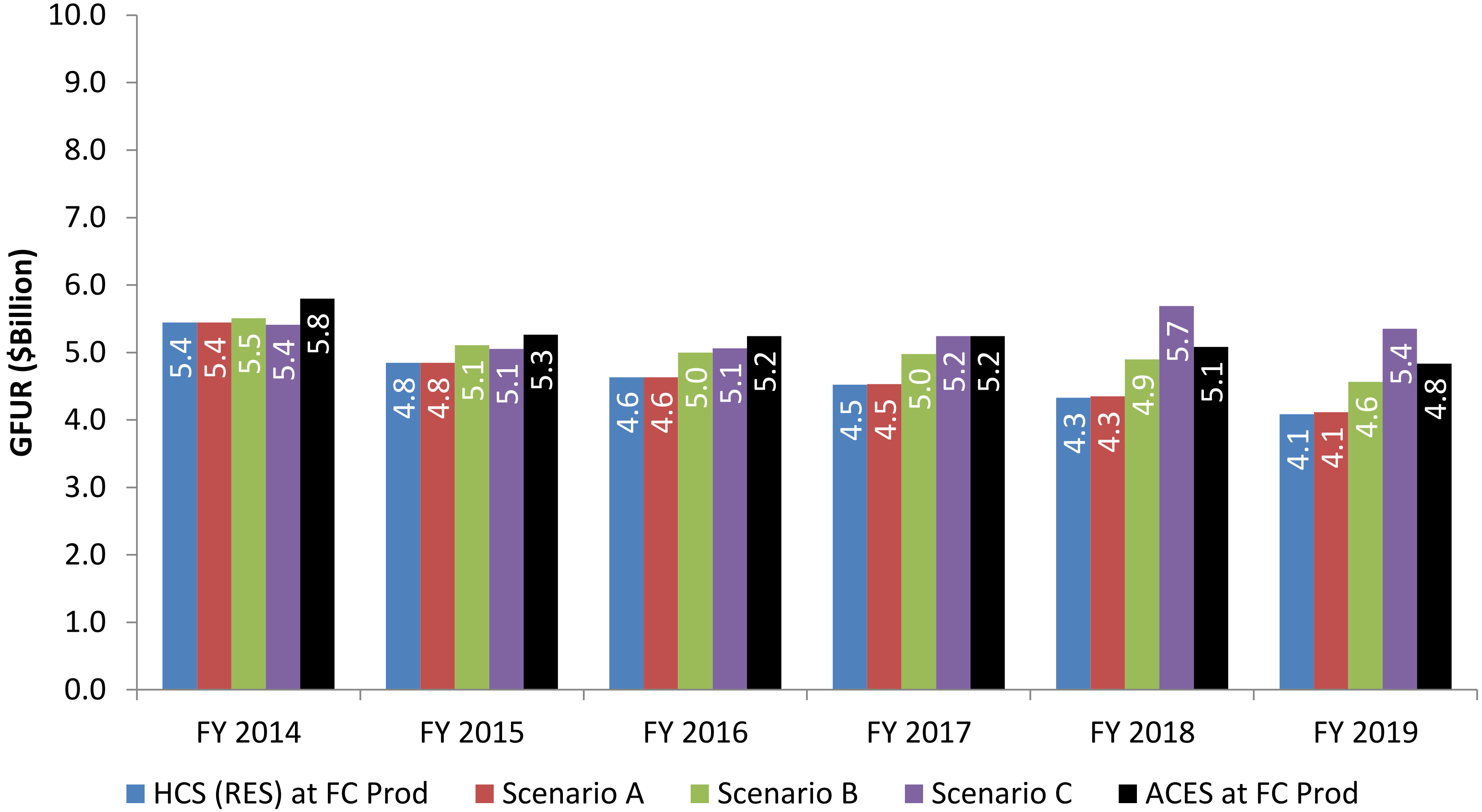
Note: Compares CSSB21(RES) under several production scenarios, to ACES under forecast production.

Projected revenues under production scenarios – at $90 / barrel ANS



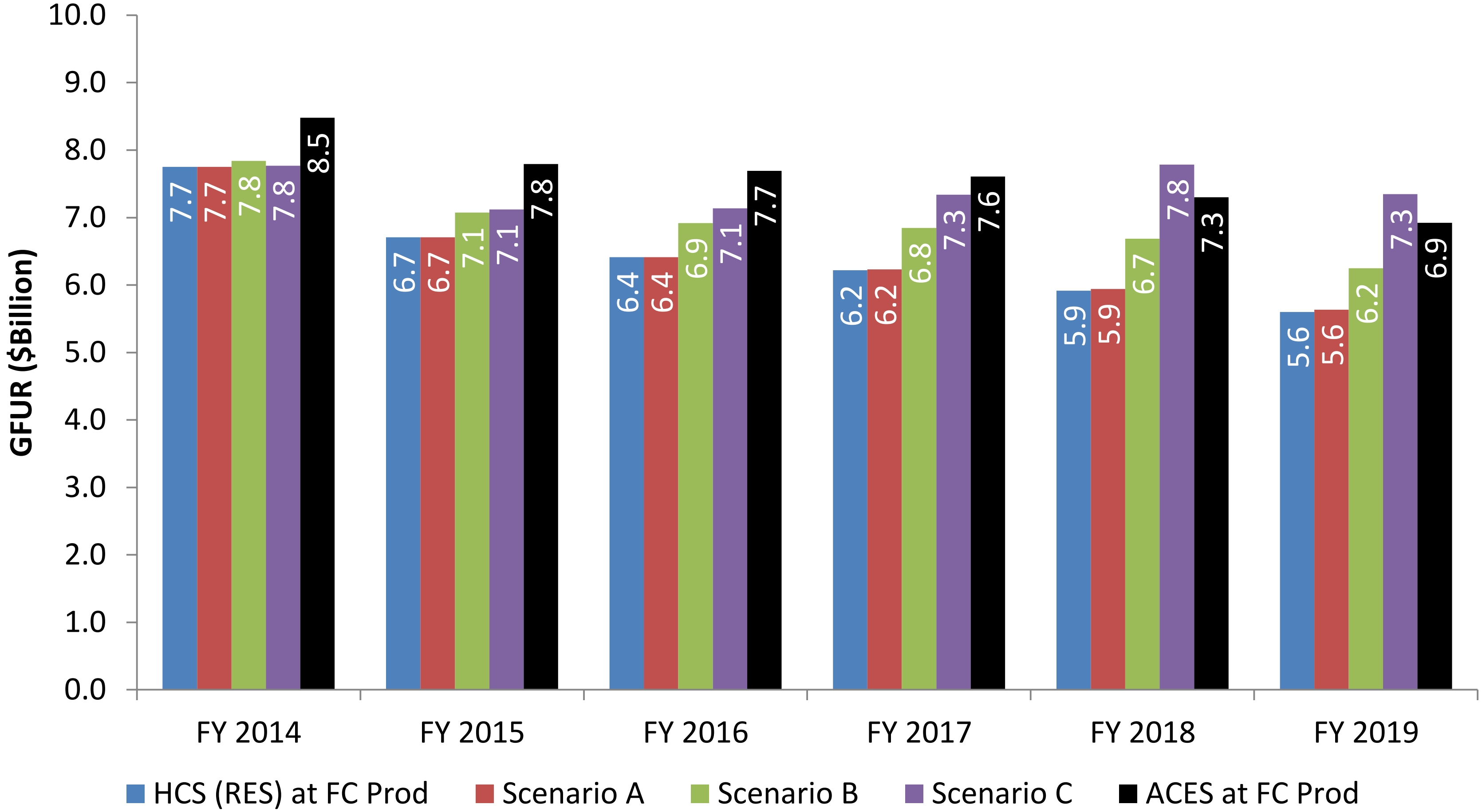
Note: Compares CSSB21(RES) under several production scenarios, to ACES under forecast production.

Projected revenues under production scenarios – at $100 / barrel ANS



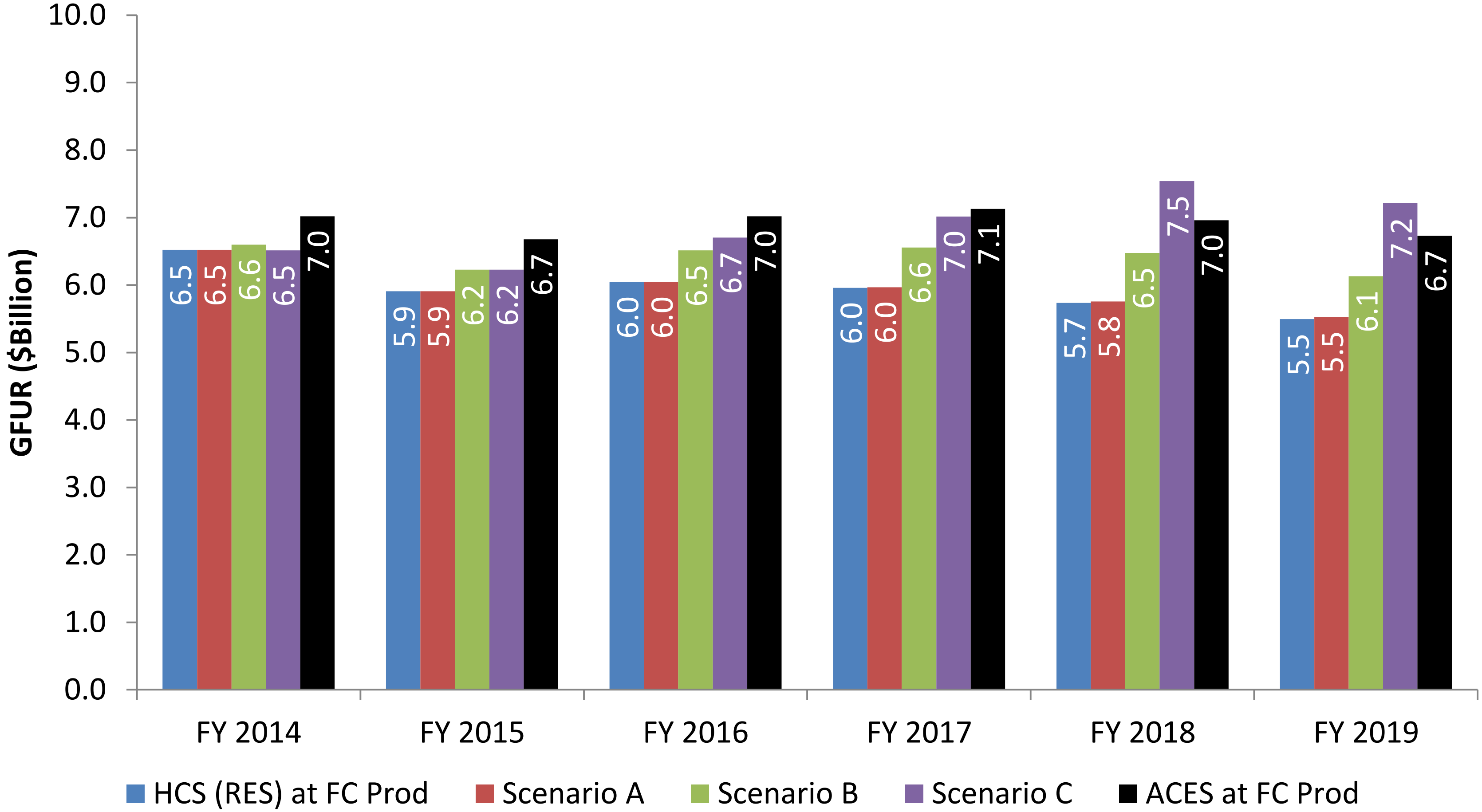
Note: Compares CSSB21(RES) under several production scenarios, to ACES under forecast production.

Projected revenues under production scenarios – at $120 / barrel ANS



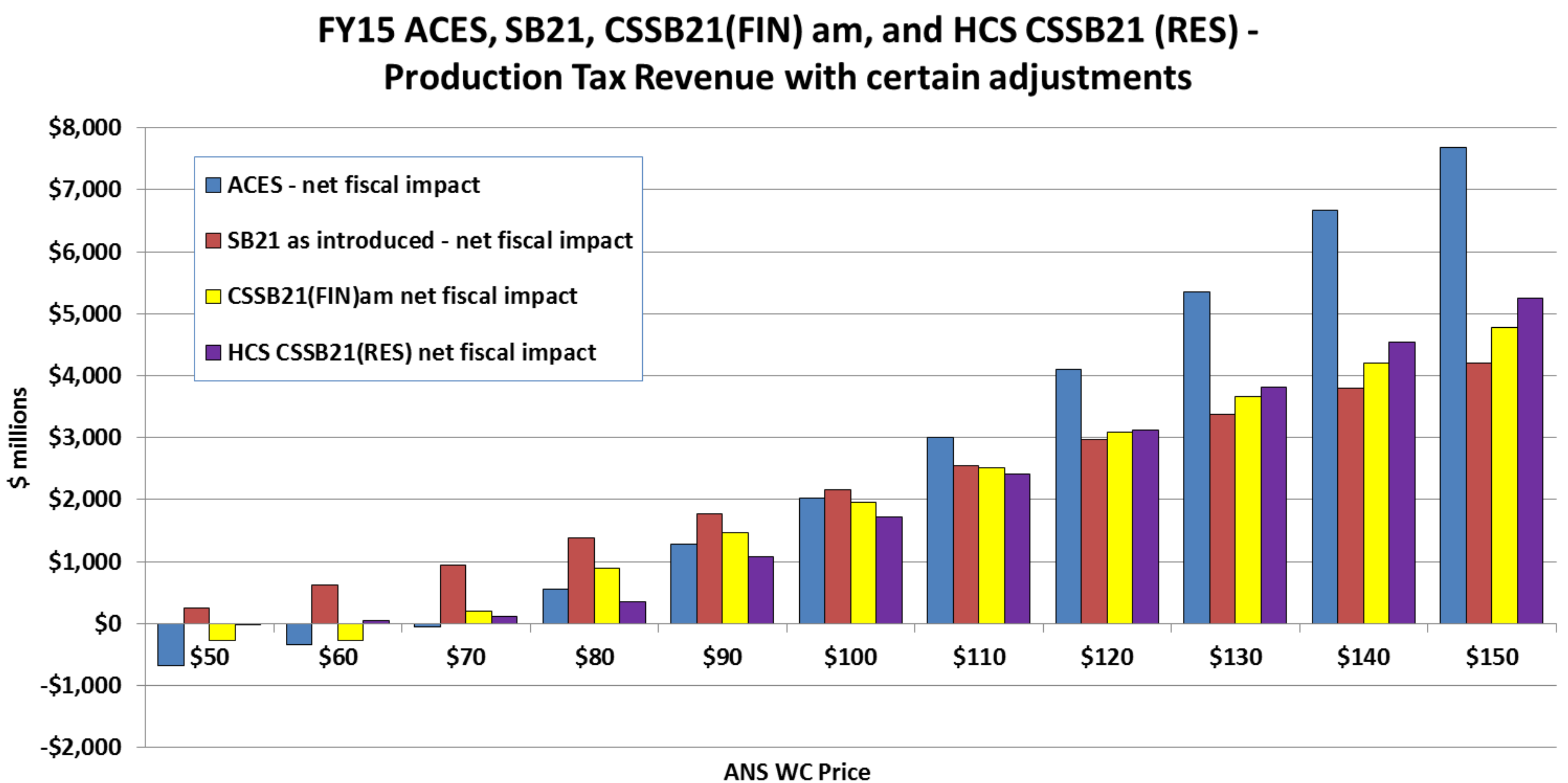
Note: Compares CSSB21(RES) under several production scenarios, to ACES under forecast production.

Projected revenues under production scenarios – at forecast ANS price



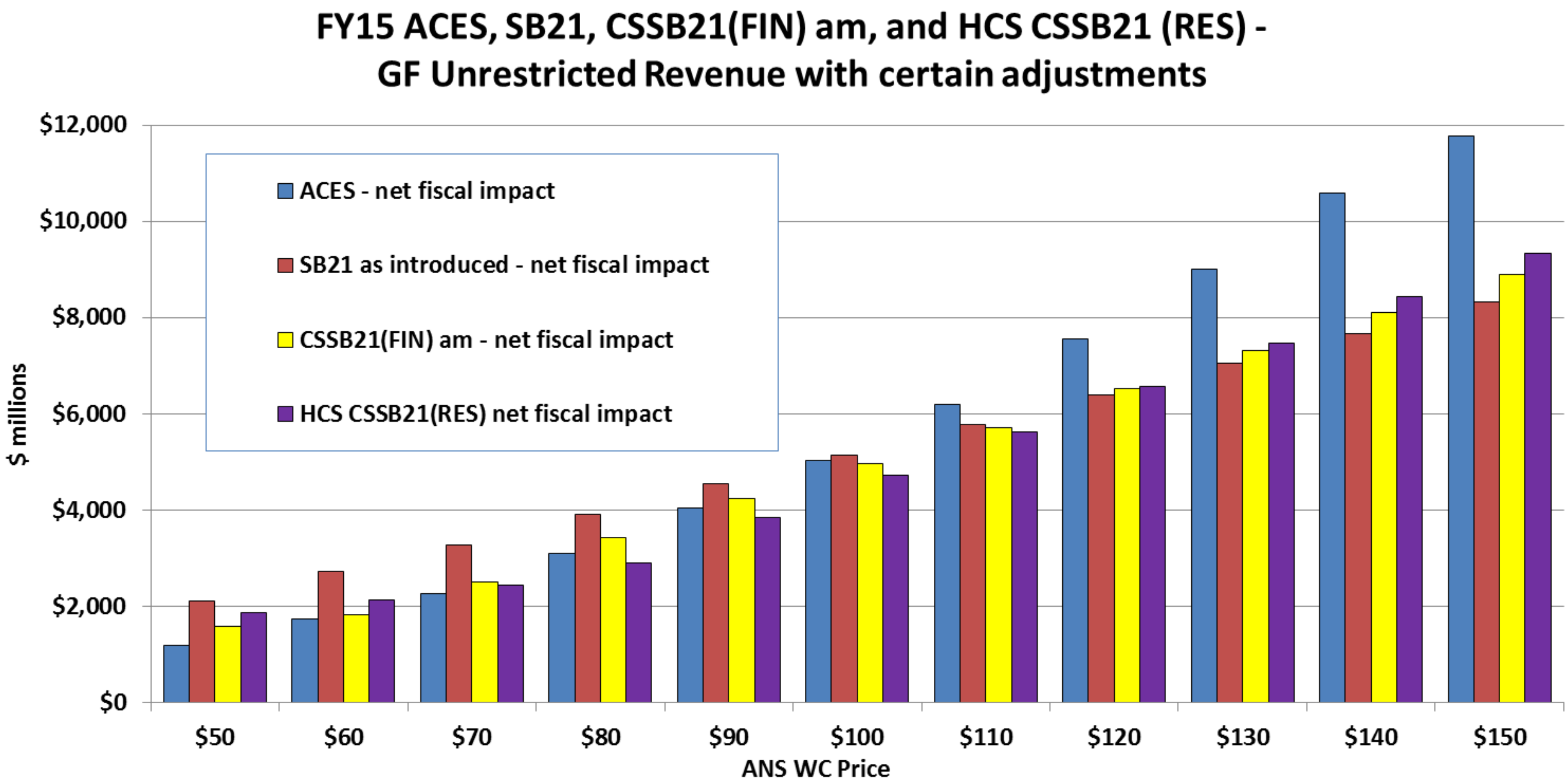
Note: Compares CSSB21(RES) under several production scenarios, to ACES under forecast production.

Production Tax Revenue, less North Slope refunded and carried-forward credits



Source: Fall 2012 forecast model modified for SB21 and CSSB21. Note, "Net fiscal impact" includes forecast revenue, less expected North Slope credit payments. For $50, also includes expected liability for carried forward credits in excess tax liability for major producers. CSSB21(FIN) and HCS CSSB21 (RES) do not include impact of new service industry CIT credit or reduced interest rate for late payments and assessments on most taxes.

General Fund Unrestricted Revenue, less North Slope refunded and carried-forward credits



Source: Fall 2012 forecast model modified for SB21 and CSSB21. Note, "Net fiscal impact" includes forecast revenue, less expected North Slope credit payments. For $50, also includes expected liability for carried forward credits in excess tax liability for major producers. CSSB21(FIN)and HCS CSSB21 (RES) do not include impact of new service industry CIT credit or reduced interest rate for late payments and assessments on most taxes.

Thank You