

# **The Cost Story**

**Alaska Department of Revenue  
October 21, 2007**

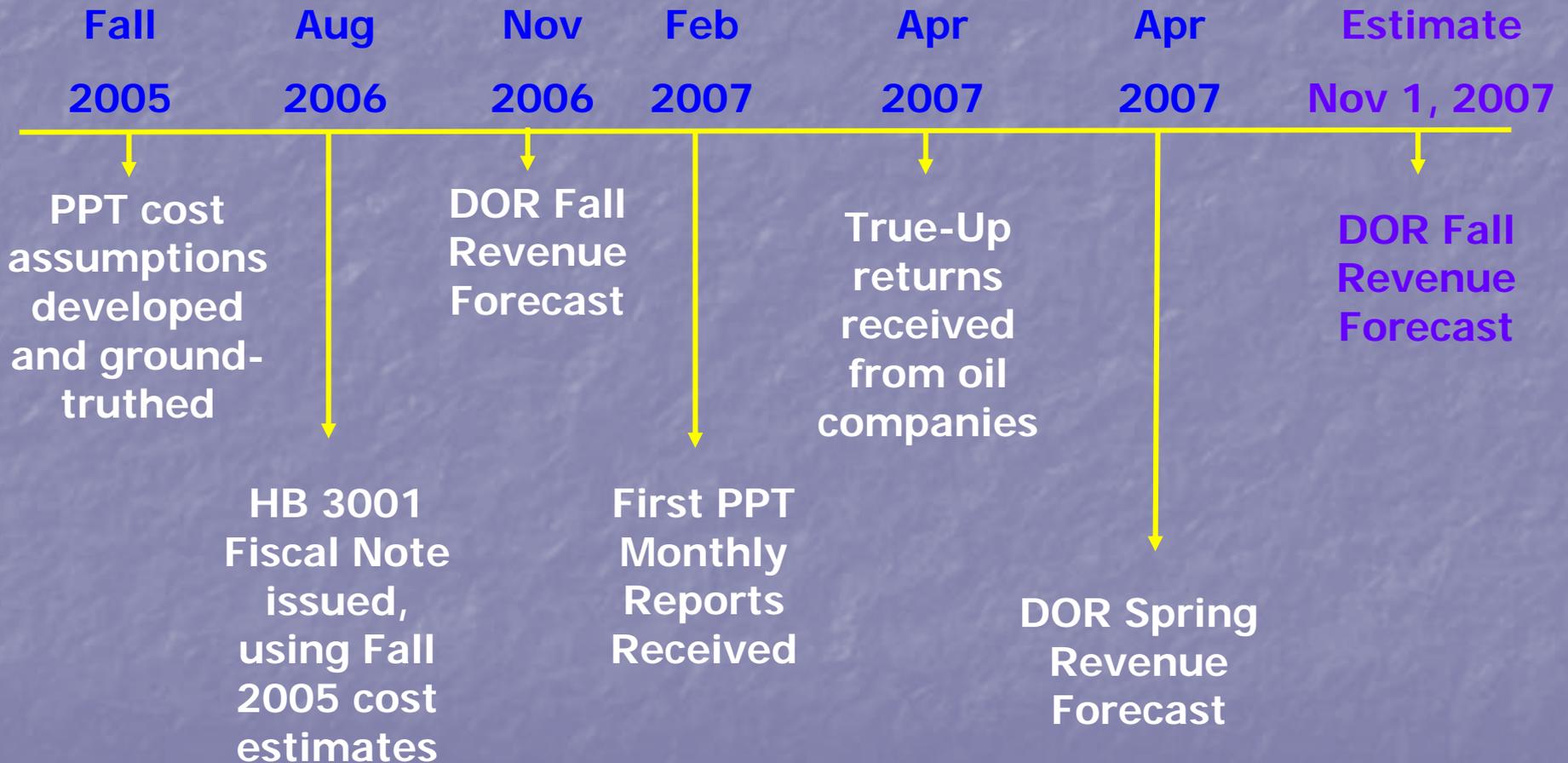
# Production Tax Revenue Involves Three Unknowns

- Production
- Price
- Costs – Operating  
and Capital

# 2006 PPT Costs

- **Cost Assumption Sources:**
  - Historical data from 2002 - 2004
  - Published reports from consulting firms
- **Consultations with industry**
- **Reviewed by Legislature's Consultants**

# PPT Forecast Timeline

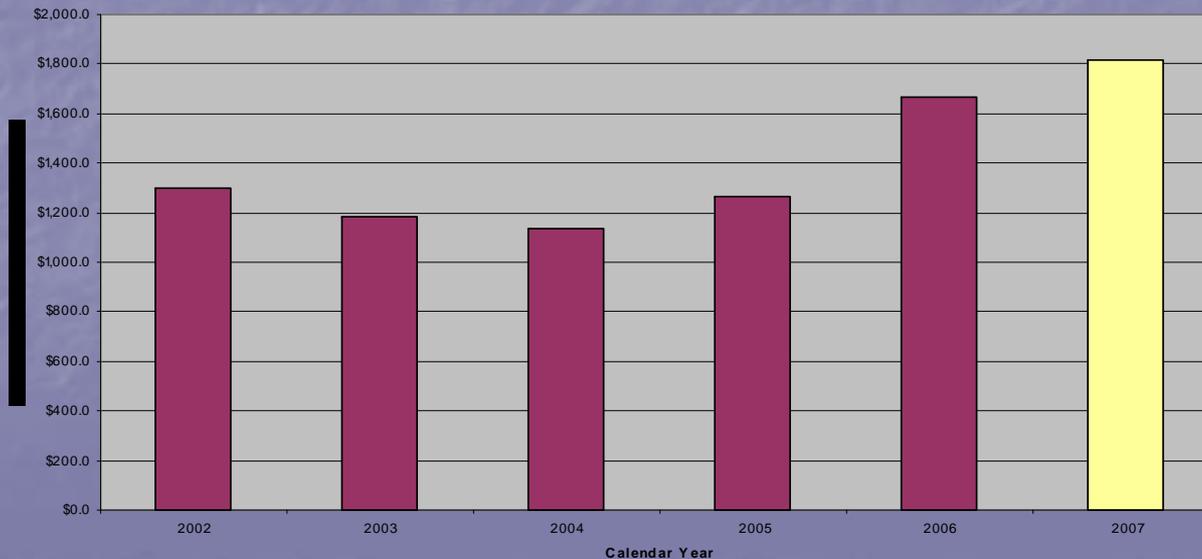


# How our Assumptions Changed

- Costs have been adjusted based on actual PPT tax return filings
- Costs are now expressed in nominal dollars (have inflation component)
- Additional data has become available on which to base future costs

# Capital Spending as Reported in PPT Tax Returns, March 2007 and 2007 Forecast

Calendar Year	Capital Spending in Alaska in \$millions nominal
2002	\$1,296.7
2003	\$1,186.8
2004	\$1,136.9
2005	\$1,268.0
2006	\$1,665.3
2007	\$1,817.0



# Cost Forecasts

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>		
Production (barrels per day)	802,000	764,000
Operating costs (\$millions)	\$1,076	\$2,160
Capital costs (\$millions)	\$1,052	\$1,900
<b>Total Costs</b>	<b>\$2,128</b>	<b>\$4,060</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

# Current Revenue Forecasts

Actual

DOR Forecast

Estimated Production Tax Payments (in \$millions)				Three Month Tax Calculation	
July 2007	\$184.5			Average Price	\$72.96
Aug 2007	\$213.5			Less Transport	-\$6.44
Sep 2007	\$166.7			Wellhead Value	\$66.52
Total Payments - Quarter	\$564.7			Times production	0.702407
<i>less estimated credits &amp; refunds</i>	<i>-\$50.0</i>			Times days in Qtr	92
<b>Total Quarter</b>	<b>\$514.7</b>			Total prod value	\$4,298.4
				Less Royalty	-\$537.3
<b>Production</b>	mmBbls/day			Total value at Pt. of Prod.	\$3,761.1
July 2007	0.724636				
Aug 2007	0.724564			Capex/bbl	\$7.80
Sep 2007	0.658021			Opex/bbl	\$8.35
Average	0.702407			Total Capex	\$513.0
				Total Opex	\$525.0
<b>Price</b>	\$/bbl ANS WC			Production Tax Value	\$2,723.1
July 2007	\$69.11				
Aug 2007	\$75.93			Tax Rate	22.5%
Sep 2007	\$73.83			Tax b/f credits & progressivity	\$612.7
Average	\$72.96			Progressivity tax rate	2.0%
				Progressivity Surcharge	\$54.5
				Tax before credits	\$667.2
				Capex credits	\$153.9
				<b>Total after credits</b>	<b>\$513.3</b>
				Percent Error	0.3%

# Tools for Forecasting Costs

- \*Require cost reporting (current and forecast)
- \*Monitor data submitted to DOR
- \*Monitor data submitted to other agencies (e.g. plans of development)
- Monitor publicly available information (e.g. economic indicators, labor and material costs)

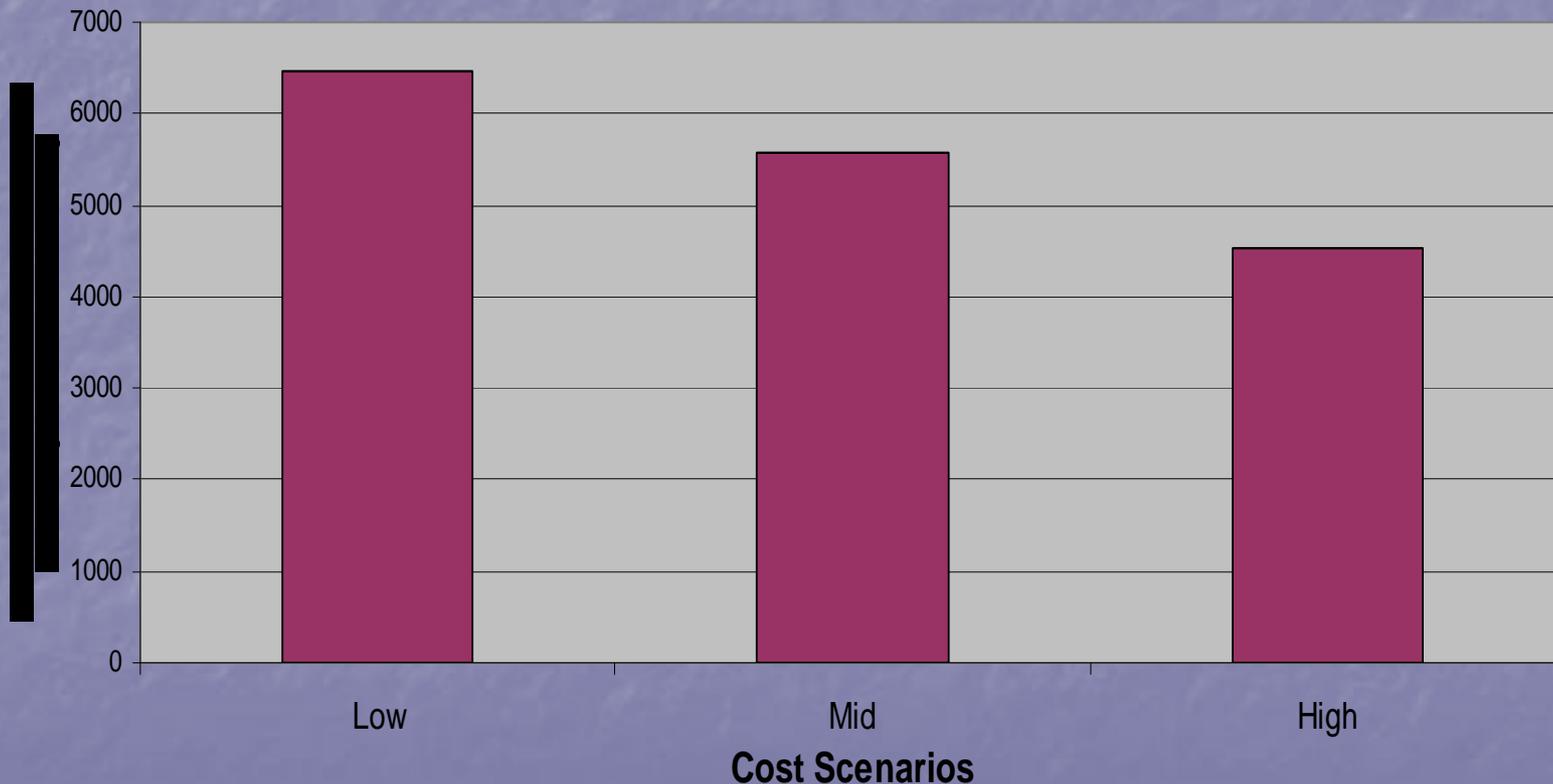
\*New Enhanced Tool Under ACES

# Three Cost Forecasts

- Mid, Low, and High
- All Costs in Nominal Dollars
- Forecasts reflect different assumptions about unplanned maintenance costs, spending behavior; not simply a +/- 20%
- Costs and investments reflect oil price changes

# Impact of Low, Mid, and High Forecasts on Tax Revenues

Cumulative Forecasted Production Tax Revenues, FY 08 - 10, at \$60/barrel ANS WC, under Three Cost Scenarios



# Forecast Adjustments

- Forecasting is a dynamic process
- DOR adjusts price, revenue, production forecasts every 6 months
- Cost forecasts to be reviewed quarterly and adjusted as necessary

# Forecasting Improved Through ACES

- ACES requires more complete cost reporting, both monthly and annually
- ACES requires forward-looking cost information
- ACES provides clearer rules for defining lease expenditures
- ACES improves audit function

# Costs Policy Implications

- Costs of production should not be ignored in tax policy
- Understanding industry costs benefits the state
- Cost sharing through credits puts state in “partnership” with industry