The Palin-Parnell Administration presents

ACES

Alaska's Clear and Equitable Share

Last Updated: 10-18-07

ACES Is About Investment!

•Investing in Alaska's Oil Development
•Investing Today's Surplus for Tomorrow

Alaska As Investor in Oil Development

- **PPT was a Fundamental Shift in the Relationship between the State and the oil and gas industry**
  - Companies can reduce their tax bill (or receive a State payment) in the amount of 40% to 52 ½% of their capital investments
  - The State of Alaska is the single largest investor in new projects on the North Slope
  - The State is sharing the risks associated with whether these investment decisions pan out

ANS Production Forecast
(Spring 2007)

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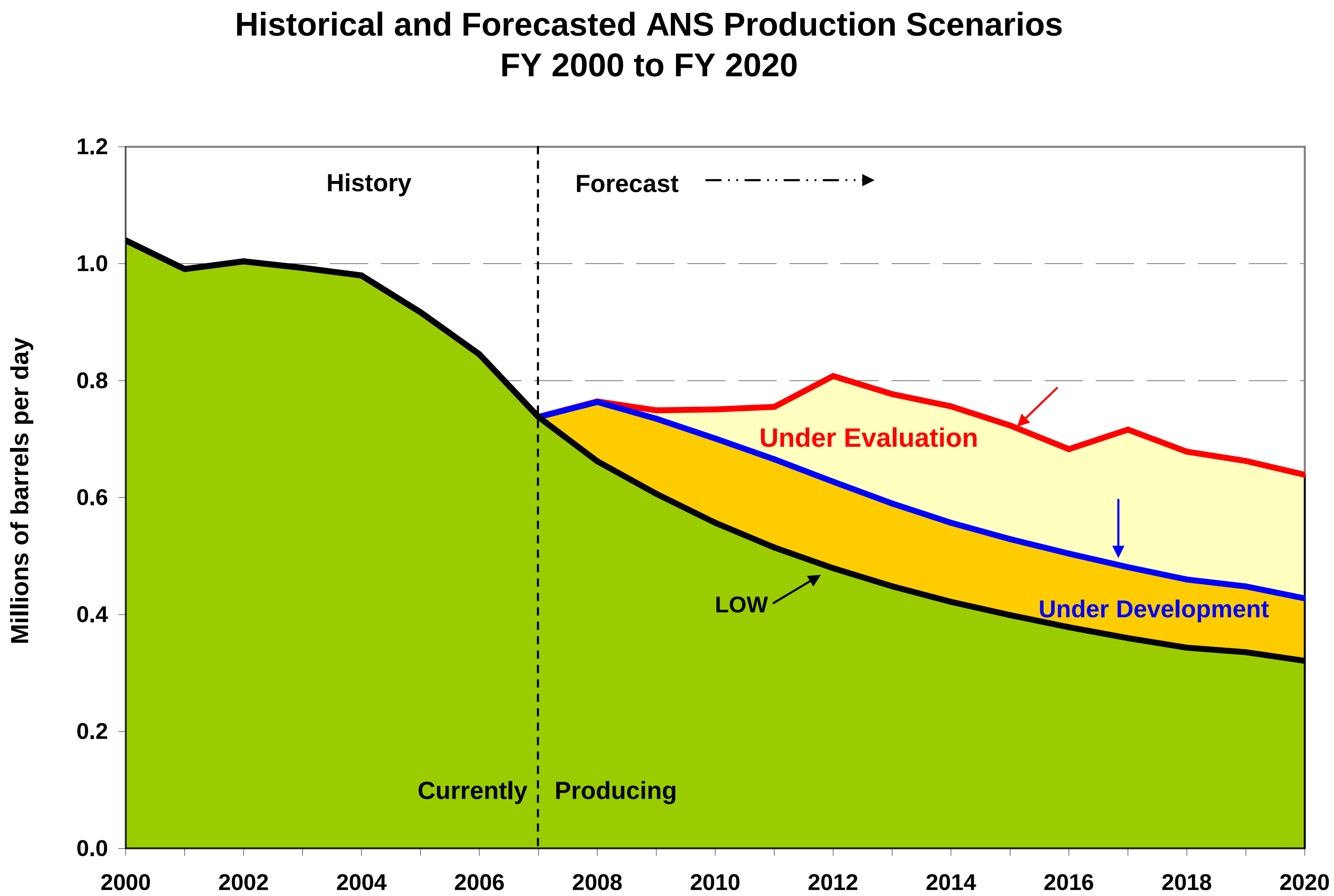
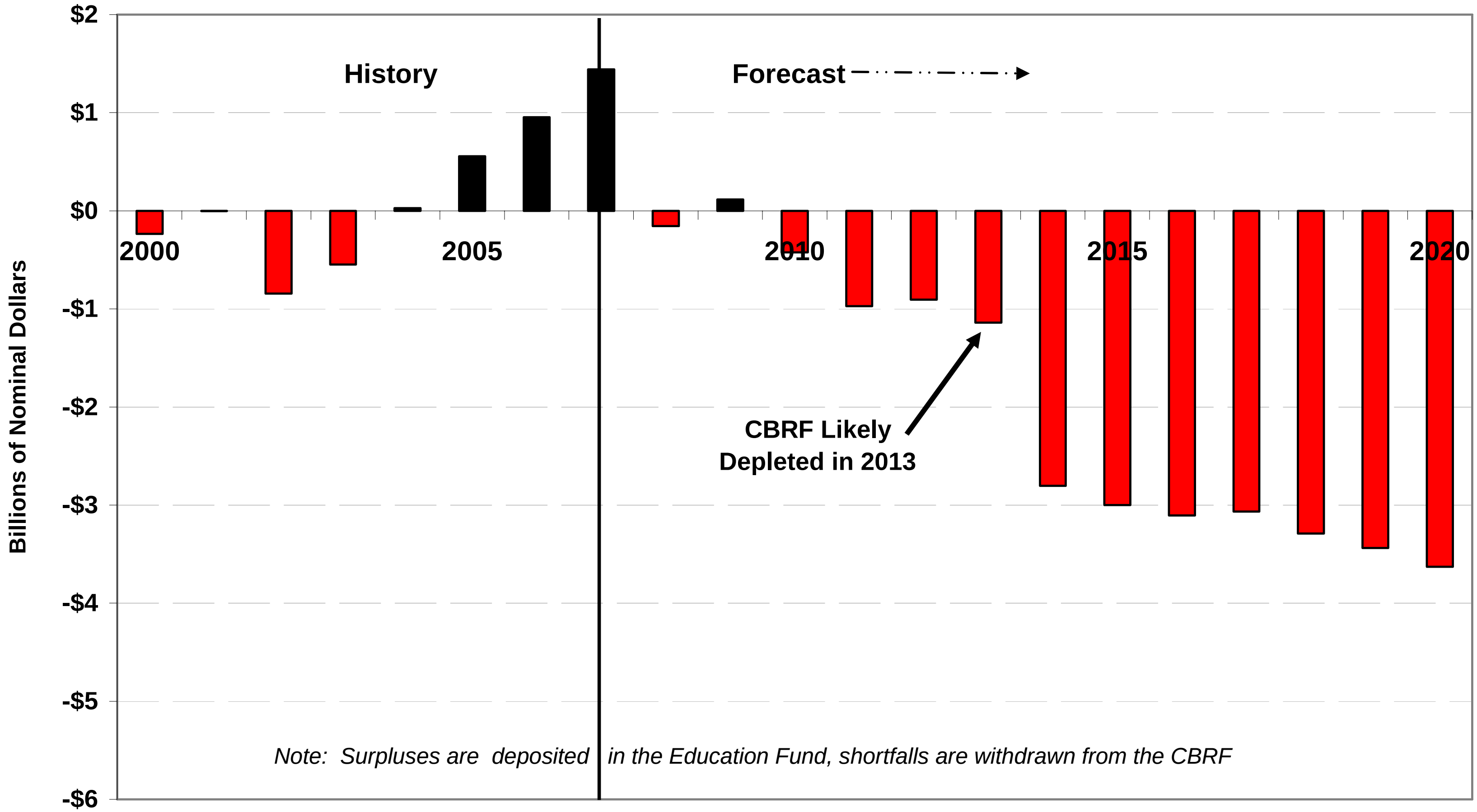


- ACES Seeks a Fair Share of Oil Revenues
  - To Meet the State's Current Fiscal Needs
  - Invest Surplus Revenues to Cover Future Short-falls
    - Protects Economy from Future (Sales or Income) Taxes
    - Provides Stability for Diversification of Alaska's Economy

State Budget Forecast
(Spring 2007)

EXAMPLE
Revenue Shifting



State Budget Forecast
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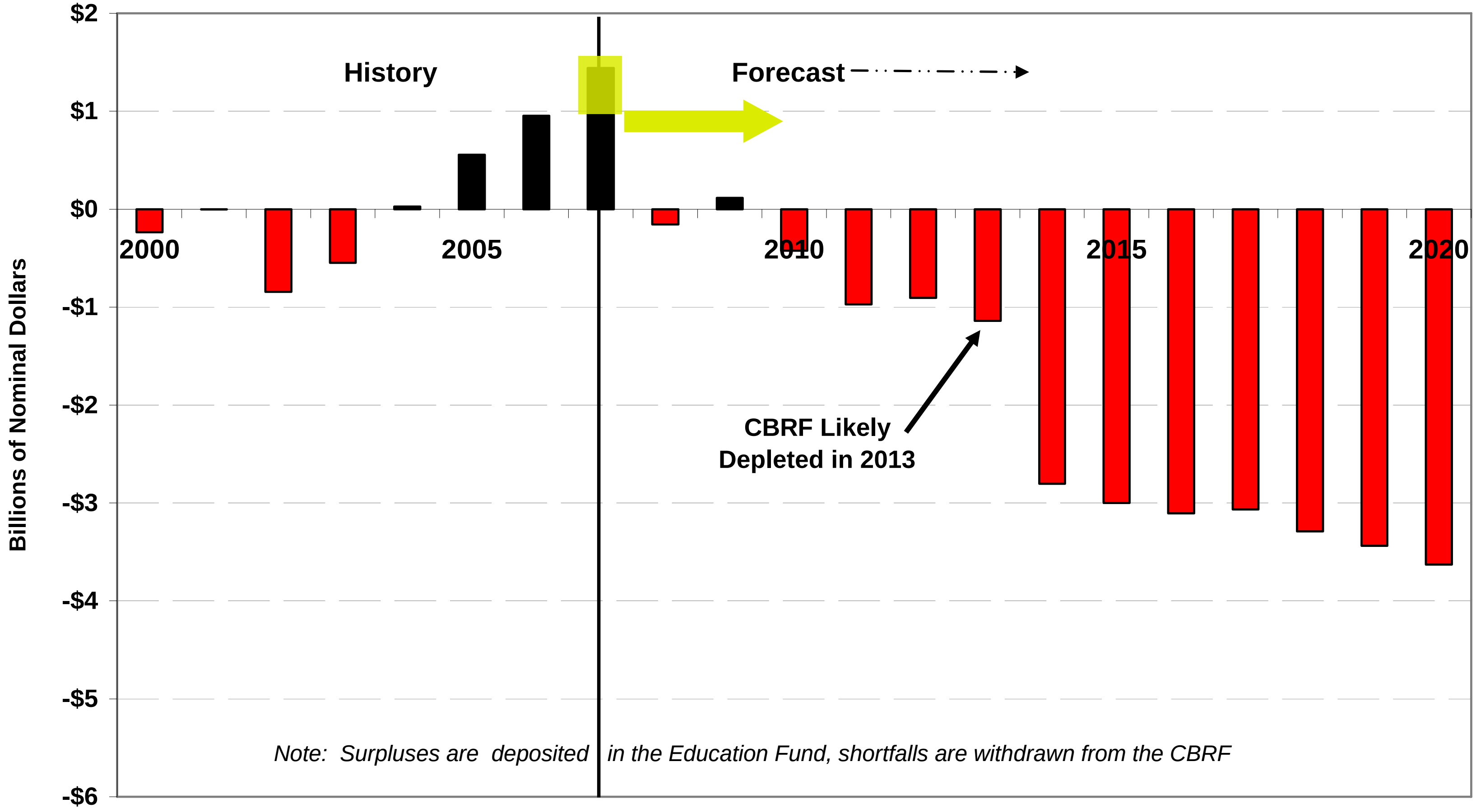
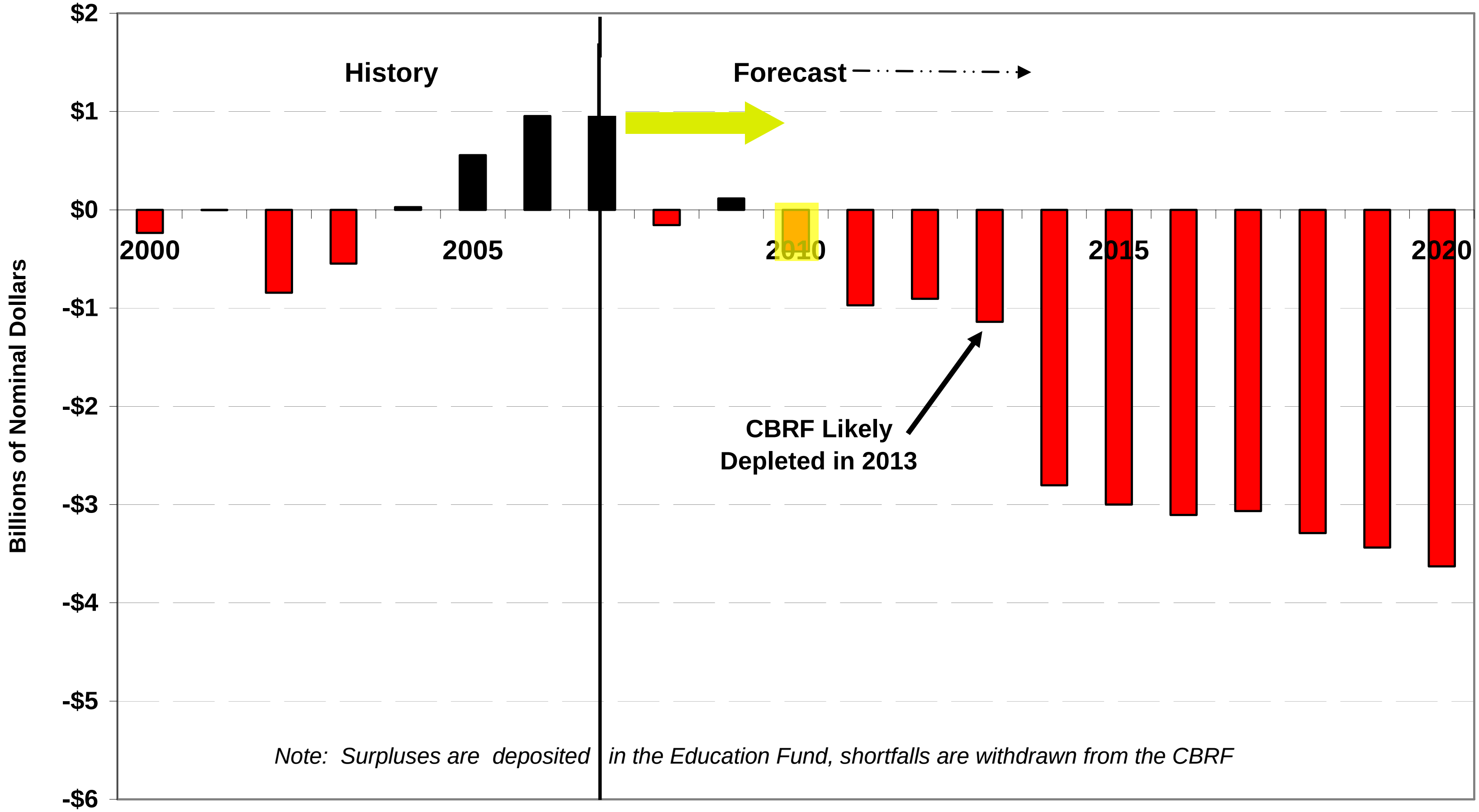


State Budget Forecast
(Spring 2007)

EXAMPLE

Revenue Shifting



Balancing Investment Goals

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- ACES Balances Our Investment Goals
  - Preserves Investment Climate for Oil Development Projects
  - Achieves a Fair Share of Oil Revenues to Maximize Investment in Alaska's Economic Future

Three Days – Three Modules

Friday: Tools to Protect the State

- Information, Auditors, Lease Expenditures, Credit Adjustments

Saturday: Global Competitiveness

- Global Tax Systems, Government Take Measurements and Models, Global Investment Factors, Country Case Studies

Sunday: Investment Climate & Sectional

- Oil Field Economic Models, Cost Story, Tax System Economic “Knobs”, Exploration Incentives, ACES Sectional Overview

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Tools to Protect the State

Tools to Protect the State

- **Information**
  - Data Collection
  - Usability
  - Public disclosure
- **Auditors**
- **Lease expenditures**
  - Definitions
  - Exclusions
- **Credit Adjustments**

Information

Reporting, Use and Sharing

Information Reporting

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PPT provides for minimal reporting of information, primarily on annual basis

- Reporting is not commensurate with other world-wide net-tax jurisdictions
- Makes it difficult for state to understand and respond to dynamic industry needs
- Leads to delay and conflict with taxpayers

ACES Requires Reporting

- Annual statement must be filed by all producers and explorers regardless of whether a tax payment is due
- Expands the list of specific information requirements for returns
- Explorers and producers that have lease expenditures or credits but no production must file with the department, all relevant expenditures, adjustments and credits

Clarifies DOR Authority

- Clarifies that DOR may require a producer, explorer or operator to file monthly reports with information necessary to administer the tax
- ACES provides DOR explicit authority to require producers, explorers and operators to file reports or records needed to forecast state revenue.

Filing Format

- Information currently filed with department is extremely variable and inconsistent. ACES would allow DOR to require electronic filing in a form compatible with the department's information management database

Information Use

Information Management Database

- Electronic reporting form would feed into database where information would be readily available and usable for regulatory purposes, including auditing, forecasting, responding to inquiries, and generating reports
- Will accommodate ELF-based data and will be integrated with the division’s accounting systems
- Will collect on volumes, wells and production, and will include profit-based data, including tracking credits, required under ACES.

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DOR – DNR Information Sharing

- Clarifies DOR authority to share with DNR information contained in tax returns; maintains DOR confidentiality requirements under current law.
- Clarifies DNR authority to share with DOR oil and gas leasing information; maintains DNR confidentiality requirements under current law.
- Allows each agency to be fully informed and be more responsive to dynamic industry needs; helps to facilitate informed policy making and analysis

Guideline Interpretation

- Gives DOR express authority to issue advisory bulletins for information and guidance to producers, explorers and other interested person concerning DOR's interpretation of production tax statutes and regulations.

Statute of Limitations

- Period within which tax must be assessed is extended from 3 to 6 years from date of filing tax return

Public Disclosure

- Expressly allows publication of oil or gas production, production taxes, effective tax rates, gross value at the point of production, transportation costs for oil or gas, qualified capital expenditures, production tax values, lease expenditures and adjustments to them, and tax credits.
- Information must be aggregated among at least three taxpayers; this is similar to the rule applied in other Alaska tax areas.

Information Reporting Standards in Other Countries

Gaffney Cline

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Auditors

Auditors

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- **Currently authorized auditor positions**
  - 18 O&G production tax auditors (Includes 1 Supervisor and 1 O&G Specialist) (DOR)
  - 7 royalty auditor positions (DNR)
- **Currently vacant auditor positions**
  - 5 DOR O&G Auditors
  - 2 DNR royalty auditors

Auditors

- State has been unable to recruit and retain enough qualified oil and gas auditors
- Employee classification system does not allow for targeted pay increases

Auditors

- ACES creates exempt class of Oil and Gas Tax and Royalty auditors
  - Allows DOR to recruit high-level, industry experienced auditors to manage the state production tax audit section
  - Current auditors would have the option of remaining with union or moving to exempt status
  - Allows the state to offer competitive salaries to retain qualified and experienced auditors

Auditors

- **Contract Auditors**
  – ACES also provides funding for contract auditors over the next 4 years to perform special projects, help create audit systems and train new auditors.

Lease Expenditures

Lease Expenditures

Regulatory Definitions

- PPT sets general categories of allowable deductions with specific <u>exclusions</u>
  - Leads to lack of clarity and conflict with taxpayers
- ACES allows clarification through specific regulatory <u>inclusion</u>
  - Clarifies department's authority to set forth allowable costs
  - Avoids misunderstanding over what lease expenditures are allowable

Repeals

- Provisions allowing the department to substitute cost billings under unit operating agreements in place of general standards for allowing lease expenditures
  - 43.55.165(c) and (d)

Lease Expenditures

Exclusions

- Disallows deduction of costs incurred for repair, replacement, or deferred maintenance of facilities and equipment, other than a well, that results in, or is undertaken in response to, an event that results in an unscheduled interruption in production or a release of oil or gas.
  - Encourages proactive maintenance
  - Does not apply to “Acts of God”

Lease Expenditures

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Exclusions

- Clarifies that costs to construct, acquire or operate a refinery or crude oil topping plant are not deductable.
  - Can still deduct, as an operating expense, the cost of diesel used for production

Lease Expenditures

Exclusions

- Disallows deduction of Dismantlement Removal and Restoration (DR&R) expenses
  - DR&R must be done to the satisfaction of the DNR commissioner, a subsidy of DR&R costs creates a potential conflict of state goals.
  - PPT only excluded DR&R expenses attributable to production occurring before April 1, 2006.

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Exclusions

- Disallows tax-exempt entities from obtaining transferable credit certificates under AS 43.55.023, and from transferring production tax credit certificates under AS 43.55.025

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Credit Adjustments

Credit Adjustments

- Eliminates Transitional Investment Expenditure (TIE) Credits
  - Credits are based on expenditures from as far back as 2001 and are not transferable
  - TIE credits are available only to incumbents and not new entrants

Credit Adjustments

- Clarifies that deductions arising from Cook Inlet operations must first be used up in Cook Inlet and may not be shielded by tax ceilings
  - Consistent with existing regulations

Conclusion

- ACES provides Tools to Protect the State