

**Limitations on Upside Profit  
Potential under  
Alaska's Oil and Gas Production Tax  
("The Problem with ACES")**

Roger Marks

Presentation to Board of Directors

Commonwealth North

December 14, 2010

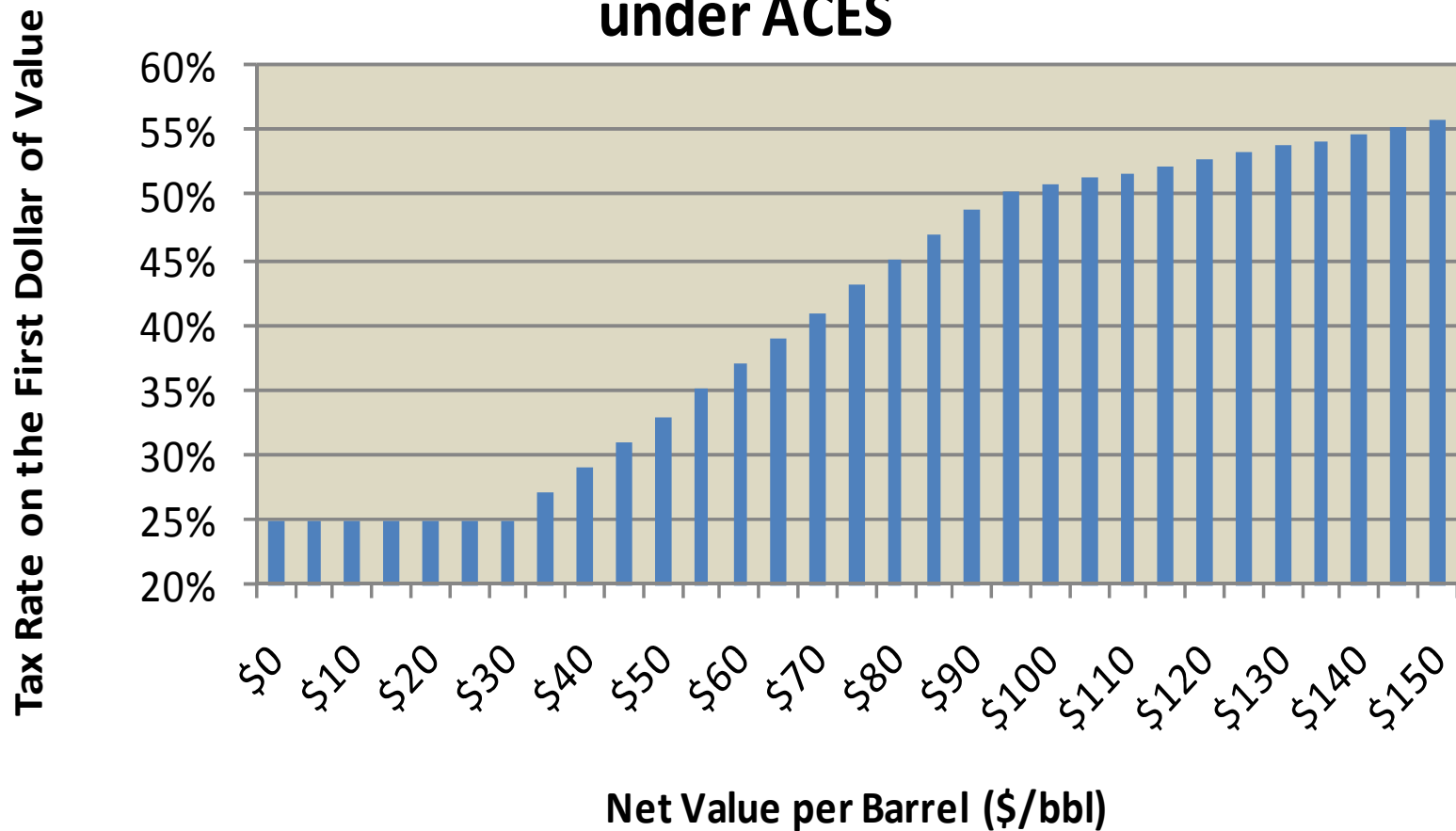
# Tax Rate under ACES

- Base rate of 25% of net value (after deducting all costs)
- Progressivity element when net value per barrel exceeds \$30/bbl:
  - $(\text{Net value per barrel value} - \$30) \times .004$
- So if oil price is \$85/bbl:
  - Net value per barrel is about \$56/bbl
  - Progressivity =  $(\$56 - \$30) \times .004 = 10.4\%$
  - Total tax rate =  $25\% + 10.4\% = 35.4\%$
  - **APPLIES TO ENTIRE NET VALUE**

# U.S. Tax Rate for Single Taxpayer

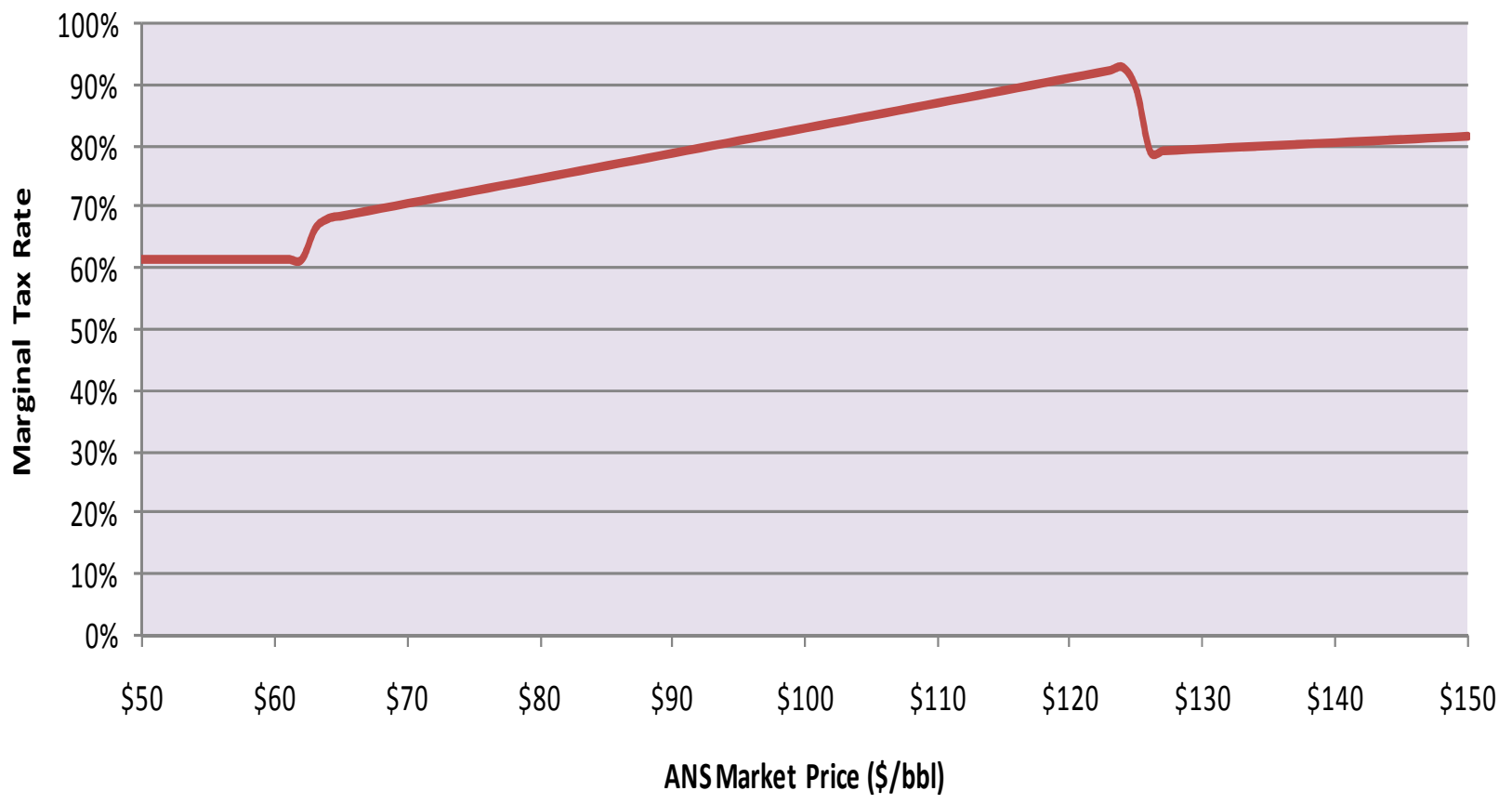
- First \$8,350 10%
- Next \$25,600 15%
- Next \$48,300 25%
- Next \$89,300 28%
- Next \$201,400 33%
- Anything over \$372,950 35%

## What Happens to the First Dollar of Value under ACES

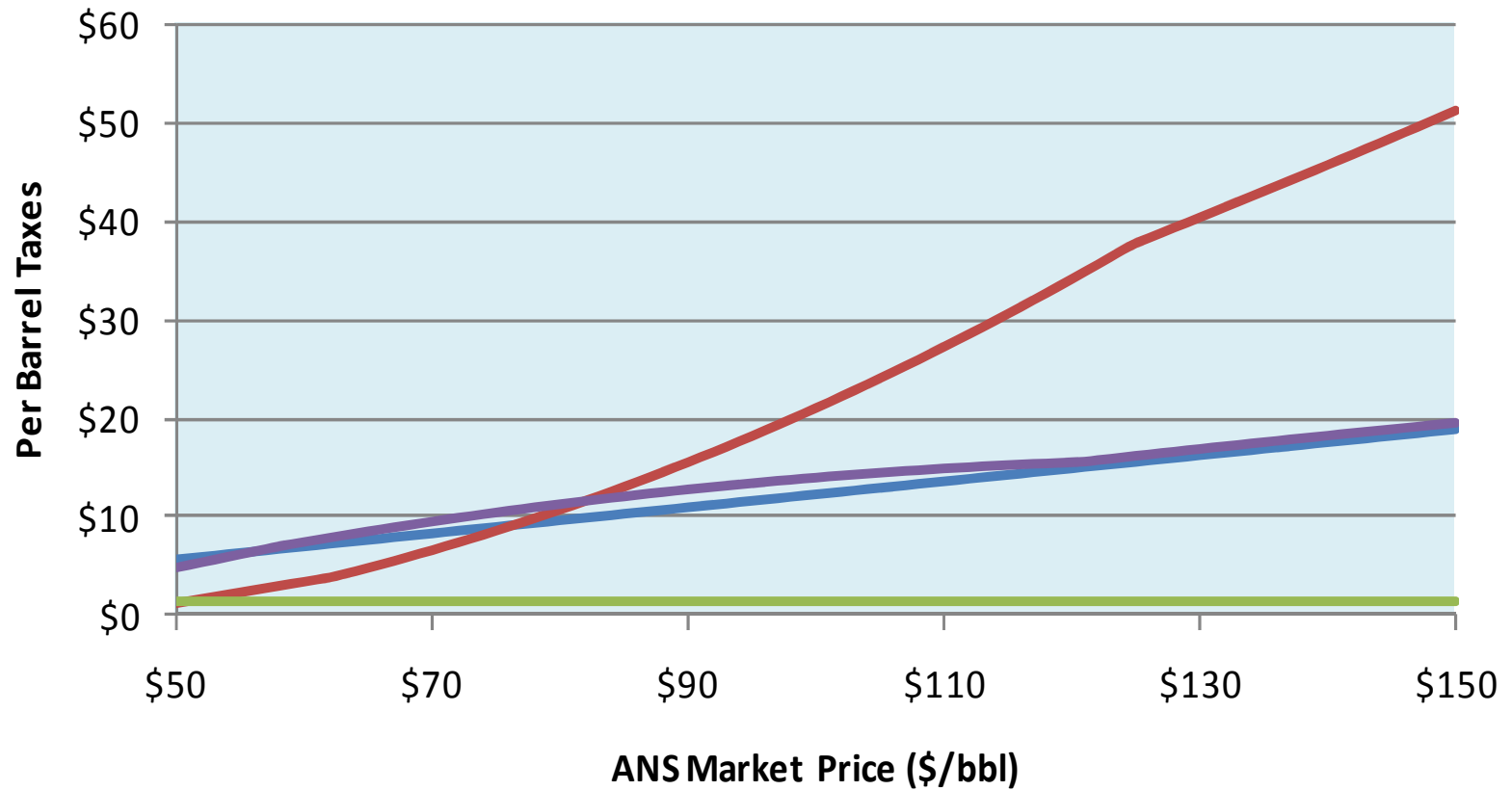


# Marginal Tax Rate under ACES (All State & Federal Taxes & Royalties)

## How Much Gov't Gets When Price Goes Up \$1

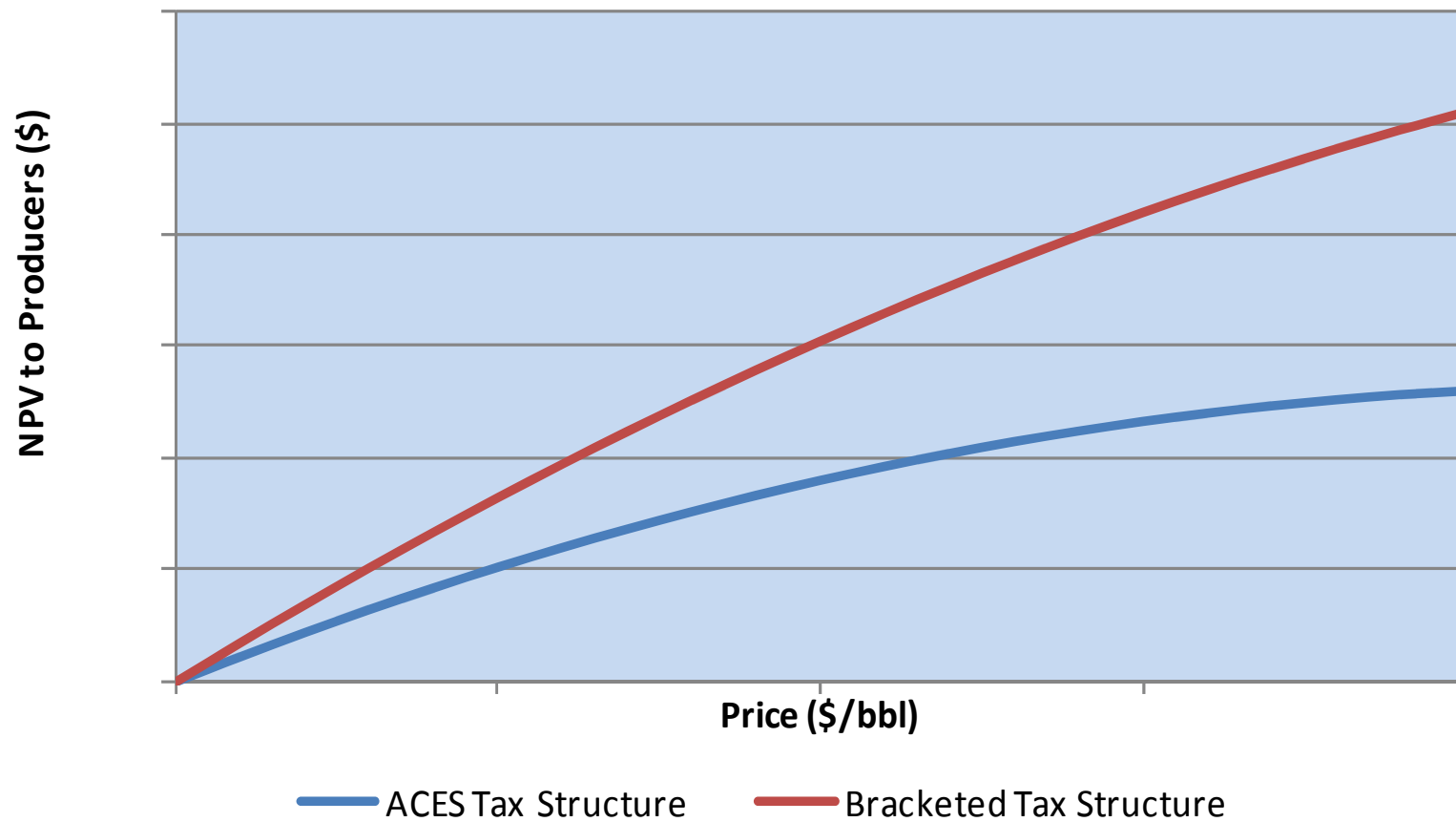


# Relative Taxes Under ACES

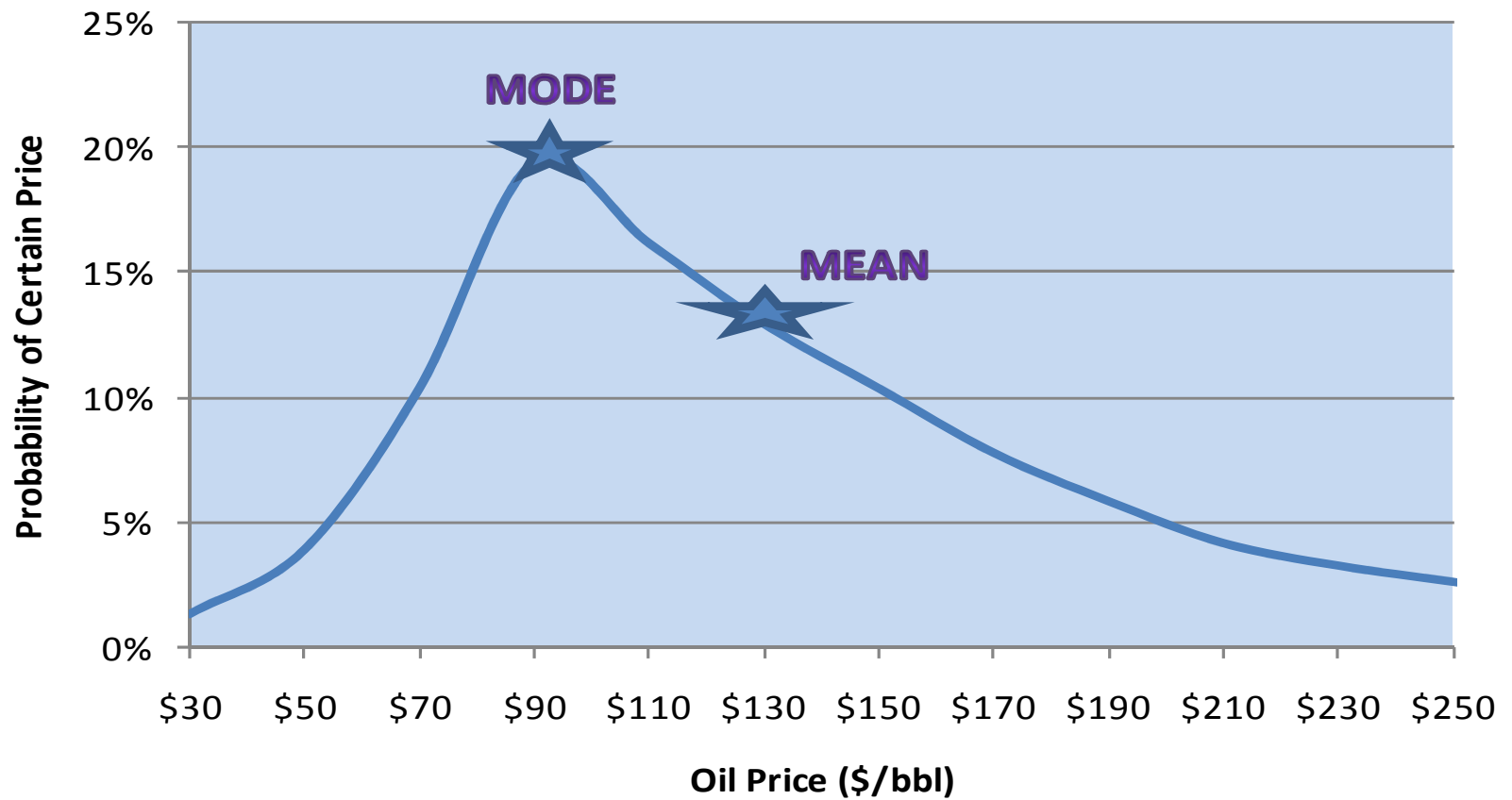


royalty severance tax (ACES) property tax state & fed corp inc tax

## Conceptual Net Present Value to Producers ACES vs. Bracketed Tax Structure



## Hypothetical Expected Price Distribution





# Getting a Fair Share

# Fair Share: Maximum Benefit to the People

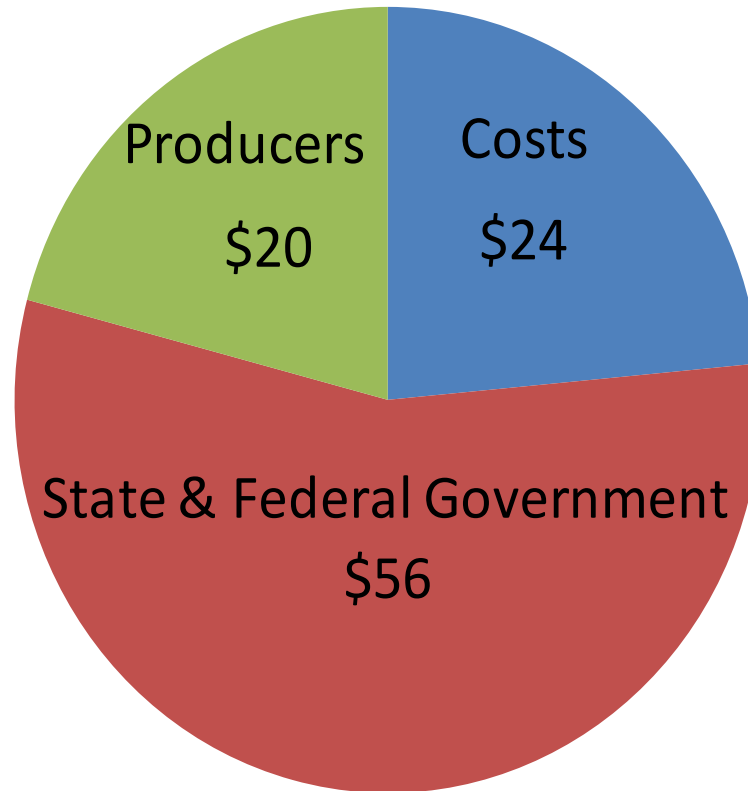
- Assume this is the long-run benefit
- Maximizing long-run benefit linked to maximizing long-run production
- Long run production of oil & gas can only be maximized by continual investment
- Alaska competes with other jurisdictions for investment

# What is the Fair Share

- “The World is Flat”
  - Capital is fluid
  - Capital is finite
  - Capital goes to where it gets the best deal
- What is “fair” is what you can get in a competitive environment
- Have to consider how investing in Alaska stacks up against other investment opportunities

# International Competitiveness

## Where did \$100/bbl in Alaska Go in 2008?

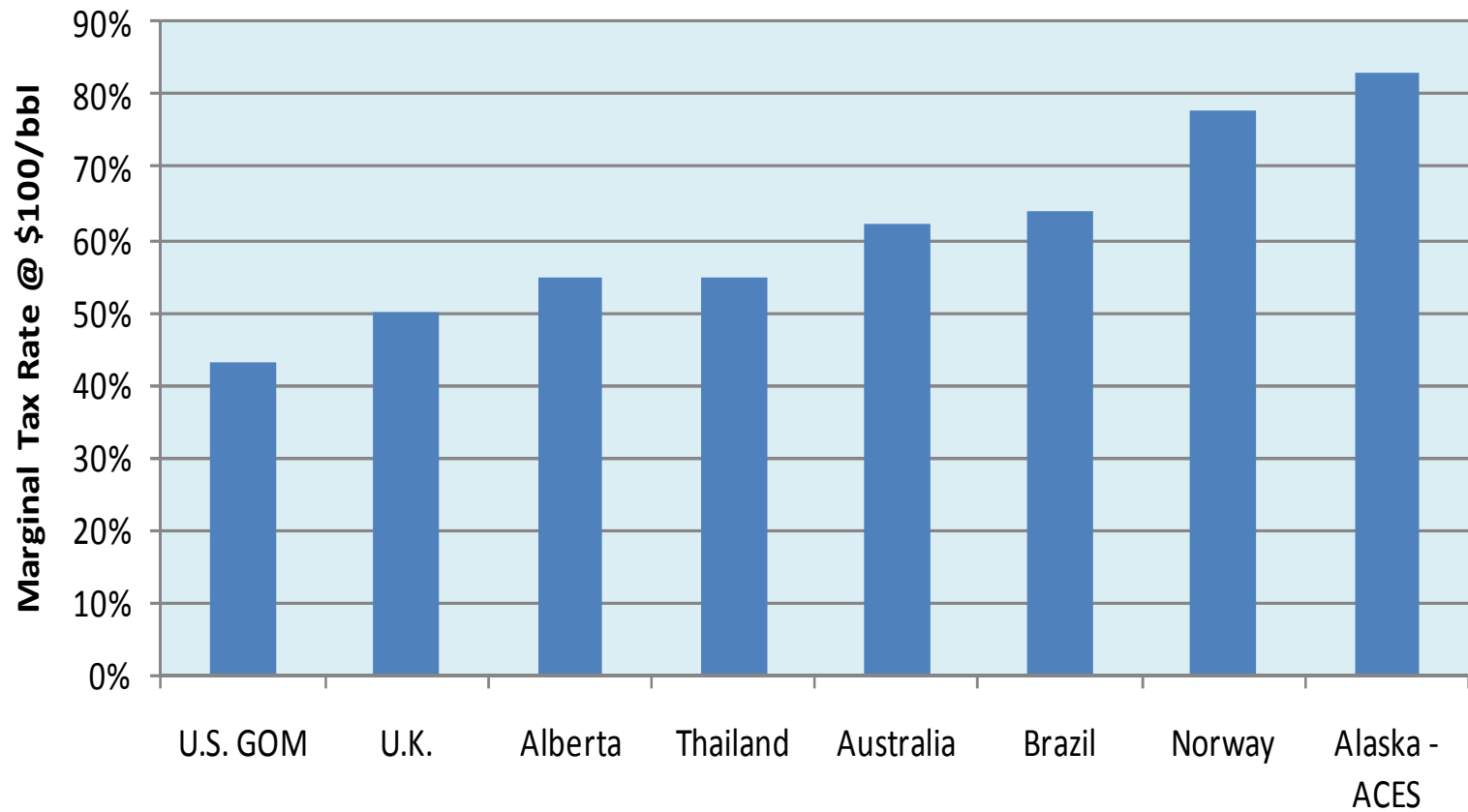


**ConocoPhillips Financial Performance: Alaska vs. Rest of World  
2008 & 2009 (\$millions)\*  
(Oil Prices averaged \$62/bbl in 2009 and \$100/bbl in 2008)**

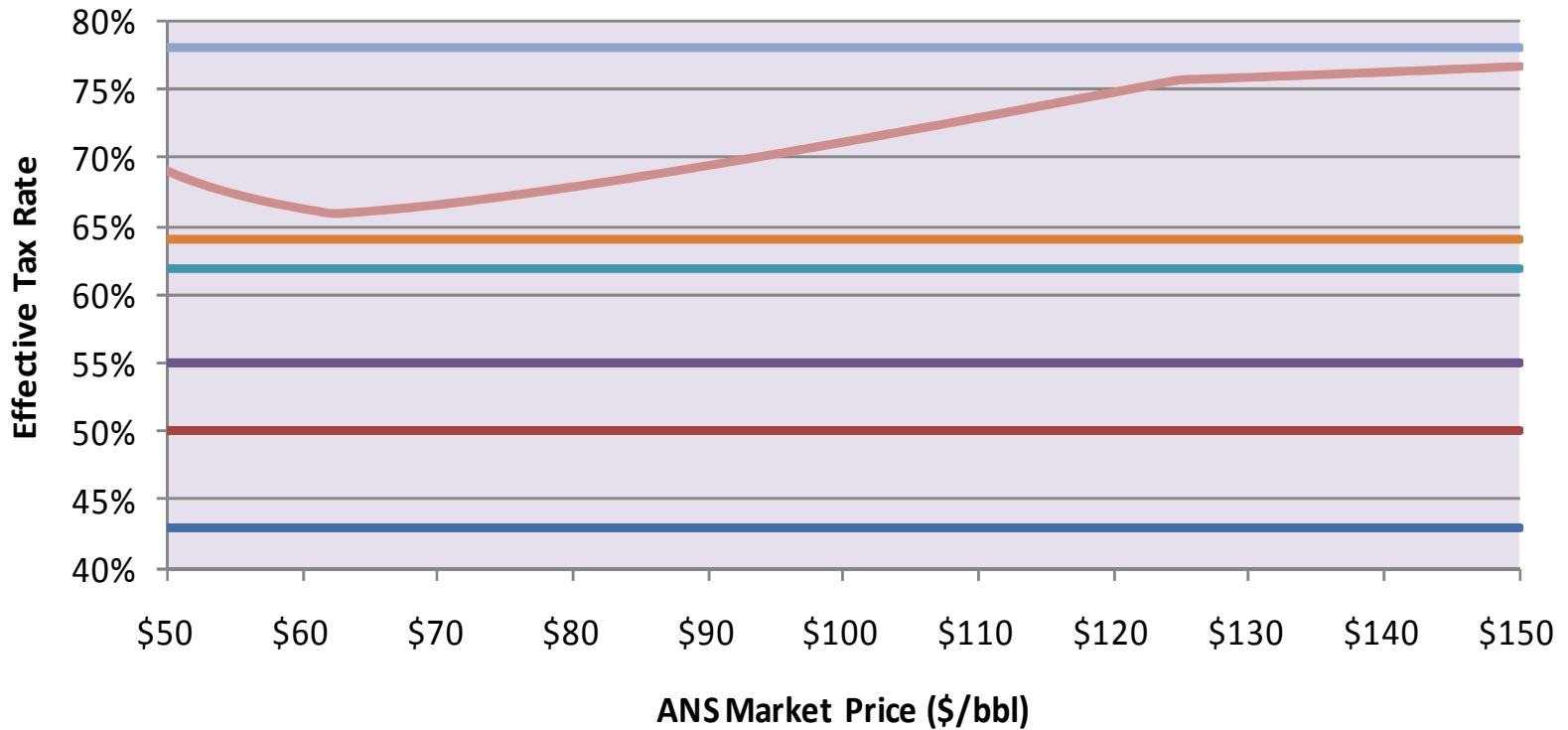
	<u>Alaska</u>			:	<u>Non-Alaska Rest of World</u>		
			Additional	:			Additional
	2009	2008	(Difference)	:	2009	2008	(Difference)
Pre-tax income	3,391	7,064	3,673	:	6,799	21,506	14,707
				:			
Total taxes	1,851	4,749	2,898	:	4,837	12,000	7,163
				:			
After-tax income	1,540	2,315	775	:	1,962	9,506	7,544
				:			
Percentage of additional pre-tax income retained after-tax			21%	:			51%

\* includes natural gas

## International Marginal Tax Rates @ \$100/bbl Market Price Tax & Royalty Regimes



## International Effective Tax Rates (Total Tax / Net Value)



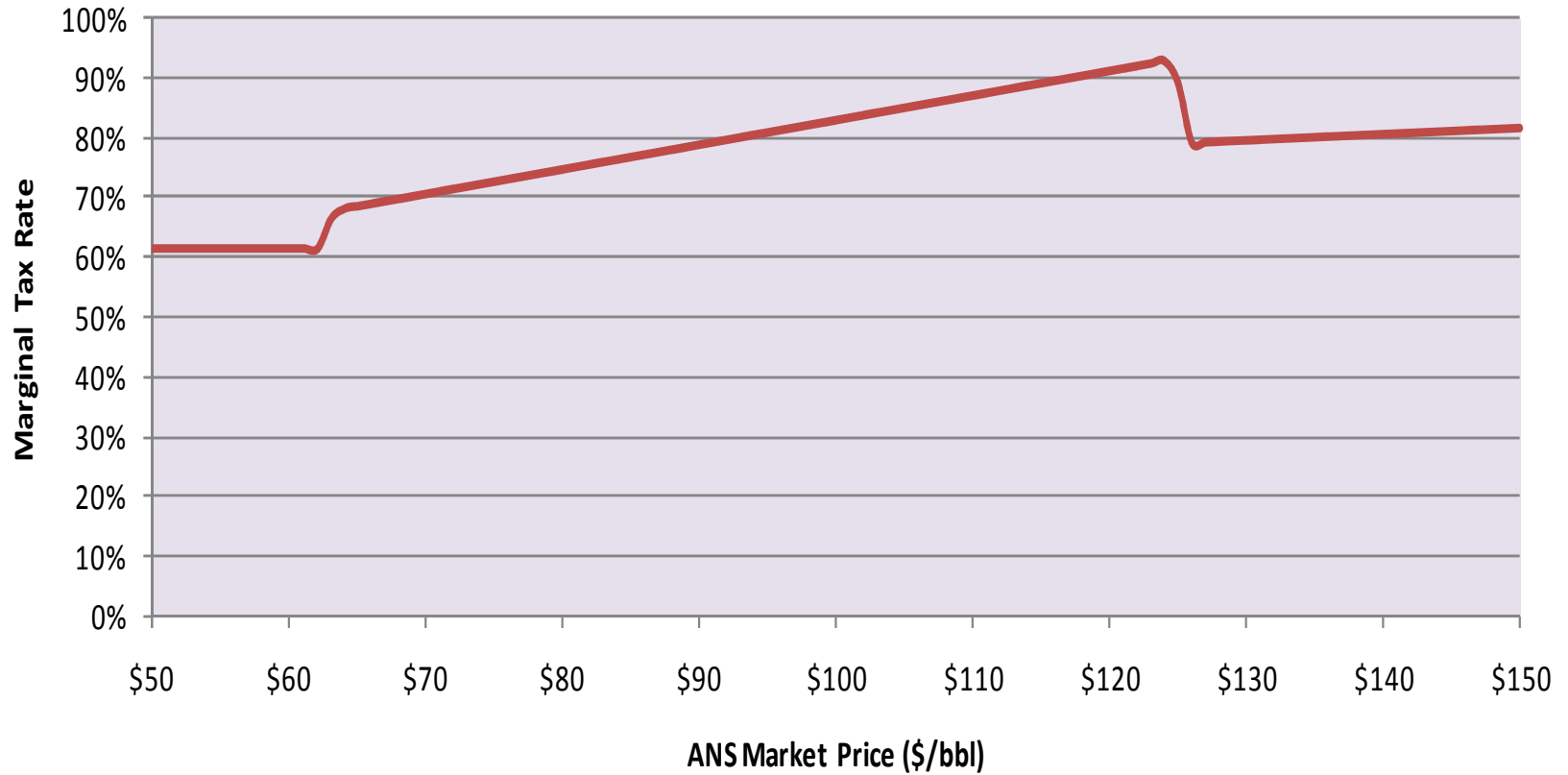
— U.S. GOM     — U.K.     — Alberta     — Thailand  
— Australia     — Brazil     — Norway     — Alaska - ACES



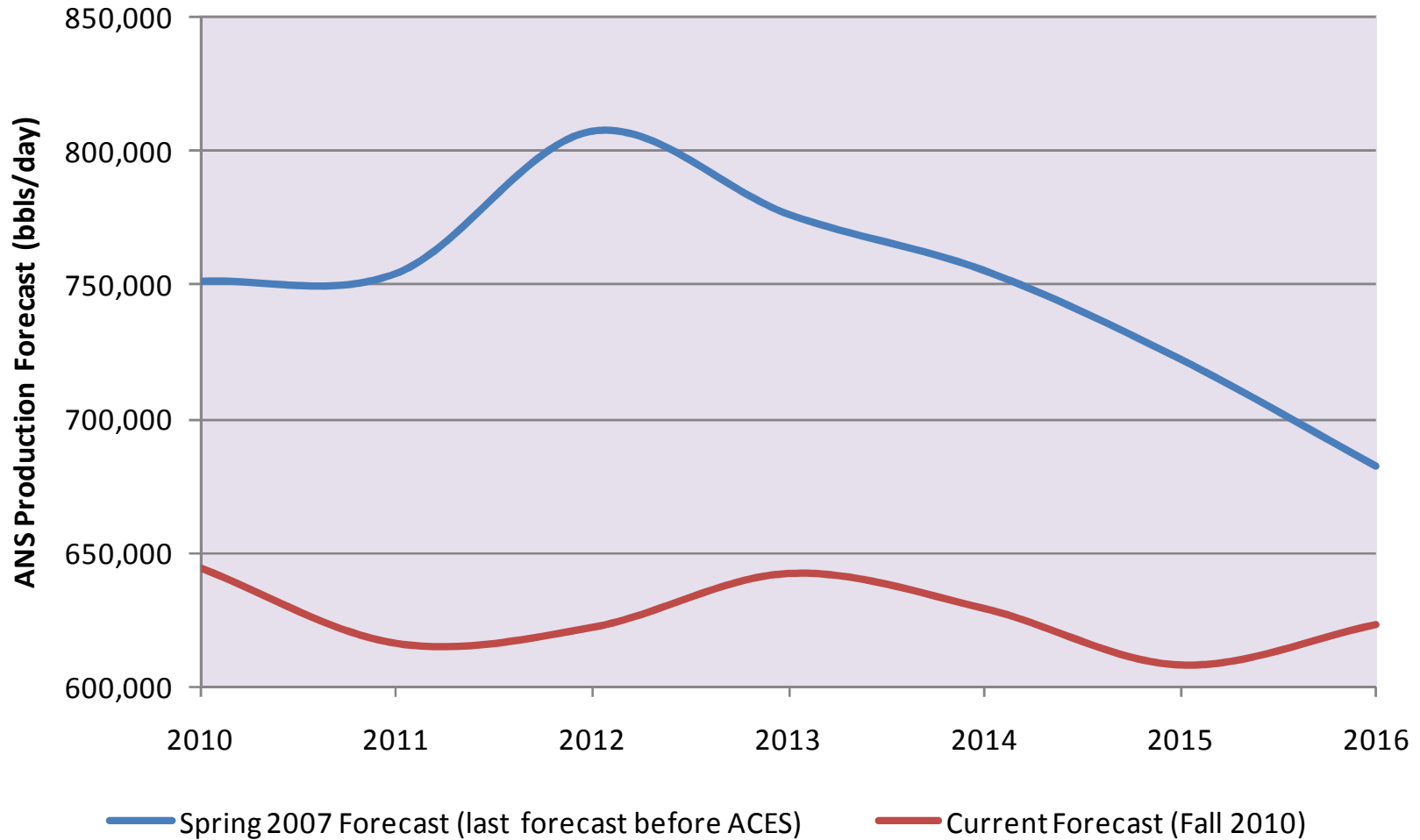
# Evaluating ACES

# Gold-Plating

## How Much of a Dollar of Spending is Picked Up by Gov't



## Dept of Revenue ANS Production Forecast Before & After ACES (bbls/day)

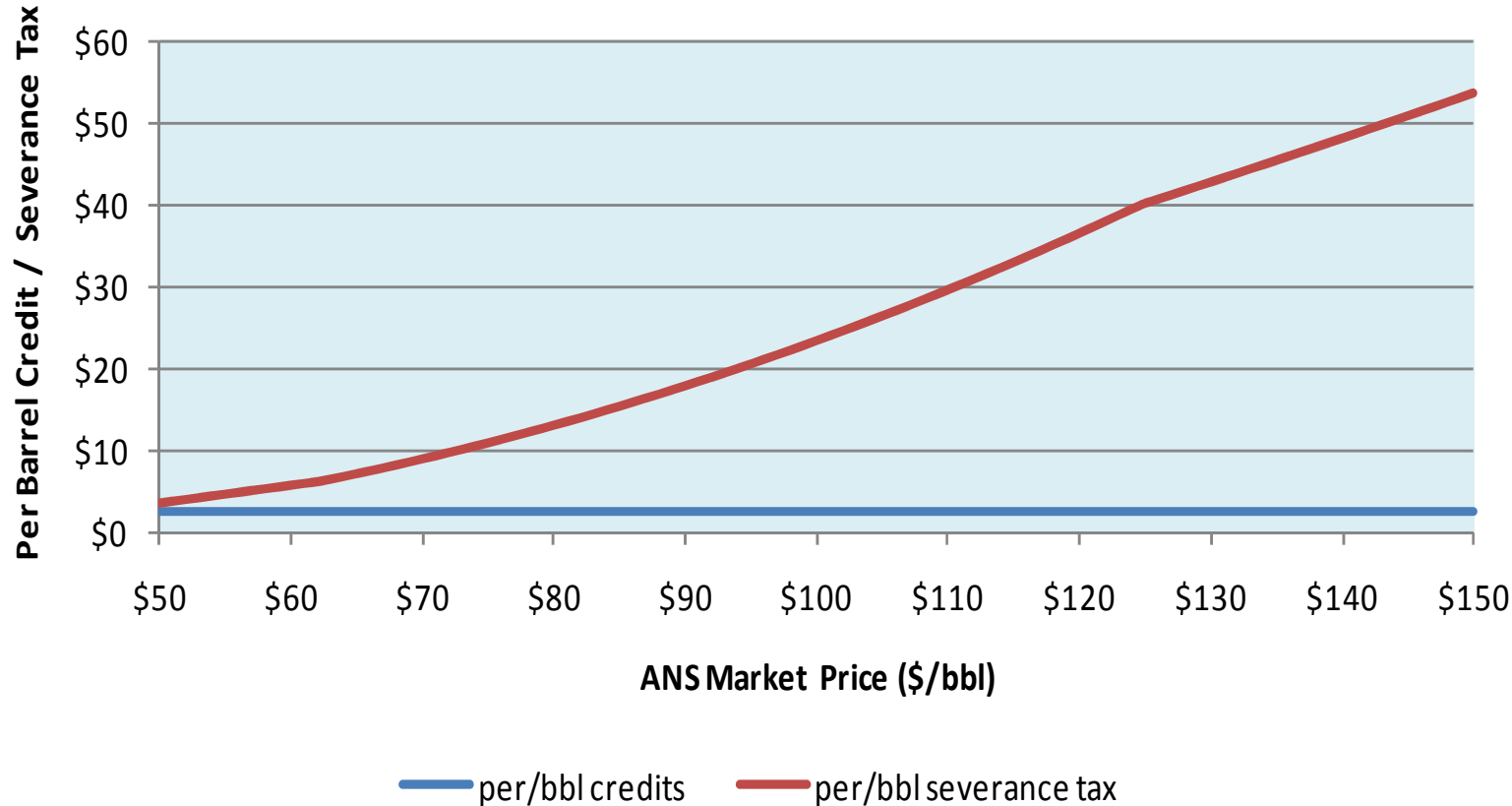


# Fixing ACES

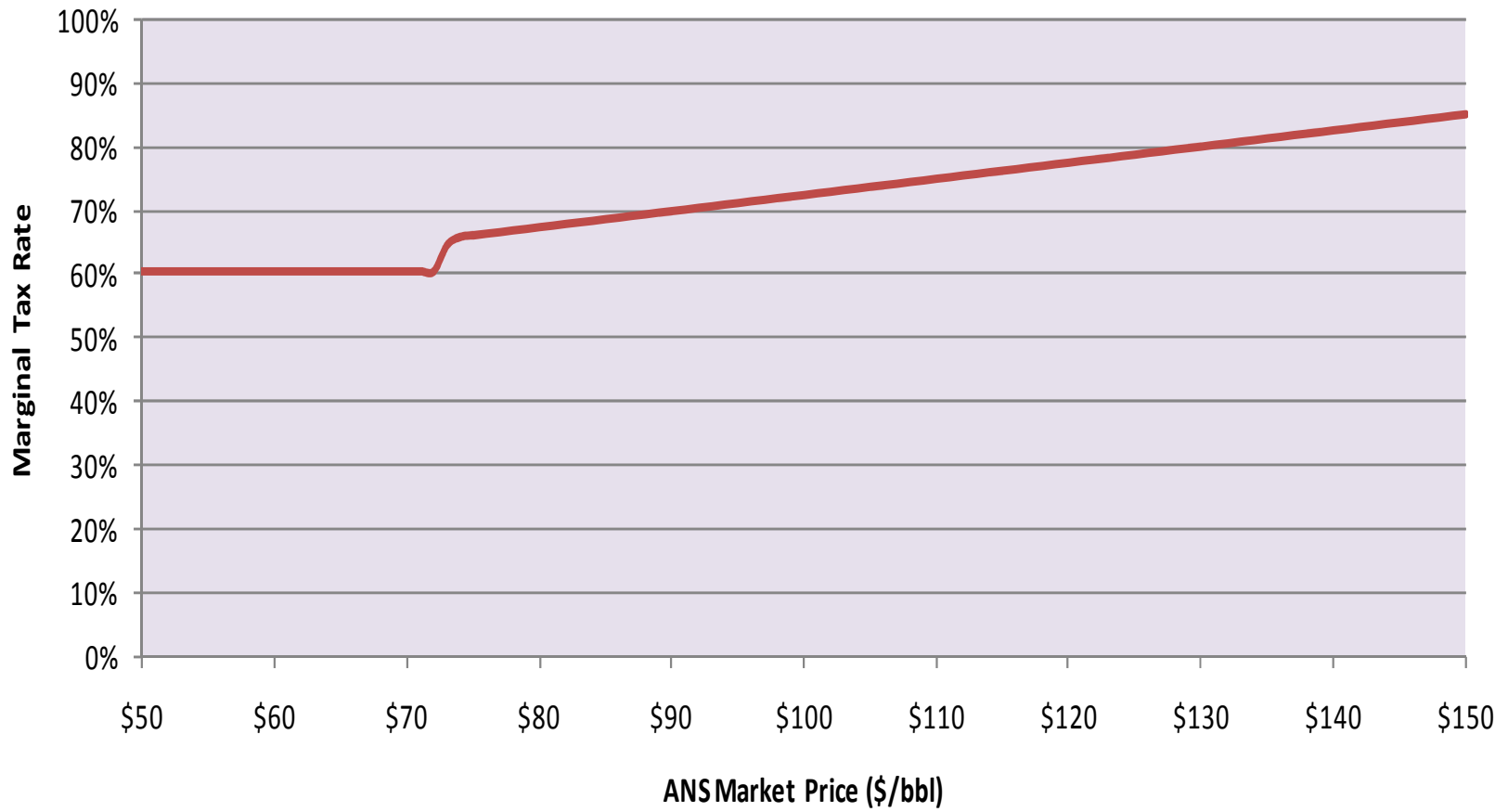
# How **NOT** to Fix It: Mechanisms that Retain Current Structure

- More credits
- Go back to PPT
- Cap progressivity rate
- Reduce base rate

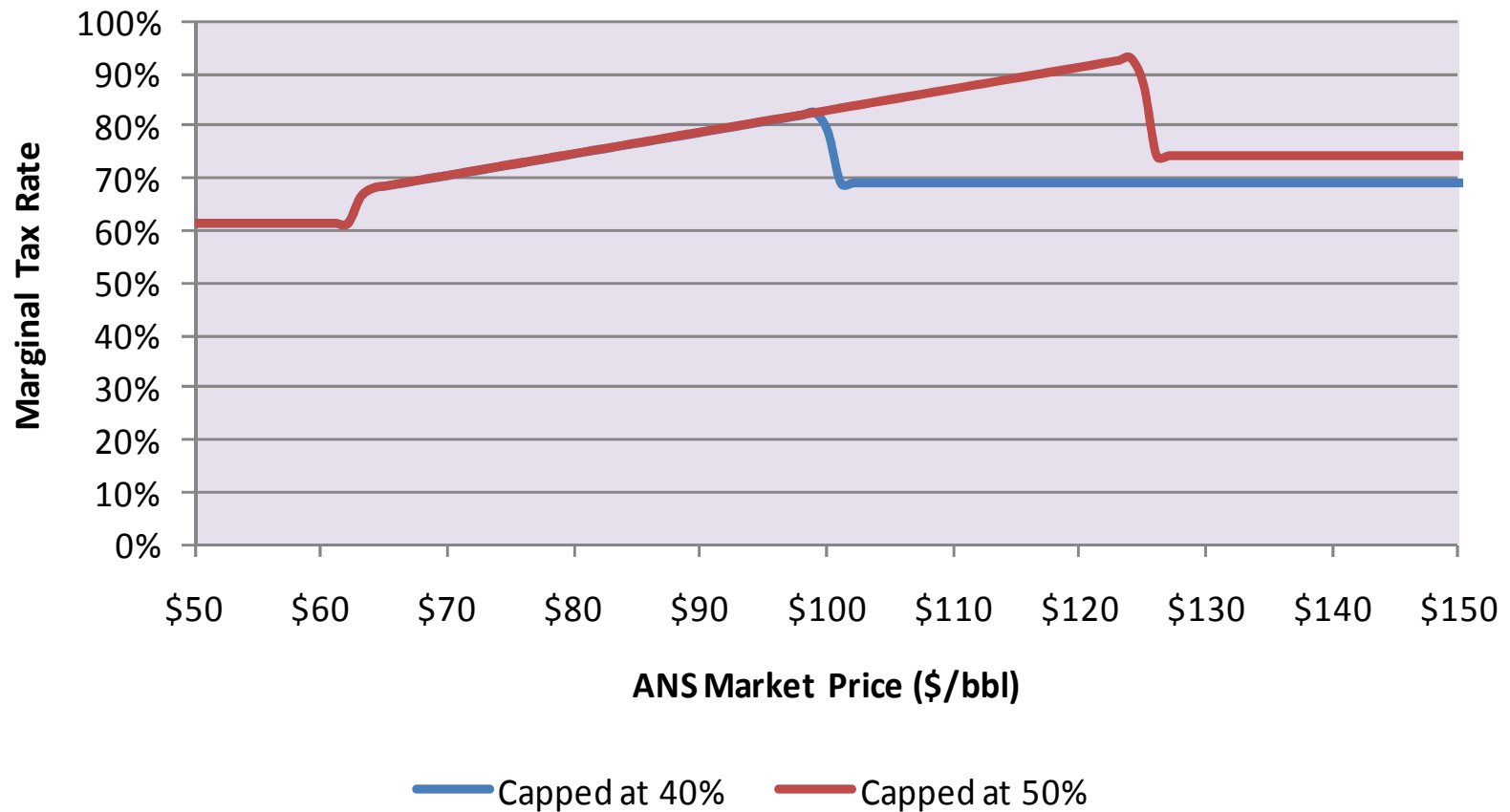
# Cash Flow Impact: Credits vs. ACES Severance Tax



## Marginal Tax Rate under PPT

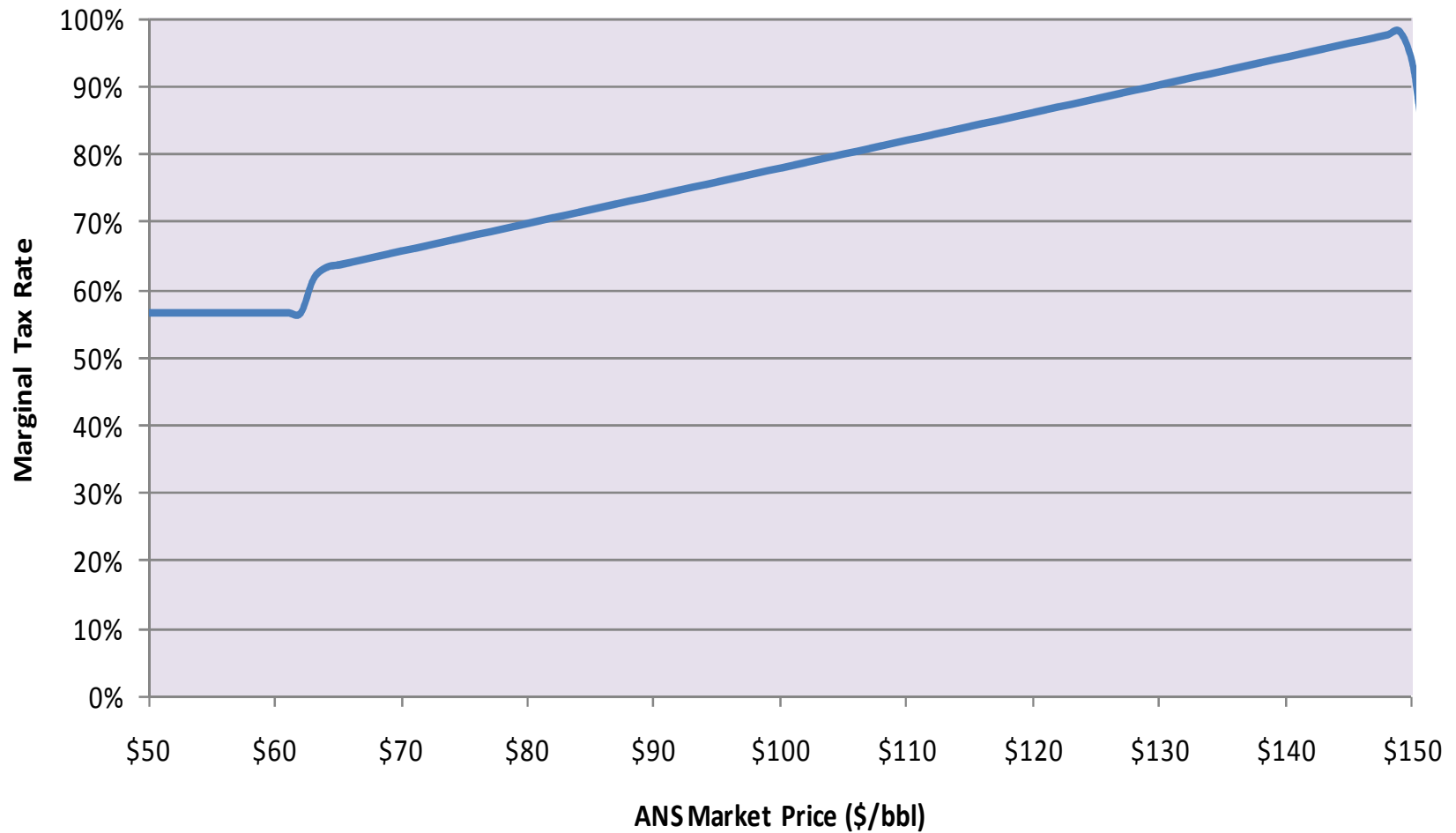


# Marginal Tax Rate With Tax Rates Capped at 40% and 50%





## Marginal Tax Rate under ACES with a 15% Base Tax Rate



# Proposal for Fix: Bracketed Tax Rates

# Brackets: Design Considerations

- Base rate
- When progressivity starts
- Number of brackets
- Size of brackets
- Net value for peak
- Peak rate
- All gauged to international competitiveness

# Proposed Bracket Structure Based on Net Value p/bbl\*

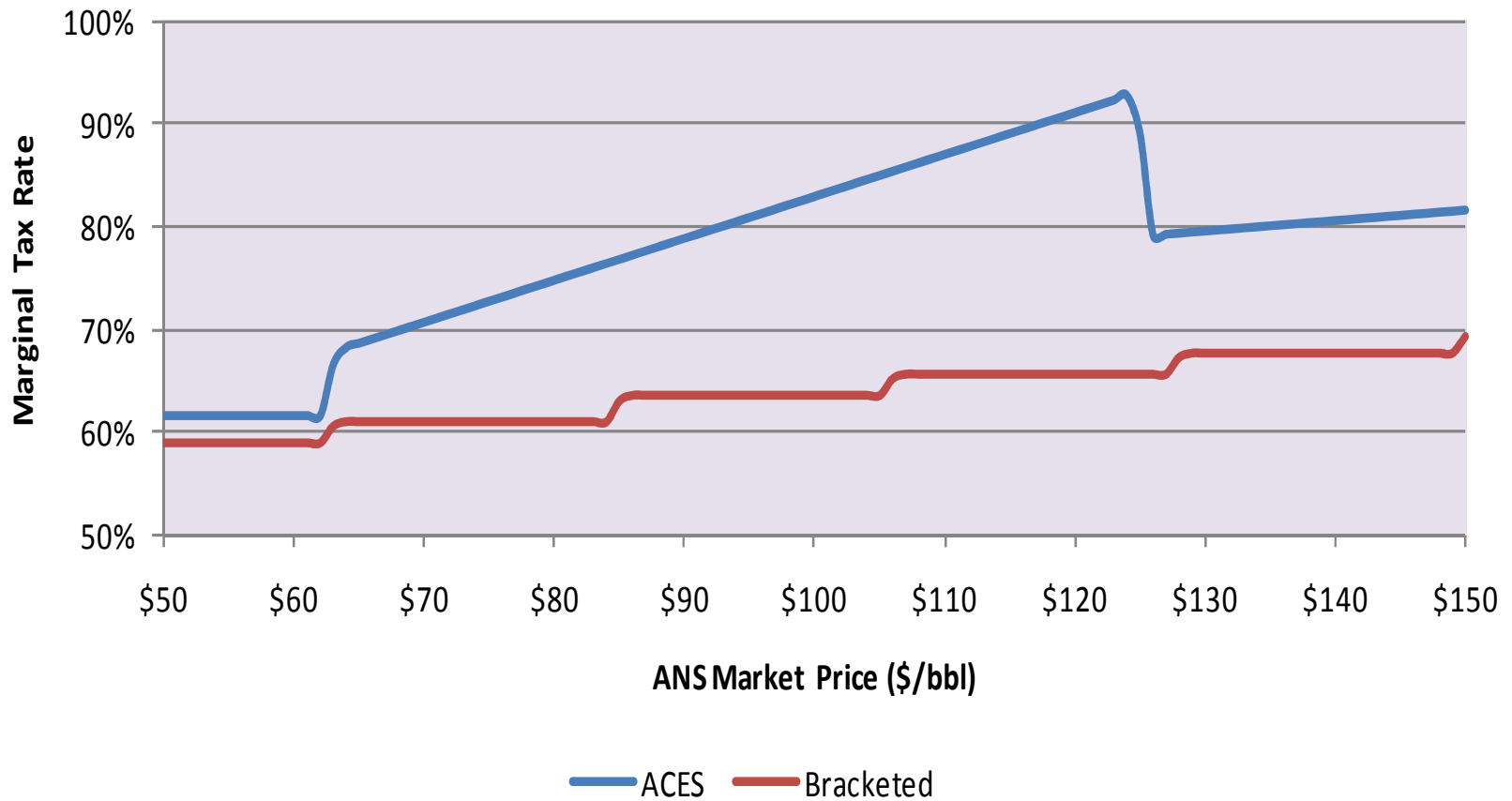
• \$0/bbl - \$30/bbl	20%
• Next \$22/bbl (\$30 - \$52/bbl)	24%
• Next \$21/bbl (\$52 - \$73/bbl)	29%
• Next \$22/bbl (\$73 - \$95/bbl)	33%
• Next \$22/bbl (\$95 - \$117/bbl)	37%
• Next \$21/bbl (\$117 - \$138/bbl)	41%
• Next \$22/bbl (\$138 - \$160/bbl)	46%
• Anything over \$160/bbl	50%

\* These net values are approximately \$30 less than market values (the ANS West Coast price).

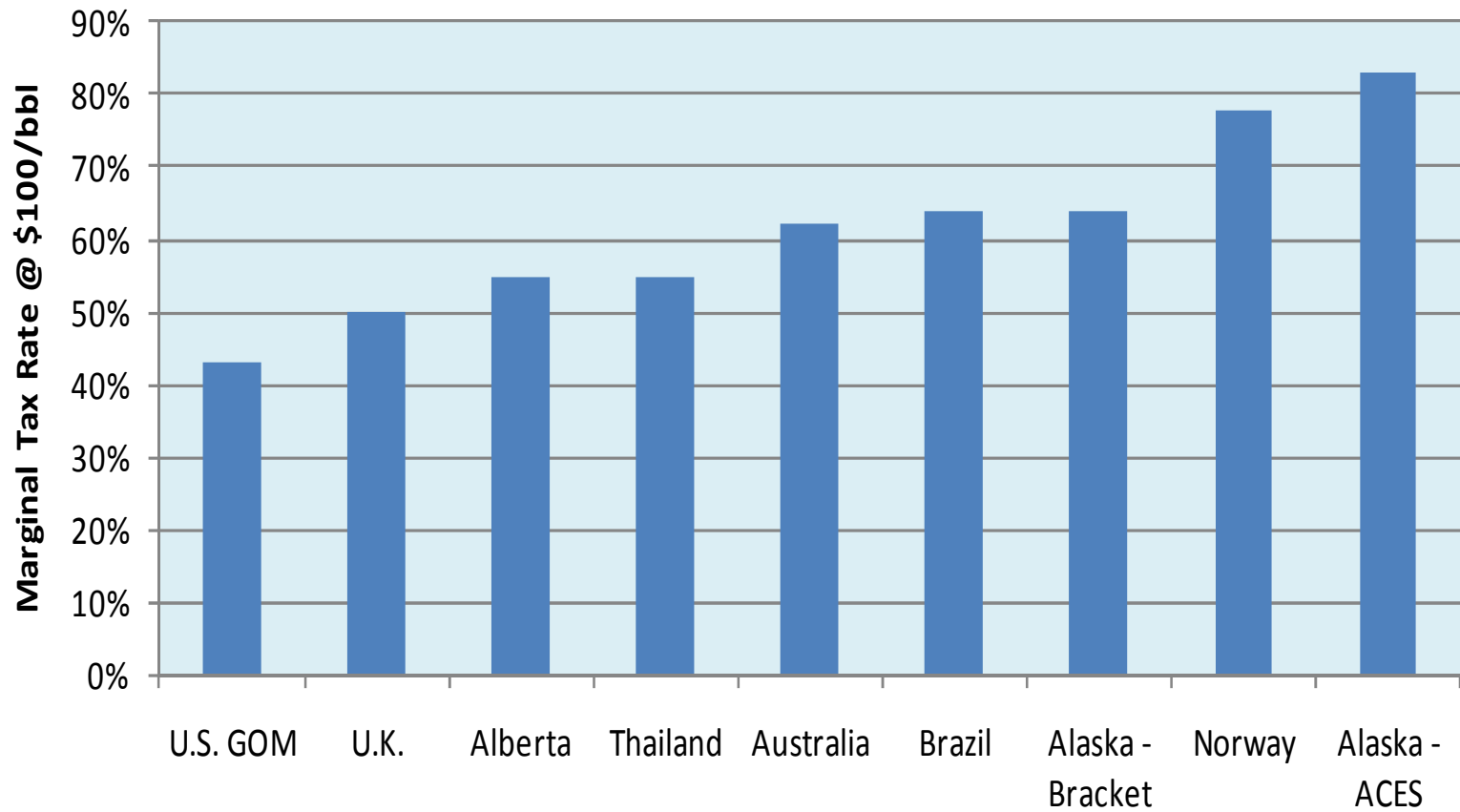
# Example: \$130/bbl ANS Market Price

<b>Market Price</b>	<b>\$130</b>		
<b>Costs</b>	<b><u>\$30</u></b>		
<b>Net Value</b>	<b>\$100</b>		
<b>Bracketed Tax</b>			
	<b>Dollars in</b>	<b>Tax</b>	
	<b><u>Bracket</u></b>	<b><u>Rate</u></b>	<b><u>Tax</u></b>
<b>Bracket 1: \$0/bbl - \$30/bbl</b>	<b>\$30</b>	<b>20.0%</b>	<b>\$6.00</b>
<b>Bracket 2: Next \$22/bbl (\$30-\$52/bbl)</b>	<b>\$22</b>	<b>24.0%</b>	<b>\$5.28</b>
<b>Bracket 3: Next \$21/bbl (\$52-\$73/bbl)</b>	<b>\$21</b>	<b>29.0%</b>	<b>\$6.09</b>
<b>Bracket 3: Next \$22/bbl (\$73-\$95/bbl)</b>	<b>\$22</b>	<b>33.0%</b>	<b>\$7.26</b>
<b>Bracket 3: Next \$5/bbl (\$95-\$100/bbl)</b>	<b>\$5</b>	<b>37.0%</b>	<b><u>\$1.85</u></b>
<b>Bracketed tax per barrel</b>			<b>\$26.48</b>

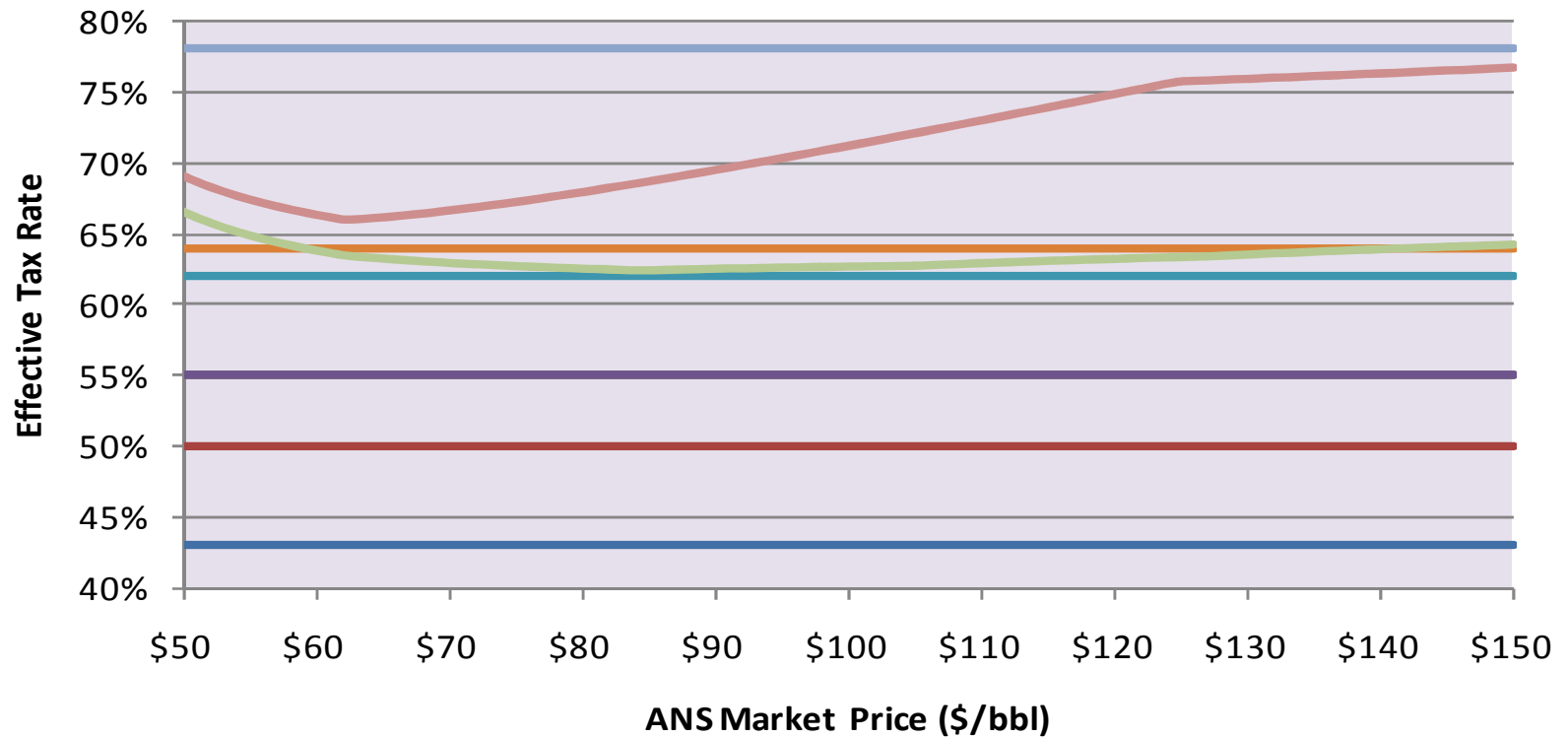
# Marginal Tax Rate ACES & Proposed Bracketed



## International Marginal Tax Rates @ \$100/bbl Market Price Tax & Royalty Regimes



## International Effective Tax (& Royalty) Rates



- |          |               |                    |
|----------|---------------|--------------------|
| U.S. GOM | U.K.          | Alberta            |
| Thailand | Australia     | Brazil             |
| Norway   | Alaska - ACES | Alaska - Bracketed |



# Severance Tax Per Barrel

