ALASKA STATE LEGISLATURE

Session

State Capitol, Rm. 419
Juneau, AK 99801
(907) 465-2435
Fax: (907) 465-6615

Interim

716 W. 4th Ave, Ste. 409
Anchorage, AK 99501
(907) 269-0120
Fax: (907) 269-0122

Senator.Bill.Wielechowski@akleg.gov

Resources Committee

State Affairs Committee

Joint Armed Services Committee

Judiciary Committee

SENATOR BILL WIELECHOWSKI

November 27, 2015

Senator Cathy Giessel
Alaska State Legislature
716 W. 4th Avenue, Suite 511
Anchorage, AK 99501

Dear Senator Giessel,

Thank you for the opportunity to participate in the 2015 Oil and Gas Tax Credit Working Group. After reflecting on the content shared during our six meetings, I have compiled my suggested improvements to the State's current tax credit system. Please consider the following for inclusion in the Oil and Gas Tax Credit Working Group report.

The oil tax credit and deduction system currently in place must be reformed. Over FY 15 and FY 16, the State of Alaska is paying out approximately $642 million more in refundable oil tax credits than we receive in production taxes. While the level of refundable tax credits has come under recent scrutiny by the Administration, and also seemed, at first, the main focus of the working group's agenda, refundable tax credits are only a small portion of the problem we face.

Huge deductions allowed under our current oil tax system threaten to overwhelm our budget. In FY 17, credits used against tax liability (predominantly going to large, still very profitable North Slope fields) are projected to skyrocket to $1.25 billion, remaining at $1.21 billion in FY 18 and $999 million in FY 19. Combined with refundable oil tax credits of hundreds of millions per year, the largest cost driver in Alaska is neither Education nor Healthcare, but oil tax credits and deductions. Unfortunately, this working group touched very little on the per-taxable-barrel credit issue during its discussions. Nor did this working group have the opportunity to hear from BP, ConocoPhillips or ExxonMobil, the three largest oil companies operating in the State of Alaska and predominant recipients of the tax credits under discussion here.

Under ACES, Alaska agreed to provide extremely generous tax credits and deductions (experts have said the most generous in the world - providing credits and deductions of as much as 85% of oil company costs) in exchange for a higher percentage of profits to state coffers as oil prices increased.

However, under our new oil tax system, SB21, we continue these generous credits and deductions while taking away the upside benefits to the State at higher oil prices. Alaskans were promised these changes would be a good deal for the State, as they would lead to increased oil production, thus making up the lost revenue in volume. However, while some new projects have come online (which one could argue were planned under ACES), the Director of DOR's Tax Division testified we can still expect oil declines of 5% per year well into the future. Instead of the million barrels of oil promised as part of our new tax structure, we are now told we can expect about 250,000 barrels in ten years.

As seen in recent SEC disclosures, Alaska remains one of the most profitable places in the world for the oil industry to do business. Through our tax credit and deduction system, we have virtually guaranteed the oil industry a profit via our massive subsidies, yet we get little in return for this guarantee when oil prices rise. The system is so generous that now bankrupt Buccaneer Energy's Chairman once infamously bragged at an industry conference that Alaska is "about the closest thing you're going to get to free money from a government in the world."

There is no other oil jurisdiction in the world with such a massively imbalanced system as Alaska. Alaska has often been compared to North Dakota, and we have often heard that we need to be competitive with North Dakota's oil tax structure. Yet if Alaska had North Dakota's tax and royalty structure, the oil industry would be paying roughly double (another $2 billion) than what they are currently paying. Instead, the State of Alaska is now socializing the oil industry's risk while privatizing the profits. This is simply not sustainable and must be changed.

There are a number of ways our broken oil and gas tax system could be fixed. In the near term, Representative Les Gara and I have proposed emergency legislation to stem some of our losses over the next two years (see HB 174, SB 96). Some of our suggestions, reflected as provisions in the bill, include instituting a higher minimum gross tax and temporarily reducing the deductible tax credits for the three most profitable fields on the North Slope. With one session remaining in the 29th Legislature, and this being extremely topical as we face a severe budget deficit, I look forward to timely hearings on this important and necessary legislation.

Regarding the refundable tax credits, there are a number of ways to improve this system. The State could continue to provide these tax credits, but only to those companies that prove their project is not financially feasible without them. We could take an equity stake in exchange for these credits. We could increase our royalty rates in exchange for credits. There are many creative ways we could address this situation.

While I appreciate the efforts made to start the conversation, I am afraid Oil and Gas Tax Credit Working Group missed an opportunity to try and address our broken system. As mentioned above, arguably the largest issue with our tax structure is in fact the deductible tax credits, yet there were no hearings fully devoted to this section of statute. It is my hope that in sharing these recommendations with you in writing, this issue may still be addressed in this body's final report and perhaps in future meetings, should the Working Group continue to meet. I appreciate your attention to this matter, as failure to make changes in these areas will cost the State billions.

Thank you again for the opportunity to participate and provide comment. I look forward to working together this upcoming session to repair our tax credit system in the best interest of Alaskans.

Thank you for your consideration,

Bill Wielechowski

Senator Bill Wielechowski