

Alaska Oil and Gas Association



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COMMENTS OF THE ALASKA OIL & GAS ASSOCIATION
ON HB 3001
HOUSE ENERGY & RESOURCES COMMITTEES
APRIL 25, 2012

Co-Chairmen Seaton, Feige, and Foster, Members of the Committee: good afternoon. For the record, my name is Kara Moriarty and I'm the Executive Director of the Alaska Oil and Gas Association (AOGA). Thank you for the invitation and opportunity to testify.

AOGA is a business trade association whose mission is to foster the long-term viability of the oil and gas industry for the benefit of all Alaskans. Our 16 member companies are a diverse group of companies with both an on-shore and off-shore presence, in Cook Inlet and on the North Slope, from legacy companies to new entrants to Alaska. We also represent the three in-state refineries and Alyeska Pipeline Service Company.

All told, AOGA's members hold active leases for more than 1.2 million acres of state land. There is little doubt we represent the majority of oil and gas exploration, production, transportation, refining and marketing activities in Alaska.

One of the key purposes of AOGA is to provide a forum for the discussion of matters of general interest to its members, and it is the policy of AOGA that there has to be 100% consensus before any positions are taken on tax policy matters.

AOGA did not support the changes that were made to the production tax system in 2006 and 2007. We believed then and we believe now that the current tax makes Alaska uncompetitive for investment dollars for long-term development and production. All of my member companies, from explorers like Repsol, to refineries like Flint Hills, to producers like Pioneer and BP believe meaningful changes to the tax system are necessary to stem the decline in oil production.

Today's testimony marks the sixth time AOGA has officially testified before the 27th Legislature on the need for oil tax reform. Throughout our testimony to the Legislature and to the public at large, we have stressed that declining production is a problem that cannot be ignored.

(Decline graph) This graph shows the historical production in the past decade, with the Department of Revenue's forecast for the next decade. If one examines the past three

years a bit closer, you will find that production is declining by just under 40,000 barrels per day. The DOR forecast is predicting that in the next decade, almost half of our production will be from “new oil” – oil yet to be developed. In fact, the latest Spring 2012 forecast is showing by next fiscal year, 71,000 barrels per day of new oil will be in production.

Our question is where is this new oil going to come from, especially in the short term? The two newest fields – Oooguruk and Nikaitchuq – are each expected to peak at around 20,000 – 28,000 barrels per day. As I just mentioned, the current production decline in the last three years is about the same as these two new fields combined. In other words, to simply offset the decline, two new fields like Oooguruk and Nikaitchuq would need to come into production each year, but to my knowledge, there are no new fields expected to produce oil in the next 3-5 years.

In 2006 and 2007, many companies testified that ACES would not attract the investment Alaska needs to change the production curve. Unfortunately, this prediction came true. In fact, production is significantly lower today than what Alaska was forecasting when it passed ACES in 2007.

(Actual vs. forecast chart) This chart indicates that the forecast in 2007 was predicting Alaska’s production was going to be 754,000 barrels per day in 2011. The actual production was 603,000.

(Industry investment chart) Industry investment has remained stagnant over the last three years. Capital investment has averaged \$1.7 billion for the last three years, which (show declining production chart) in the same three years resulted in the loss of about 40,000 barrels per day. Current investment levels are not even stemming our production decline, let alone increasing production.

Without bold and meaningful reforms, Alaska’s production will continue to decline at a rate that, according to the Office of Management and Budget, creates potential deficits as early as 2015 growing larger in each succeeding year. From AOGA’s perspective we have a production problem that will soon result in a serious revenue problem for the state.

AOGA’s member companies and others have been testifying about what is happening with their businesses on the North Slope, about the interrelationship between levels of new investment each year and the rate of decline in ANS production, and about the effects taxes have on investment decisions. These explanations are not threats, but they are not bluffs either. They have been candid attempts to describe to you how those companies evaluate their investment opportunities here against their opportunities elsewhere, and how Alaska’s tax regime can influence the decisions about which opportunities to take.

The Legislature's consultants also explained how investment decisions are made last Saturday before this committee and gave a similar conclusion that investment decisions reflect the expectations of the companies' respective shareholders that companies will choose the opportunities that it perceives to be best, all things considered – including taxes. If an Alaskan opportunity is better than one elsewhere and there is enough budgeted money for only one of them, the shareholders expect, and in a very real sense demand, that the Alaska opportunity be taken. The reductions in the level of companies' investments in Alaska since the enactment of ACES are not any kind of retaliation for ACES' enactment, nor does a company cut back here to prove a point. The investments are nothing more, and nothing less, than the results of the competition of the Alaskan opportunities against opportunities elsewhere.

Declining production is a Slope-wide problem that needs a Slope-wide solution. AOGCC Commissioner John Norman described Alaska's legacy fields as "an anchor tenant" and we continue to provide the analogy that the North Slope oil province is like a tree, with the two great legacy fields being its trunk, and with the other fields being branches rising out of the trunk. If one peels the bark off all the way around the trunk and make it unhealthy, all the other branches will become unhealthy too, no matter how robust they might have been if the trunk had stayed strong.

(Rich in resources slide) If one looks at the resources remaining on the North Slope, we should be encouraged. In fact, our legacy fields, our "trunk" per se, hold the most promise. In addition, at these record high oil prices, we should see a flurry of activity to get these resources to market.

The producers of the existing non-legacy fields on the Slope, and the developers of any new fields that may be discovered, need as much production as possible flowing from the legacy fields through the TAPS oil pipeline in order to keep the costs affordable to ship their oil from the Slope to its refinery destinations. High transportation costs could cripple the economics of any new fields that might be found, as well as the economics of non-legacy fields currently in production.

Alaska needs to appreciate the North Slope production problem with a great level of concern and react with bold and meaningful reforms. Without comprehensive reform for the legacy fields as well as the other production, the bark will continue to be peeled off the tree trunk, harming the entire tree.

Tax policy does affect business decisions. The competition for these dollars is real, and we encourage the committee to put Alaska in a better and more competitive position, for near-term and long-term production.

HB 3001 recognizes the overall government take in Alaska is too high and does provide meaningful reform. We recognize that a solution that benefits all fields may not reached this special session because the Legislature seems to be so fractured on this issue.

However, AOGA will continue to work with the legislature now, in the interim, and into the future until meaningful reform is reached for all fields on the North Slope.

Thank you for the opportunity to testify and I'm happy to take any questions the committee may have.