



121 W. Fireweed Lane, Suite 207  
Anchorage, Alaska 99503-2035  
Phone: (907) 272-1481 Fax: (907) 279-8114  
*Kara Moriarty, President/CEO*

October 8, 2017

Via email: [john.larsen@alaska.gov](mailto:john.larsen@alaska.gov)

John Larsen  
Alaska Department of Revenue  
550 West 7th Ave., Suite 500  
Anchorage, AK 99501

Re: Exploration expenditures for carried-forward annual loss

Dear Mr. Larsen:

The Alaska Oil and Gas Association is submitting this to offer suggestions regarding regulations to implement AS 43.55.165(s), which was passed as part of House Bill 111. AS 43.55.165(s) provides:

(s) In adopting a regulation that defines the lease or property where a lease expenditure resulting in a carried-forward loss is incurred for the purpose of (o) and (p) of this section, the department shall include an exploration lease expenditure that is reasonably related to the lease or property. [emphasis added]

This subsection shows that the legislature recognized that exploration activities necessarily cover much larger areas than just the lease or property that later commences production. This is simply the nature of exploration work, which is needed to locate, define and de-risk prospects to bring them into development and production. The legislature intended that the exploration expenditure need only be “reasonably related” to the lease or property for purposes of the carried-forward annual loss.

We recognize that it would be daunting to set forth a reasonable list of criteria or requirements regarding what would be “reasonably related” that would impart the flexibility needed to address exploration programs, and doing so would create additional complexity and uncertainty rather than clear rules that enable projects to advance. Such an approach would also result in otherwise unnecessary disputes about what costs are “reasonably related” to the lease or property that commences production.

Accordingly, for purposes of determining what would be “reasonably related,” we suggest looking to principles that already exist in current law based on whether the cost is incurred for exploring on the North Slope or in Middle Earth. In other words, consistent with AS 43.55.165(b)(2), an exploration lease expenditure is reasonably related to the lease or property if it is for exploration in the same area of the state, either: (i) land north of 68 degrees North

latitude; or (ii) land outside the Cook Inlet sedimentary basin not including any land north of 68 degrees North latitude, regardless of where the exploration lease expenditure was incurred.

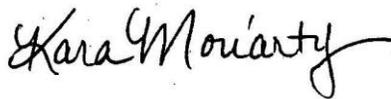
Please note that there remain a number of questions regarding the allocation of losses between properties within the areas of the state described above, producing or otherwise. We look forward to discussing this separate issue with the department.

We also suggest that it would be worth defining “exploration lease expenditure” to help clarify what costs would be eligible. Given the legislature’s intent to recognize that exploration work should be treated differently, we would suggest that this be defined to broadly include any exploration work that is not otherwise defined as development or production operations<sup>1</sup> to, for example, include any surveying, exploration drilling and geological and geophysical exploration activities, including the analyzing and processing of the data obtained from these activities.

In addition, although it is unlikely that a party would be interested in purchasing an explorer simply to obtain the explorer’s carried-forward annual loss, that concern was expressed. The concern could be met by a regulation providing that the successor may apply the loss once regular production ultimately commences from any of the leases or properties that were owned or explored by the predecessor during the prior year(s) in which the loss was incurred.

Thank you for considering these suggestions.

Sincerely,



Kara Moriarty  
President/CEO

Cc: Commissioner Sheldon Fisher, Department of Revenue  
Division Director Ken Alper, Department of Revenue

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<sup>1</sup> See 15 AAC 55.900(a)(23); and 15 AAC 55.900(a)(26).