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TESTIMONY OF CRAIG HAYMES
ON PROPOSED CS SB 2001 (JUD)
TO THE ALASKA SENATE FINANCE COMMITTEE
NOVEMBER 8, 2007

INTRODUCTION

Mr. Chairman, members of the committee:

Good afternoon. For the record, my name is Craig Haymes. I am the Alaska Production Manager for ExxonMobil, a position I commenced in January of this year. I reside in Anchorage with my family. I want to thank the committee for the opportunity to express ExxonMobil's views regarding the Administration's proposed tax increase.

I would like to state at the outset that ExxonMobil believes the current PPT tax rate and the increase proposed by the Administration will not result in the additional investment needed to maximize the development of Alaska's resources. When you consider Alaska's resource potential and the current production decline we do not support the tax increase proposed by the Administration.

ExxonMobil has had a presence in Alaska for over 50 years and has been a key player in Alaska's oil industry development, spending and investing over \$20 billion dollars. We are currently active with our co-owners at Prudhoe Bay, Kuparuk, Duck Island, Granite Point and Point Thomson. Our current working interest share of oil production in the State is approximately 150,000 barrels per day and we are the largest owner of

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discovered Alaska gas resources. We look forward to working with Alaska for many years to come.

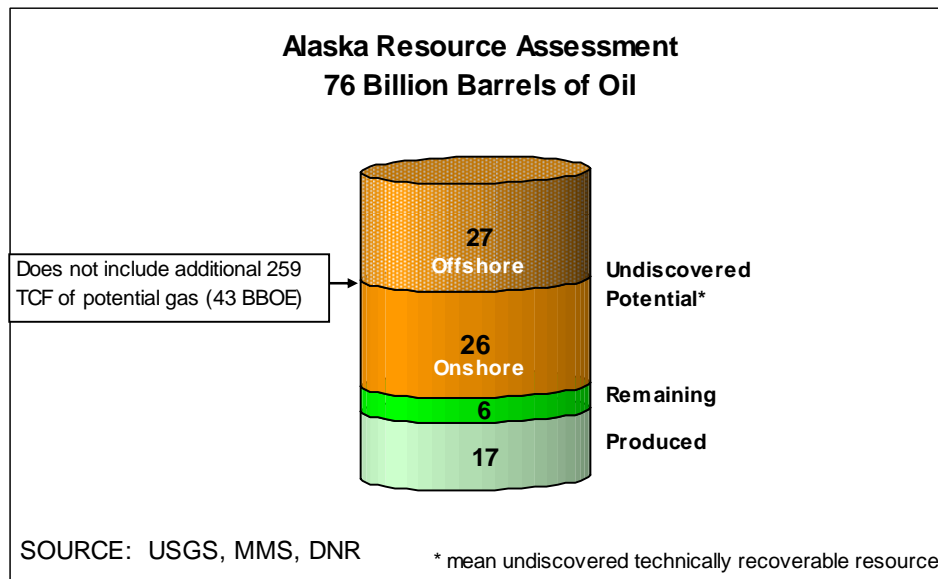
Alaska has significant undiscovered resource potential in both oil and gas; but oil production is declining - today it is one third of the peak of over 2 million barrels per day in 1988. Increasing investment in Alaska is needed to mitigate oil production decline - Government and industry have a common goal – to maximize economic resource development, both oil and gas. Challenging this significant resource potential, and the pace of exploration and development, is Alaska's high cost environment. For any investor, higher costs reduce attractiveness of opportunities.

ExxonMobil believes technology is the lifeblood of the industry and the key to unlocking Alaska's future resources. Historically, the effective application of technology by ExxonMobil and other companies has proven to be successful in reducing costs for the exploration and development of Alaska's resources. Significant long term research and development of technology will be required to realize Alaska's resource potential.

The full development of Alaska's resource potential will require Government, the industry, and the people of Alaska to work together to enhance the development of Alaska's resources. We believe that Alaska needs to create a long-term resource development policy, a policy that will encourage increasing investment needed to mitigate production decline, a policy that recognizes Alaska's high cost and challenging environment, a policy that will encourage the full development of Alaska's oil and gas resources.

ALASKA RESOURCE POTENTIAL IS SIGNIFICANT

According to the US Geological Survey and the US Minerals Management Service, Alaska still has undiscovered technically recoverable resources of over 53 billion barrels of oil. This is in addition to the Department of Natural Resources estimate for known remaining oil resources of 6 billion barrels. When you consider this resource potential, Alaska has only produced one quarter of its oil potential. Alaska still has the potential to produce another 59 billion barrels of oil. Expanding the resource assessment to include gas almost doubles this undiscovered potential on an oil equivalent basis. Alaska has significant oil and gas resources.

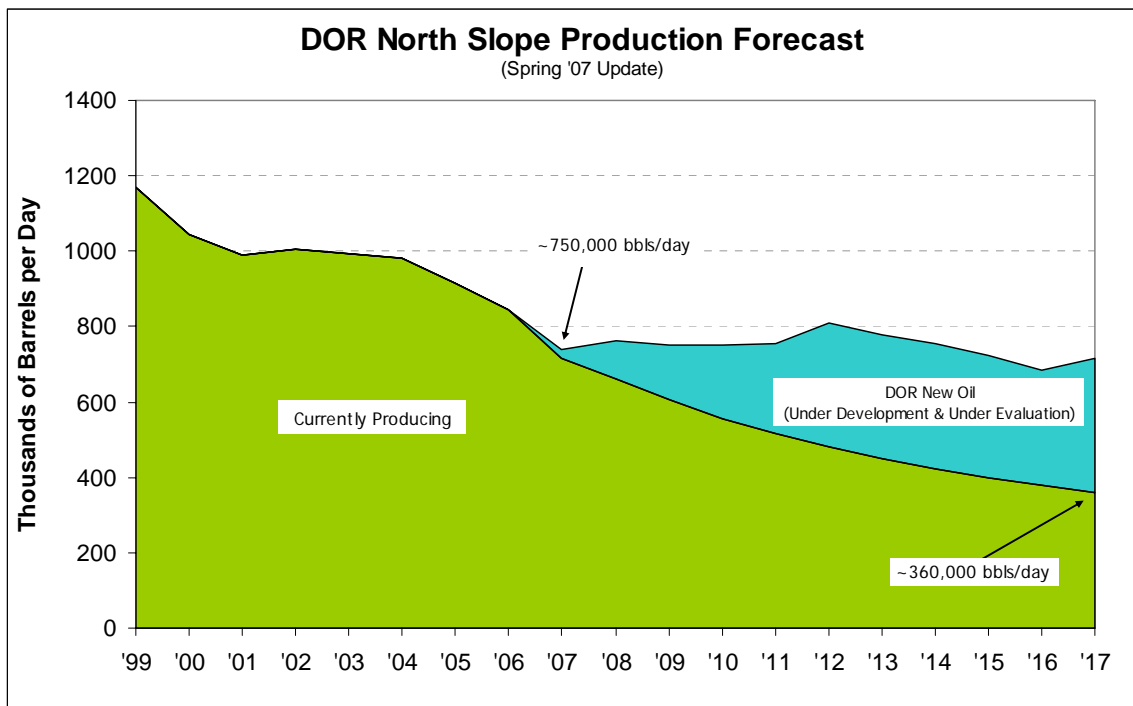


Whilst Alaska’s resource potential is high, the Oil and Gas Journal and Energy Information Administration report that its world ranking of proved reserves has declined from 14th in 1977 to a position closer to 30th today. How can Alaska increase proved reserves; how can we commercialize Alaska’s resource potential?

ALASKA'S FUTURE OIL PRODUCTION

Alaska is currently producing approximately 750,000 barrels of oil per day from the North Slope, one third of its peak production. The Department of Revenue released a production forecast in their Spring Revenue Sources Book. The forecast consists of two main components, as shown in the chart below.

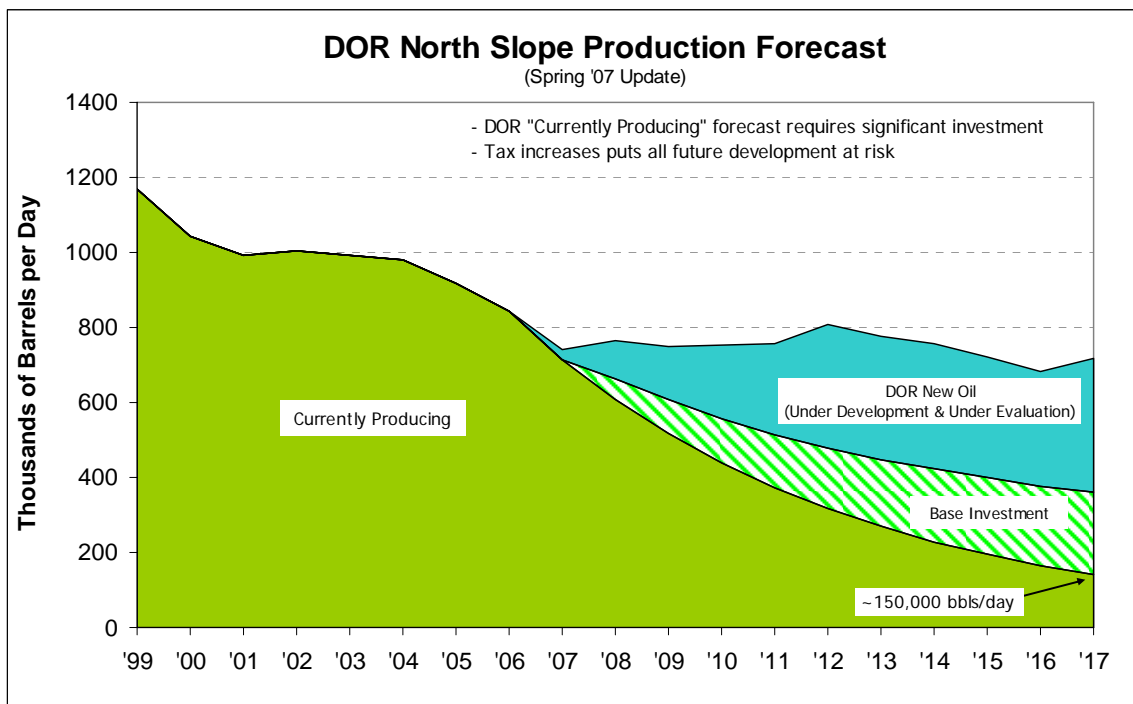
- Current base production (shown as green)
- Future "Under Development and Under Evaluation" production (shown as blue)



As the Department's forecast shows, the current base production is estimated to decline at 9% annually to approximately 360,000 barrels per day by 2017 with continued investment. That is a production level of less than half of today's. The Department's forecast also shows that this production decline will be partially mitigated by the "Under Development and Under Evaluation" production – which includes future investments in areas such as development drilling in non core areas, satellite developments, and enhanced oil recovery from existing fields. Based on this forecast, 50% of future oil

production in 10 years is not even developed or producing today. Considering that most North Slope projects take at least 5-7 years to bring discovered resources to production, near term investment for these activities will be critical to underpin the future of Alaska's oil production.

As I mentioned earlier, the Department of Revenue's forecast is based on a 9% annual decline in Alaska's current base production. However, this decline includes current production enhancement investments at the core Prudhoe Bay, Kuparuk and Alpine areas. The Department's forecast does not highlight that this activity requires investment decisions that are no different from the "Under Development and Under Evaluation" categories. As such, a more accurate representation of the future investment levels required to achieve the Department's forecast is show in the chart below.



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As this chart shows, Alaska's oil production from the North Slope could be as low as 150,000 barrels per day within 10 years without ongoing and increasing investment (assuming 15% decline, which is typical for large oil fields such as Prudhoe Bay). Based on this forecast, within 10 years, 75% of production will come from new investments.

Conservatively, we estimate that at least \$30-40 billion of new investment is required within the next 10 years to achieve the Department of Revenue forecast. This does not include the billions of dollars of additional operating expenditures that would be required to support the developments once they are producing. This is a significant level of future investment and spending.

ALASKA'S TWO LARGEST OIL FIELDS

The two largest oil fields in Alaska - Prudhoe Bay and Kuparuk account for over 70% of the State's North Slope oil production. With continued investment these fields could remain at this portion of production for the next decade. But like any oil field in the world, in order to keep the oil flowing, additional investments are required; such as the historical significant investments at Prudhoe Bay resulting in the installation of water and gas injection, and gas compression facilities.

Currently, the owners spend over \$2 billion dollars annually to optimize and enhance production from Prudhoe Bay and Kuparuk. These spending levels are in addition to the capital investments pursuing new wells, projects, and enhanced oil recovery opportunities. These operating expenditures are essential to mitigate production decline at these significant fields.

Many of today's exploration and development activities are occurring in and around Prudhoe Bay and Kuparuk. As an example, since the year 2000 there have been multiple Prudhoe Bay satellite fields developed (Aurora, Borealis, Midnight Sun, Polaris, and Orion) which are currently contributing over 40,000 B/D of oil production. By leveraging existing Prudhoe Bay and Kuparuk infrastructure, satellite development costs have been significantly reduced. If the major Prudhoe Bay and Kuparuk developments did not exist these satellite fields would not have been economic to develop. As infrastructure on the North Slope expands the economic viability of future satellite developments increases.

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Development drilling in and around Prudhoe Bay and Kuparuk is another example of their critical contribution to Alaska's oil production. For the past seven years over 900 new wells have been drilled in Prudhoe Bay and Kuparuk. The drilling of these new wells has slowed the overall production decline from 12-15% to an estimated 6-9%. Almost 40% of Prudhoe Bay's production today is from these new wells. For the past two years, development drilling at Prudhoe Bay alone has achieved the equivalent development of resources as the important Oooguruk development.

Prudhoe Bay and Kuparuk have the potential to remain key hubs and enablers for the pursuit of new heavy or viscous oil, light oil and gas projects. Encouraging increasing investment at these key fields is as important as encouraging investment in exploration and development of new fields.

EXXONMOBIL'S POSITON ON THE ENACTED PPT

I believe it is important that I clarify ExxonMobil's position on the current PPT.

ExxonMobil did not support the PPT that was enacted last year. As we testified last year, we supported the concept of a net based tax but stated that the proposed 20% tax rate, in the original PPT bill, would not encourage the full development of Alaska's resources. We agreed with the 20% tax rate in order to support the progression of a gas pipeline project.

The PPT that was ultimately enacted increased the high 20% base tax rate to 22.5% with progressivity - more than doubling industry's taxation. When combined with the gross royalties and the high cost environment, it reduces the attractiveness of Alaska's resource developments

There has been a lot of discussion recently on PPT revenues and forecasts, which has been used in part to support the Administration's proposal to increase taxes. PPT has only been in existence for slightly more than one year. The Department of Revenue has not completed its PPT regulations or started any PPT audit. ExxonMobil, like a number of the other producers, met with the Department of Revenue several months ago to discuss ways to help the State better forecast its expected PPT revenues and we are willing to continue those efforts. We are also willing to work with Department of Revenue auditors and our partners to improve the understanding of joint interest billings.

EXXONMOBIL'S POSITION ON THE COMMITTEE SUBSTITUTE

I would now like to offer ExxonMobil's view on the major provisions of the Committee Substitute for Senate Bill 2001 (JUD). In analyzing the Committee Substitute, we found that virtually all of the provisions are simply tax increases or further increases in complexity. In a number of instances, existing statutory provisions of general applicability are being replaced or supplemented to apply only to the PPT. Our comments are presented in the following section-by-section analysis.

Base Tax Rate & Progressivity:

The first section I would like to comment on is Section 18, commencing on line 24 of page 12. I want to start with this section because this section really is the core of the major issues with the proposed Committee Substitute. Section 12 proposes to raise the base PPT tax rate from 22.5% up to 25% and to replace the current progressivity surcharge with a higher one. As I mentioned earlier, ExxonMobil believes the current PPT tax rate will not result in the additional investment needed to maximize the development of Alaska's resources. When you increase the already high base tax rate you reduce the attractiveness of investments. When you then add an additional level of tax as prices increase, the attractiveness of future investments is substantially reduced, which will impact resource recovery and long-term state revenues. We urge this Committee to not adopt Section 18 and to reconsider the current base tax and progressivity element.

Transition Tax Credits:

Section 29, commencing on line 8 of page 19, proposes to eliminate the availability of tax credits for capital expenditures incurred during the five years immediately preceding the enactment of the PPT for producers with existing production. ExxonMobil believes the current transition provision, allowing 100% cost recovery of the prior five years of capital investment, is an important feature of the PPT since it recognizes the long time-frame required for a return on an oil and gas investment to occur.

Conversion to the PPT resulted in a 250% tax increase on the entire industry under today's prices— regardless if you had existing production or were a new entrant. The Legislature recognized this dramatic change to Alaska's production tax regime by including a five-year transition allowance. The transition allowance was put in place to address the impacts on historical investments made under a significantly lower tax rate.

The transition recovery period is also consistent with the State's objective to encourage future capital investment since the producer has to spend \$2 of additional new capital for every \$1 dollar of prior year investment recovered.

We recommend that the Committee reinstate the transition credits originally intended by the Legislature to mitigate the impacts of the conversion to the higher PPT tax and not adopt the propose changes to Section 29.

Additional reporting requirements for exploration tax credits:

Paragraph (B) of Section 36, beginning on line 18 on page 24 would require that in order to qualify for an exploration tax credit an explorer has to agree in writing to release highly proprietary information; such as seismic, well geophysical surveys and core samples.

Providing this type of proprietary information is not the norm throughout North America. Releasing key competitive and high value information would be a concern to any explorer. It often takes decades to progress from exploration to production phase. The release of proprietary and competitive information before an asset is producing is not appropriate so early in the phase of a future development. This would decrease the value of the exploration credit and may discourage an explorer from applying for the credit.

In addition, providing this type of information to the State would increase the amount of investment required of an explorer. Core samples, for example, are very costly. Providing one-third of the core material to the State would not only add to the costs of exploring, but would be physically challenging and potentially damaging to the integrity of the entire core. The same constraints also apply to other very limited gas, fluid, and solid samples collected by downhole devices like sidewall core guns or formation samplers. Cores can always be made available for state review upon request and analyses of downhole-collected samples are already routinely provided to the state.

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The confidentiality provisions are also of serious concern. The proposal provides confidentiality protection for only ten years for most of the seismic data required to be produced, and for only two years on the rest. Seismic data typically has a shelf life in exploration areas (especially frontier areas) much longer than 10 years. More troubling is that under the proposal, an operator is required to provide a copy of check shot surveys or vertical seismic profiles. These geophysical surveys are expensive and are intended solely for seismic interpretation. They are key pieces of proprietary data. They have an indefinite shelf life and can be used to tie seismic of any vintage, new or old, to wells. Yet under the administration's proposal, such information would be classified as "well data", and afforded only a 2-year period of confidentiality.

These requirements go against the basic principle that if a party is willing to spend money and take risks to collect information critical to the success of a project, that party should be entitled to maintain the confidentiality, value and integrity of that information for the life of the project. Exploration is a long-term effort, requiring the allocation of finite resources across a spectrum of competing opportunities over a number of years to successfully identify those opportunities that will bring financial returns to the explorer. Alaska's exploration tax credits will improve the attractiveness of future programs, but the value of these credits will be undermined by tying them to complying with onerous requirements. ExxonMobil urges this Committee to remove the onerous requirements outlined in Section 36.

Information Requests:

The Administration is proposing that they require additional information to assist in the administration of the PPT and improve their ability to forecast future revenues for PPT. We recognize conversion to the net based PPT structure has increased the information needs for the Department of Revenue, and ExxonMobil is willing to help the Department meet its needs. We believe that additional information requirements beyond that currently submitted with our tax filings needs to be carefully considered. There must be some limitations and reasonableness standards established.

For example, subsection (f) of Section 45 of the Committee Substitute, commencing on line 16 of page 31, lists items a producer, explorer or an operator would be required to provide the Department on a monthly basis. Items (1)-(7) are clear, however item (8) on line 29 would obligate the producer, explorer or operator to provide any "other records and information the department considers necessary. . ." - every month. This language is ambiguous on what standards would be applied and how a taxpayer would comply. Taxpayers would be required to provide whatever the Department's auditors consider "necessary". We believe item (8) is too open-ended and should be deleted.

Paragraph (5) of Section 46, commencing on line 29 of page 32, would require a producer, explorer or operator to file whatever reports and copies of records the Department considers "necessary" to forecast PPT revenues. We believe this language in paragraph (5) is too vague. While recognizing the Department's need for forward looking data we believe the tax statutes should specify the required information.

Penalties:

Section 44, commencing on line 25 of page 30 proposes to allow the Department of Revenue to assess a penalty of up to \$1,000 per day for each day a "tax return" is not filed when required. Paragraph (7) of Section 46 commencing on line 12 of page 33, proposes to allow the Department of Revenue to assess a \$1,000 penalty per day for each "report, statement or other document" the Department "considers necessary" to forecast state revenue that a producer, explorer or operator fails to provide when the Department deems necessary. Both amendments are excessive and unnecessary.

Under current law, there are already significant penalties to ensure taxpayer compliance with filing tax returns and providing other information to the Department. Such penalties include a 5% penalty per month (25% maximum) for failure to file a tax return and a similar penalty for failure to pay the full amount of tax when due, among others. The Department also has significant powers to compel production of information, including holding investigations, issuing subpoenas and taking depositions. For these reasons, ExxonMobil believes the proposed penalties are unnecessary.

In addition, the proposed penalties are unreasonably excessive. A \$1,000 per day penalty for each "report, statement or other document" that is not produced "at the time required" by the Department can quickly result in amounts disproportionate to the nature or severity of the offense. For example, a single one page document that a taxpayer did not provide six months earlier because the taxpayer reasonably believed it was already addressed in another submission, would subject the taxpayer to a penalty close to \$200,000. The \$1,000 per day penalties should be removed.

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Section 49, commencing on line 3 of page 34, would establish punitive understatement penalties which will likely lead to delayed audit assessments and increased audit disputes. Substantial underpayment penalties already exist under Alaska law.

ExxonMobil is required by law and its internal policies and controls to file complete, accurate and timely tax returns. Establishing such punitive measures would create greater uncertainty, undermine positive working relationships between the Government and industry, and add complexity to the administration of the PPT. The proposed amendment is unnecessary. Section 49 should not be adopted.

Production of Taxpayer Information:

Paragraph (6) of Section 46, commencing on line 7 of page 33, proposes that taxpayers with at least 100,000 barrels a day production must report their gross sales revenues and expenses. ExxonMobil opposes this amendment.

ExxonMobil discloses financial information as required by the Securities and Exchange Commission (SEC), and other regulatory bodies. SEC rules do not require that ExxonMobil's Alaskan affiliates be separately disclosed in our periodic financial statements. Additionally, ExxonMobil's affiliates which operate principally in Alaska have no outstanding publicly traded debt, and therefore ExxonMobil is not required to separately report the earnings of those subsidiaries.

Being a global company, ExxonMobil does not disclose U.S. earnings on a state-by-state basis because such information could be used by our competitors to discern information regarding our operating costs, investments, contract terms, or other competitive information.

While Alaskan operating results are monitored internally, since these results are calculated to measure operating performance rather than for financial reporting, they are not in conformance with Generally Accepted Accounting Principles (GAAP) requirements for external disclosure. The fact that our internal results are recorded for a purpose other than financial reporting and are not kept in accordance with GAAP means they are not strictly comparable to the Alaskan numbers that our competitors

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publicly report and they are competitively sensitive information, the disclosure of which would be harmful to ExxonMobil.

ExxonMobil understands the Alaska Legislature's desire to set a tax framework that provides the state of Alaska with a fair return on the development of its energy resources. We remain prepared to work with the state to improve the state's ability to forecast PPT revenues. Given the confidentiality provided to taxpayers, ExxonMobil has and will continue to provide the Department of Revenue with all data required to successfully administer PPT. We urge this Committee to not adopt this proposed amendment.

Statute Of Limitations

In lines 25-27 on page 34, Section 50 of the Committee Substitute proposes a new six-year statute of limitations for the PPT only. Currently, the statute of limitations for the PPT, as well as all other taxes under Title 43, is three years. The Department has not started a single PPT audit and increasing the statute of limitations can only delay audits and increase administrative costs. We fail to understand why this amendment is needed. Historically, most companies generally extend the audit deadlines as appropriate when requested by the Department of Revenue.

The purpose of a tax statute of limitations is to establish a reasonable time within which an audit must be brought so that the records, documents, and recollections of witnesses are not lost by the time the claims are finally raised. It also provides some limitation on the amount of interest that could accrue on any underpayment claimed in an audit.

Extending the statute of limitations to six years could result in audits not being completed for six years, when they may have otherwise been done more quickly, increasing the interest risk to taxpayers.

The present three-year statute of limitations has worked well for all the taxes, including the production tax. We believe lines 25-27 on page 34 should be deleted.

Actual Pipeline Transportation Costs:

Sections 52 and 53, commencing on line 16 of page 36 and continuing through line 4 on page 37, is proposing that the Department of Revenue can substitute, at anytime, its determination of "reasonable" costs of transportation for the taxpayer's actual pipeline tariffs or marine transportation costs.

Currently, a taxpayer's actual transportation costs are used to determine the taxable value of the taxpayer's oil unless the Department establishes all three conditions set forth in AS 43.55.150(a). The proposed amendment would ease that standard to allow actual costs to be disregarded by an auditor by simply asserting the actual costs do not meet the auditor's view of "reasonableness", despite the existence of valid third party contracts or federally regulated tariffs.

The proposed amendment represents another instance where the Department of Revenue is asking the Legislature to allow it to selectively determine what costs it deems reasonable versus allowing the deduction of valid costs properly incurred. The proposed changes to AS.43.55.150(a) in Section 52 of the Committee Substitute should not be adopted.

In the Committee Substitute, Section 150(b) would be amended, commencing on line 27 of page 36, to provide that only tariff rates that "have been adjudicated as just and reasonable" by the RCA or other regulatory agency are considered prima facia reasonable. This could unduly restrict rates that will be considered as reasonable costs. In certain instances, tariff rates may be properly filed, as currently allowed, and

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not challenged by any party or allowed to go into effect on an interim basis. In such case there may not be a final "adjudication" of the reasonableness of the rates when they go into effect. If challenged, a period of time may pass before the rates are finally determined to be just and reasonable. Any such final determination by the relevant regulatory agency will address any revision in the rate that may be required, including for prior periods. These matters should be left to the determination of the regulatory agencies with responsibility for such matters. There is no need to further condition how these rates will be used to determine allowable transportation costs. Subsection 150(b) should not be revised as proposed.

Lease Expenditures Determined Under Department Regulation:

Paragraph (B) of Section 57, commencing on line 16 of page 40, is proposing that the Department of Revenue can determine, by regulation, which costs should be allowed as qualified lease expenditures, despite the fact that the Legislature has already clearly identified under AS 43.55.165(e) those costs that cannot be allowed. The proposed language, "allowed by the department by regulation" is different than the normal regulation granting authority used elsewhere in the PPT statute. It is this difference that raises concern.

Generally, regulations are promulgated to interpret or apply a law. The language "as determined under regulation" or "as may be established by regulation" used elsewhere in the PPT statutes convey the Legislature's intent to have the Department interpret or apply the Legislature's policy. The proposed amendment, however, could be the basis for the Department to constrict or disregard certain PPT statutory provisions which the Legislature adopted to establish what costs qualify as lease expenditures. For example, the proposed amendment could lead to the Department adopting its own standards as to what constitutes an ordinary and necessary business expense, despite the AS 43.55.165(j)(2) requirement that the established federal rules determine what costs can be used. The proposed amendment could also cause the Department to ignore those costs allowed by AS 43.55.165(b) as direct costs. Authorizing a regulation that could provide the basis for the Department to limit or exclude costs otherwise allowed under other sections of the PPT would create an unpredictable tax law. The phrase "allowed by the department by regulation" appearing on line 16 of page 40 should be removed.

Lease Expenditures Where Upstream Activities Occurring:

The language appearing on line 6 of page 41 is proposing to disallow property taxes for properties on which no exploration, development or production is taking place. Oil and gas property taxes are generally imposed on tangible personal property upon ground disturbance. The PPT currently requires qualified lease expenditures be costs upstream from the point of production.

The proposed amendment would allow an auditor to disallow upstream costs if no actual "production is taking place" on the property, regardless if the costs are ordinary and necessary for the prudent and safe operation of the upstream facilities. For example, this proposal would disallow costs associated with a warehouse storing emergency response equipment or a facility housing North Slope workers located on a property that has no production, exploration and development occurring at the time, despite such costs being essential for oil production on the North Slope. We believe the proposed language on lines 6 and 7 of page 41 is ambiguous, will lead to increased audit disputes, and should be deleted.

Location of Lease Expenditures:

The proposed deletion of the bracketed language commencing on line 5 of page 42 would limit qualified lease expenditures to only those incurred within the producer's or explorer's leases or properties. Limiting lease expenditures to those incurred physically within the producer's or explorer's lease or property would reduce the attractiveness of development and exploration activities. Given the extreme arctic conditions and limited construction capabilities on the North Slope, necessary equipment and production modules are often fabricated elsewhere for delivery to the Slope. Drilling rigs, unavailable in Alaska but needed for exploration and well work, are imported from the Lower 48. These are ordinary and necessary costs required for the operation of the North Slope production facilities and exploration activities, both essential for the future development of Alaska's resources.

Disallowing such costs would reduce the attractiveness of future development and exploration projects and diminish the likelihood of those projects being funded. The proposed deletion of the bracketed language on lines 5 through 11 of page 42 should not be adopted.

Costs Arising From Noncompliance With Lease/Permit/License Terms:

Paragraph (6) of Section 59, commencing on line 22 of page 42, is proposing to disallow expenditures that result from failure to comply with lease obligations or permit requirements. Such a limitation raises a number of concerns. In certain instances, a lease term is a matter of contract between the lease holder and the state as a contracting party. The contract typically will spell out the means for redress by the parties and the consequence of a "breach" of the contract. This should provide adequate remedies for the state to ensure contract obligations are met. In the case of a federal permit, there likely will be specific provisions that address the consequence of any permit non-compliance and what the permit holder must do to remedy the problem. These provisions are adequate to address any concerns for the state.

There is no recognition in the proposed language of the severity of the non-compliance, or the efforts by the leaseholder or permit holder to comply. This is different from an act of "fraud" or "willful misconduct" contained in the current law. This is complicated by the uncertainty in the proposed language on how such a determination will be made.

Particularly if the state is a party to a lease, there should be a separate determination whether there has been non-compliance with the lease term or permit and the remedy should be as spelled out in the contract (or as allowed by existing law). The language "...or failure to comply with an obligation under a lease, permit, or license issued by the state or federal government" is unnecessary.

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Costs Arising From An Unscheduled Interruption Of Production/Improper Maintenance:

Paragraph (19) starting on line 22 of page 44 proposes to disallow costs incurred in response to a failure, problem or event that results in an unscheduled interruption of or reduction in the oil or gas production, is a result of "improper maintenance" or is undertaken in response to or is otherwise associated with an unpermitted release of a hazardous substance or gas, unless caused by a "super' force majeure.

We believe the language of this proposed revision is ambiguous and will lead to additional audit exceptions. What constitutes a "failure, problem or event" or "improper maintenance" and under what standards would any of those be determined? Costs associated with any temporary, unforeseen shutdown or minor interruptions, regardless how minor, could be disallowed by an auditor despite such "event" arising despite otherwise prudent and necessary business operations. In addition, given the safeguards already existing in the current PPT and the proposed amendment in paragraph (6) disallowing costs arising from violations of law, we believe paragraph (19) is unnecessary.

During the formation of the PPT legislation, the Legislature, upon the recommendation of Dr. Pedro van Meurs, adopted a flat 30¢ per barrel exclusion from what would otherwise be a producer's capital portion of its lease expenditures. The flat 30¢ per barrel exclusion provides an objective floor for maintenance cost and avoids the problems of case-by-case decisions. The 30¢ exclusion applies every year regardless if there is a triggering event or not. Adopting the proposed amendment, while leaving the flat 30¢ per barrel exclusion in the law, would result in a double disallowance of the same costs. We do not support Paragraph (19), and believe it should be removed.

Disallowance/Limitation Of Costs Associated With Refineries/Crude Oil Topping Plants:

Paragraph (20) starting on line 21 of page 45 proposes to disallow and limit costs associated with refineries and crude oil topping plants, essential components of producing oil from the North Slope.

Currently, the State of Alaska and the federal government require North Slope operators to convert to ultra low sulfur diesel to operate all North Slope motor vehicles and off road equipment. The North Slope producers are considering a modification to the existing Kuparuk crude oil topping plant to produce the required ultra low sulfur diesel. The proposed amendment reduces the economic viability of a potential crude oil topping plant modification. Without a modification to the existing crude oil topping plant, it will be necessary to haul low sulfur diesel up to the slope, requiring up to 50 trucks per day. This could potentially increase environmental impacts, including increased exhaust emissions and potential spill risks from truck accidents. Costs associated with the topping plant should therefore be recoverable just as the costs to truck diesel to the Slope would be.

The Administration's proposed amendment encourages a less optimum solution for the oil industry and the State. Paragraph (20) would increase operating costs while complicating business operations and should not be adopted.

Disclosure Of Tax Information:

Section 63 of the Committee Substitute, commencing on line 27 of page 47, proposes the publication of certain proprietary tax information when such information is aggregated among three or more producers or explorers. We understand the Administration's and Legislature's desire to obtain information necessary for the development of the PPT net tax framework to provide the State of Alaska with a fair return on the development of its energy resources. We also support the Administration's goal of transparency. Aggregation of information from three companies dramatically increases the likelihood that competitors, including competitors whose information is being aggregated, will be able to determine individual company proprietary information.

Such information could be used by competitors to discern information regarding operating costs, investments, contract terms, or other competitive information. This risk of individual company proprietary information being ascertained by competitors could also create conflicts between the proposed amendment and federal protections provided in the Federal Trade Secrets Act and federal Anti Trust laws. The proposed amendment may also violate the Alaska Constitution's right of privacy, equal protection and unlawful takings of commercially sensitive data protections.

The Legislature should ensure taxpayer information remains confidential.

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Elimination Of Requirement For Joint Interest Billings As Starting Point For Audits:

Section 65 of the Committee Substitute, appearing on line 4 of page 49, proposes to repeal AS 43.55.165(c) and (d). The effect of repealing those sections would be to remove the joint interest billings as the starting point for audits. As a non-operator at Prudhoe Bay, Kuparuk, Duck Island and Granite Point we fail to see how not using this information is to anyone's advantage.

In a field's joint operating agreement the working interest owners have specified what costs an operator can bill to the co-owners. All of a producer's deductible lease expenditures are in accordance with the monthly cost data charged by the field operator to its co-owners. Each year the operator is subjected to very detailed audits by the other owners to ensure compliance with the limitations in those agreements. ExxonMobil currently spends over 100 staff weeks each year auditing operator joint billings to ensure we are not charged any inappropriate costs.

The use of these joint interest billings as the foundation of allowable business expenses would provide greater predictability and eliminate the need for the State to re-audit the same materials. Using joint interest billings will reduce disputes over appropriate deductions as well as the State's and the producers' administrative and audit costs. AS 43.55.165(c) and (d) should not be repealed.

FISCAL PREDICTABILITY IS IMPORTANT

I would now like to address another important element of the business environment for any investor - fiscal predictability. Our investments are capital intensive and typically evaluated over timeframes of decades. A change in the fiscal regime has a direct impact on how we view predictability of the Alaskan fiscal environment. This directly impacts how we evaluate on a risked basis future investment decisions.

The Administration's proposed tax increase would represent the third significant change to Alaska's fiscal terms in the past three years. As a result of these changes, the industry tax burden has increased by approximately 350% at today's prices. With the current Committee Substitute proposal the tax increase would be approximately 470% under today's prices. Changing the fiscal environment for capital intensive projects, that take many years to generate a return, can only reduce the attractiveness of future investments. For every well or project not progressed, additional production and State revenues are forgone. Alaska needs to double its current investment levels in the near term to achieve the Department of Revenues production forecast. Increasing taxes will not encourage the increasing investment needed.

ExxonMobil expects to be involved in Alaska for many years to come. The policies established today, and in the future, will impact the attractiveness of potential projects and the future of Alaska.

ALASKA NEEDS A LONG-TERM RESOURCE DEVELOPMENT POLICY

ExxonMobil believes a long-term sustainable resource development policy is required to enable Alaska to maximize its oil and gas resource. We believe there are many factors that need to be considered. I hope that key points addressed in my testimony are considered:

- Alaska has significant resource potential, but it is in a high cost environment
- Oil production is one third of its peak, yet we have only produced one fourth of the oil resource potential. The gas resource potential is equal to oil.
- In 10 years, 75% of Alaska's future oil production needs over \$30-40 billion of new investments - investments that are needed sooner than 10 years.
- Prudhoe Bay and Kuparuk are the "hub" of the North Slope, they
 - Represent 70% of North Slope oil production for the next 10+ years
 - Can provide significant new production in the near term
 - Can be the backbone for future exploration and economic developments, whether it is existing production, future light oil, heavy oil, or gas
 - Need increasing investments to achieve their potential

We propose a collaborative approach to develop a sustainable long term resource policy that will encourage the needed increasing investments and build the future of Alaska for many generations to come. We believe that a long term resource policy should consider:

- Characterization of state-wide resource potential
- Identification of key issues challenging exploration and development
- Key factors that impact resource value, such as research and technology, exploration and development costs, regulatory and environmental considerations, land access
- Establishment of goals and measurement of progress
- Fiscal policy that will encourage development of remaining resources
- Regular meetings with industry and agency representatives

ExxonMobil looks forward to working with the Administration, the legislators, industry and the people of Alaska in the future pursuit and development of its oil and gas resources.

Thank you again Mister Chairman for the opportunity to testify today.

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