

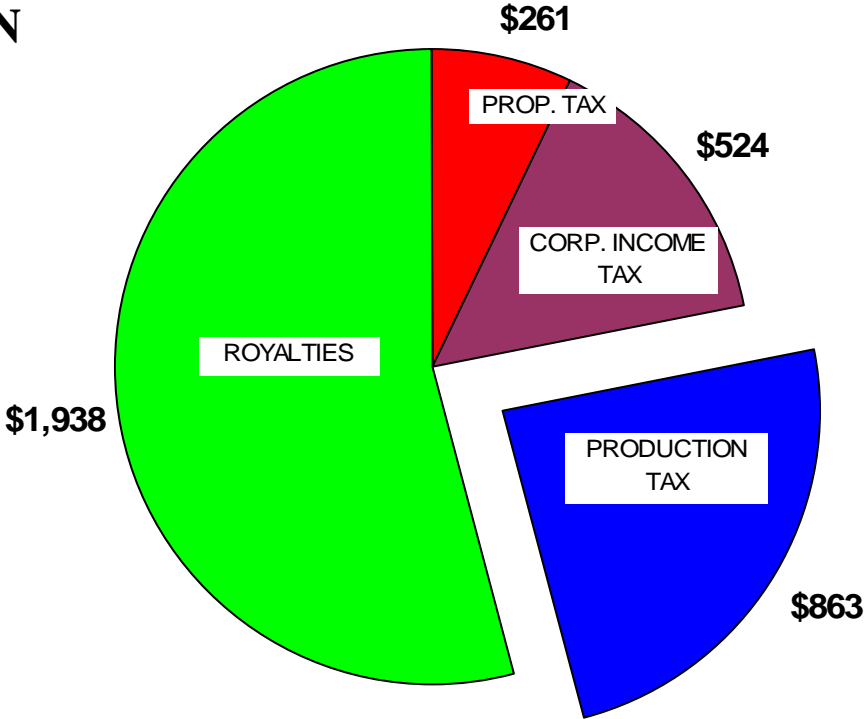
Alaska's Production Tax

Theory and Practice

Alaska's CURRENT Oil Fiscal System by Source FY '05

TOTAL

\$3631 MILLION



Alaska Dept. of Revenue Fall '05 Revenue Sources
Property taxes includes Municipalities
Royalties include Permanent Fund

Alaska's Oil and Gas Fiscal Regime

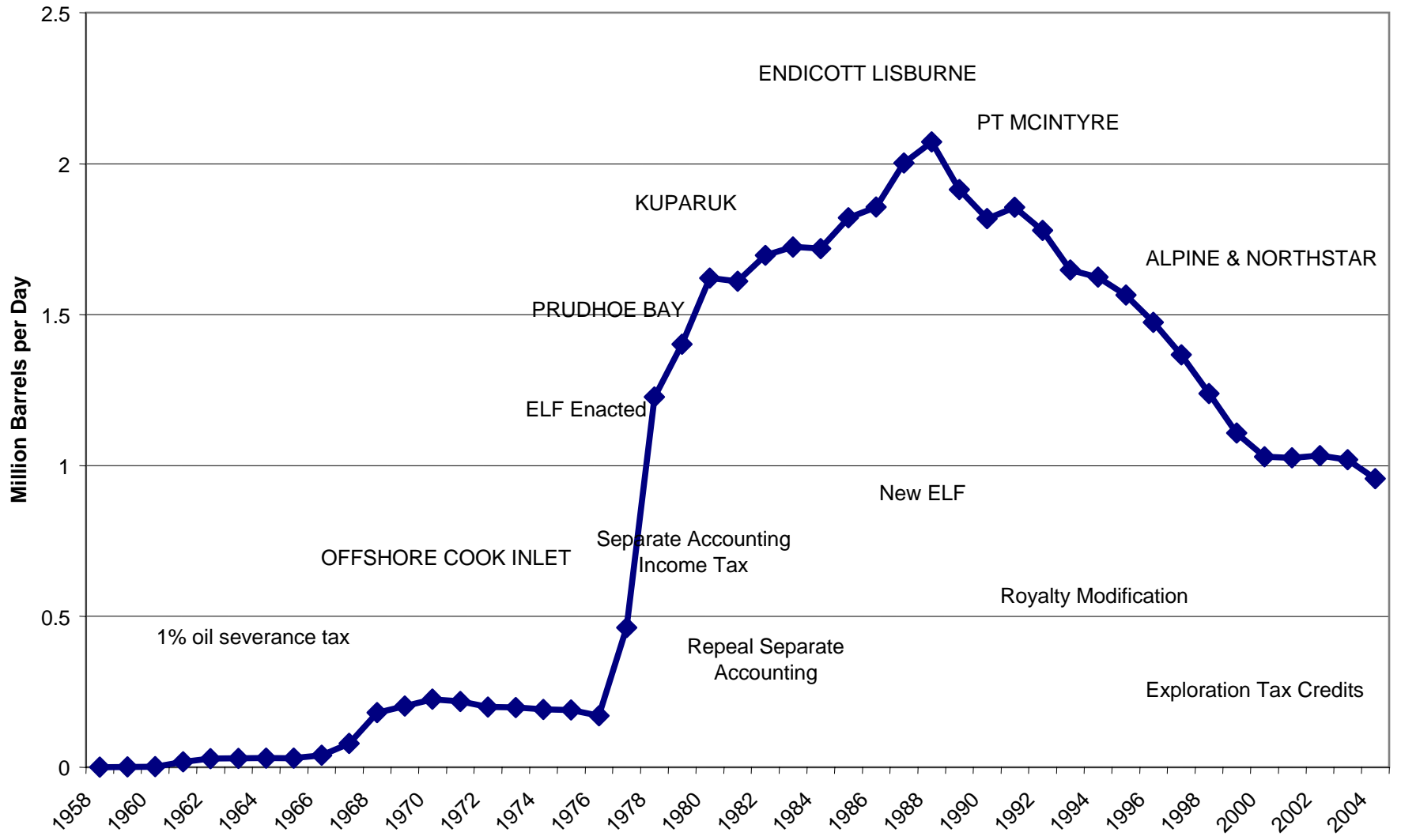
Royalty: State ownership share of the resource removed and sold from State lands.

Production tax : Tax on the severing of the resource from the State as either a % of value or a minimum cents per barrel or mcf.

Property Tax: Levied on the assessed value of production and transportation hardware at a rate of 20 mils

Corporate Income Tax: World-wide income allocated to Alaska based on three factors: production, property and sales (includes tariffs)

Alaska Oil Production and Major Fiscal Adaptations 1958 - 2004




An International Perspective on Petroleum Fiscal Systems

Norwegian Petroleum Directorate

The fiscal policy

Objective



- ♦ Government objective
 - Maximise Government take
 - Get as high share of the profit as possible
 - Maximise value of the petroleum resources
- 
- The goal is to create a win-win situations between the state and the oil companies*
- ♦ Companies objective
 - Maximise shareholders interest (private or public)

The fiscal policy

Government objective



- ♦ Important to create a win-win situations between the state and the oil companies
- ♦ The bargaining relationship depends mainly on profitability and risk
 - the government has to take the mother earth and the geological potential into consideration when it design the fiscal packages
- ♦ Crucial to relate the fiscal packages on the geological basis and where on the geological learning curve that province is

The fiscal policy

Challenge



- ♦ The challenge of the fiscal policy:
 - Ensure as high share of the value as possible for the Government
 - Encouraging the exploration and exploitation of valuable resources

- ♦ One has to find a correct balance between the state interest and the oil companies.

The fiscal policy

The fiscal package



- ♦ The fiscal packages can be characterized both by the
 - The tax level
 - The tax system

- ♦ The fiscal policy can create disincentives to explore or to exploit the petroleum resources due to either the tax level or the tax system

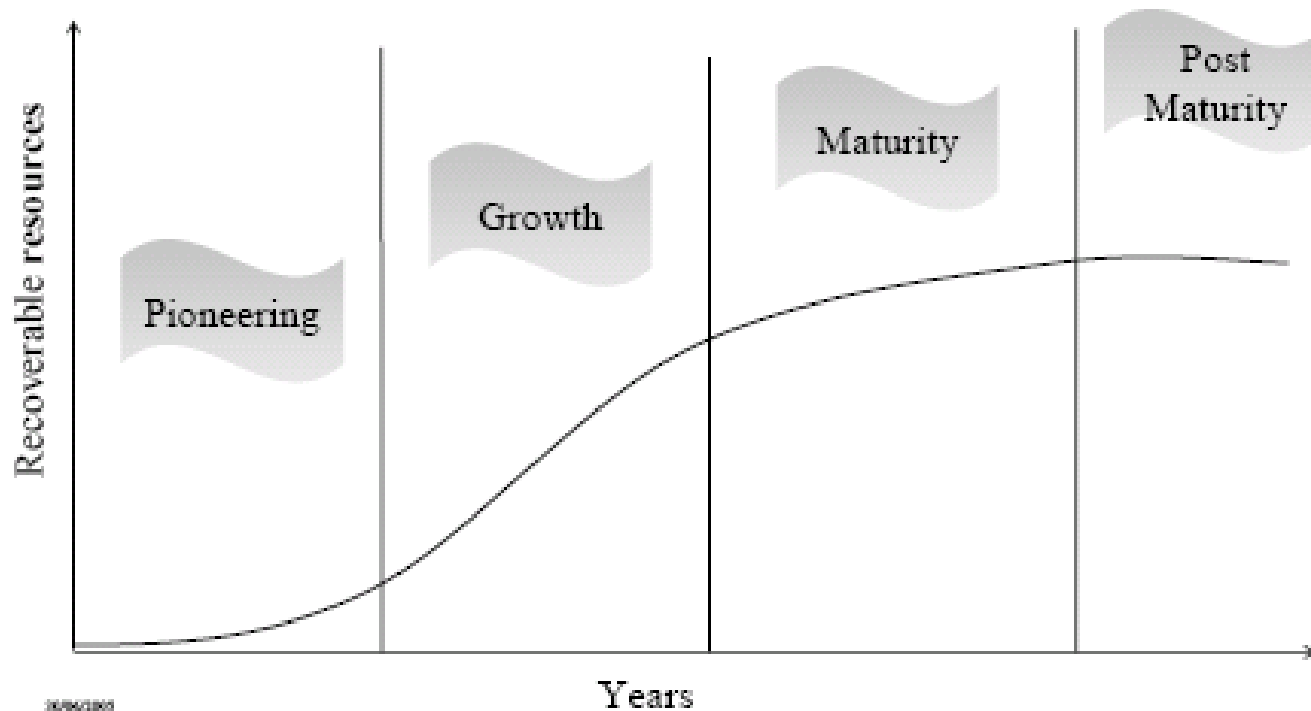
- ♦ A key question to any fiscal package is whether it will influence the investment decision of the investor adversely with respects to the nation optimal decisions.

The fiscal package

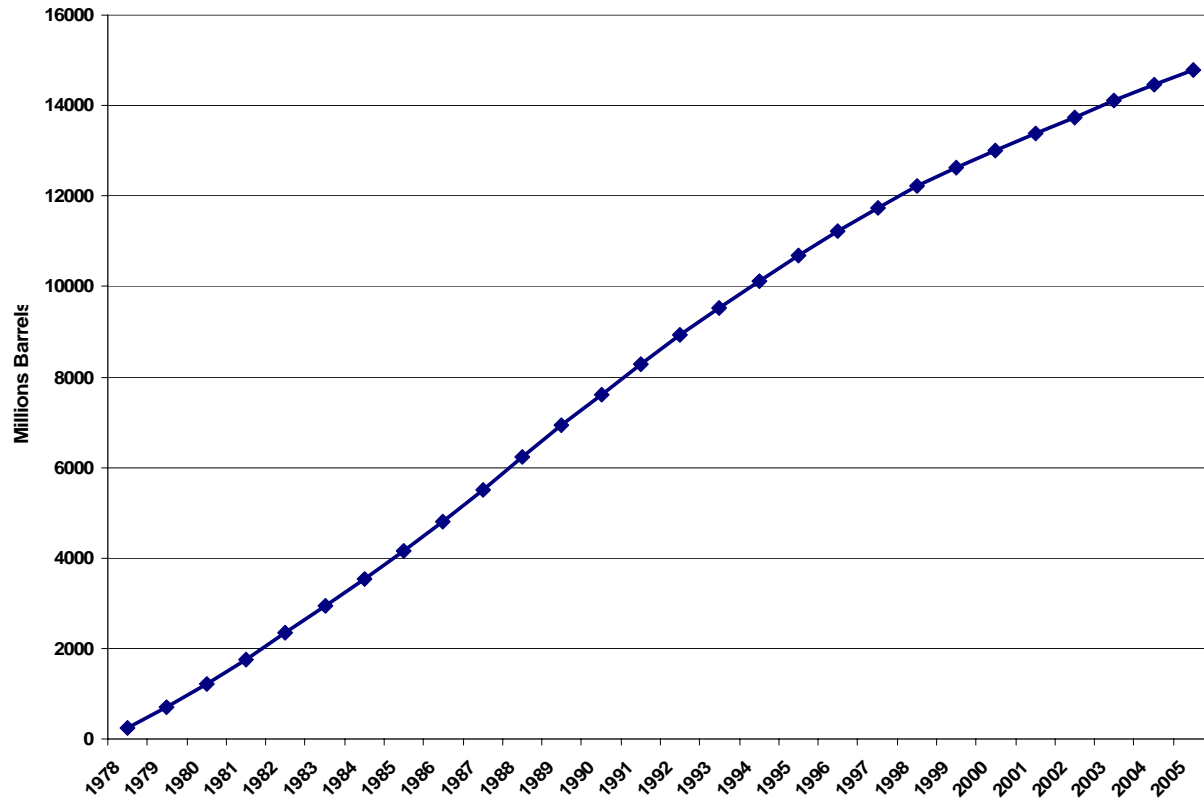
Relate to the geological basis and the geological learning curve



The geological learning curve



Cumulative Production Alaska North Slope



What Have Experts Told Us Repeatedly

- Taxes on net are more economically efficient because they allow investors to recover their investment and rate of return.
- This ensures a competitive area to invest in.
- Governments need to style their fiscal system around their geology.
- Alaska is a high cost environment

- Alaska thus is not a particularly attractive place to explore and develop with its current system (no sharing of upstream costs in a high cost environment)
- Alaska could change its system to both increase its government take and encourage investment.

A Sample of these Experts

- The 1978 study by Walter Levy and Associates which lead to the adoption of separate accounting.
- The primary conclusion in the 1989 Alex Kemp/Gaffney/Motamen study following the ELF change.
- The conclusions in the 1994 Arthur D. Little/John Gault Study

- Woods MacKenzie in its 2004 study of international fiscal systems also described Alaska as a high cost regressive system that did have a good ranking thanks to high oil prices and the discovery of the lucrative Alpine field in 1994.
- 2005, Pedro Van Meurs recommends net profit system to replace ELF to provide State revenue upside and encourage investment

Why has the State Been Reluctant to Change the System?

- Throughout the 1990's significant concern about low prices.
- This led implicitly to a desire to give up some upside potential to protect against catastrophic low prices (see FY 1999)
- Changing oil fiscal regimes is not taken lightly--especially in a declining production environment.

Conclusions

- Alaska can take a positive step to making its tax system more efficient by changing the petroleum production tax
- We will still have our royalty share calculated before upstream cost deduction
- We will still have a piece of world-wide corporate income as long as the companies produce in Alaska

Conclusions

- We will also have a property tax
- At the same time if prices stay anywhere near as high as they have been over the last three years, we will generate more revenue for the state AND
- Provide significant new incentive to spend investment dollars exploring for and developing oil and gas in the State