PRODUCTION TAX CREDITS

PRESENTATION TO THE
HOUSE FINANCE COMMITTEE
FEBRUARY 10, 2011
Overview

- Types of Production Tax Credits
  - Credits Applied Against Production Tax Liability
  - Transferable Tax Credit Certificates
  - Cash Refunds History
Types of Production Tax Credits

Credits which may be taken against oil and gas production taxes include:

- Capital Expenditure Credits
- Alternative Tax Credits for Oil and Gas Exploration
- Net Operating Loss ("NOL") Carry Forward Credits
- Transitional Investment Expenditure ("TIE") Credit
- Additional Nontransferable Tax Credits
- Well Lease Expenditures Credit
- Cook Inlet Jack-up Rig Credit
Timelines for Production Tax Credits

- 43.55.023(a) QCE and (b) CFAL credits
- 43.55.023(l) 40% Well Lease Exp (Cl)
- 43.55.023(l) TIE credits (PPT)
- 43.55.023(l) TIE credits (ACES)
- 43.55.024(a) New Area Development credit
- 43.55.024(c) small producer credit
- 43.55.025 (20%/40%) credit for expl
- 43.55.025 (30%/40%) credit for expl
- 43.55.025 (l) Cook Inlet Jack-up Rig Credit

Department of Revenue
2/10/2011
Types of Production Tax Credits

**Capital Expenditure Credits** - (AS 43.55.023(a)(1))
- **20%** of qualified capital expenditures (QCE)
- QCE include drilling, construction of facilities, new equipment, etc.
- Same expenditures may also qualify for NOL Carry Forward Credit
- Same expenditures do **not** qualify for exploration credit
- Must be spread over 2 years (except for expenditures incurred south of 68 degrees North latitude – effective July 1, 2010)
- Credits may be cashed or transferred
Types of Production Tax Credits

Exploration Credits

- Two Main Types
  - Capital Credit for Exploration Activity 43.55.023(a)(2) (20%)
  - Alternative Tax Credits for Oil and Gas Exploration 43.55.025 (30%-40%)
Types of Production Tax Credits

Capital Credit for Exploration Activity 43.55.023(a)(2)

- **20%** of qualifying expenditures
- Qualifying expenditures related to geologic and geophysical exploration, or in connection with an exploration well
- Must be spread across 2 years (except for expenditures incurred south of 68 degrees North latitude – effective July 1, 2010)
- Same expenditures may also qualify for NOL Carry Forward Credits
- Credits may be cashed or transferred
Types of Production Tax Credits

Exploration Credits

- Two Main Types
  - Capital Credit for Exploration Activity under 43.55.023(a)(2) (20%)
  - Alternative Tax Credits for Oil and Gas Exploration under 43.55.025 (30%-40%)
Types of Production Tax Credits

Alternative Tax Credits for Oil and Gas Exploration - 43.55.025

- 30% - 40% of qualified expenditures depending on well location and proximity to existing wells and unit boundaries
- Qualified expenditures include certain expenses associated with seismic and geophysical exploration work, and exploration well drilling
- Same expenditures may also qualify for NOL Carry Forward Credit
- Same expenditures do **not** qualify for Capital Expenditure Credit
- To receive credit, taxpayer must provide certain well data to DNR
- Expires 2016
- Credits may be cashed or transferred
Types of Production Tax Credits

**NOL Carry Forward Credit - 43.55.023(b)**

- **25%** of net operating loss
- Applied against tax liability in following year
- Credit based on adjusted lease expenditures which include both operating and capital expenses
- Includes capital expenditures which also qualify for qualified capital expenditure credit under 43.55.023(a)(1) and exploration credit under 43.55.023(a)(2)
- Credits may be cashed or transferred
Types of Production Tax Credits

Transitional Investment Expenditure (TIE) Credits
43.55.023(i)

- Credit equals 20% of qualifying capital expenditures:
  - incurred between March 31, 2001 and April 1, 2006, and
  - not exceeding 10% of the capital expenditures incurred between March 31, 2006 and January 1, 2008.

- Revised under Aces to cover only producer or explorer not having production prior to January 1, 2008

- Credits are not transferable and may not be carried forward beyond 2013

- Same capital expenditures may not qualify for exploration credit under 43.55.025
Types of Production Tax Credits

Additional Nontransferable Tax Credit- 43.55.024(a)

- Referred to as “New Area Development” credit
- Up to $6 million
- Available for companies producing from leases or properties outside of Cook Inlet and North Slope
- Credit can only be applied against tax liability
- Expires 2016 or 9 years after first commercial oil or gas production if before May 1, 2016
- Credits may not be cashed or transferred or carried forward
Types of Production Tax Credits

Small Producer Credit - 43.55.024(c)

- Up to $12 million, depending upon level of production
- Available for companies producing less than 100,000 bbl/day of oil BTU-equivalent
- Production not restricted by region
- Credit can only be applied against tax liability
- Expires 2016 or 9 years after first commercial oil or gas production if before May 1, 2016
- Credits may not be cashed or transferred or carried forward
Well Lease Expenditure Credit - 43.55.023(I)

- 40% of well lease expenditures incurred in the state south of 68 degrees north latitude
- Must be intangible drilling costs or geological/geophysical exploration
- Credit may be applied against tax liability, or certificated and cashed or transferred to another taxpayer
Cook Inlet Jack-Up Rig Credit - 43.55.025(l)

- Credit of 100%/90%/80% of up to $25 million each of exploration expenditures for first 3 unaffiliated persons drilling wells using the same jack up rig penetrating and evaluating prospects in the pre-Tertiary zone.
- Taxpayer obtaining credit may not claim .023 credit for same expenditures
- 50% of credit to be repaid over 10 year period if well yields sustained production
Overview

- Types of Production Tax Credits
- **Credits Applied Against Production Tax Liability**
- Transferable Tax Credit Certificates
- Cash Refunds History
Credits Applied Against Production Tax Liability

Credits may be redeemed in two ways:

(1) All Credits may be applied against production tax liability
   - Capital Expenditure and Capital Exploration Credits split over two years
     (except south of 68 degree North latitude – eff. July 1, 2010)
   - NOL, TIE, Small Producer and Alternative Tax Credits for Oil and Gas
     Exploration may all be applied against tax liability in total in a single year

(2) Some Credits may be converted into a transferable Tax Credit Certificate
   - Capital Expenditure, Capital Exploration, NOL, and Alternative Tax Credits for
     Oil and Gas Exploration are convertible to tax certificates
   - Capital Expenditure, Capital Exploration and NOL Tax Credit Certificates must
     be applied over two years (except south of 68 degrees North latitude –
     passed 2010)
   - Alternative Tax Credits for Oil and Gas Exploration Certificates can be used in
     single year
Production Tax Credits Applied Against Tax Liability (Fiscal Year)

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011*</th>
<th>Total</th>
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</thead>
<tbody>
<tr>
<td>Capital Expenditure</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Credit</td>
<td>65</td>
<td>227</td>
<td>219</td>
<td>280</td>
<td>349</td>
<td>391</td>
<td>1,329</td>
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<tr>
<td>TIE Credits</td>
<td>33</td>
<td>138</td>
<td>73</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>243</td>
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<tr>
<td>Small Producer Credits</td>
<td>9</td>
<td>37</td>
<td>30</td>
<td>26</td>
<td>28</td>
<td>40</td>
<td>155</td>
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<tr>
<td>Exploration Credits</td>
<td>1</td>
<td>47</td>
<td>55</td>
<td>28</td>
<td>34</td>
<td>20</td>
<td>169</td>
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<tr>
<td>Totals</td>
<td>107</td>
<td>449</td>
<td>375</td>
<td>333</td>
<td>417</td>
<td>450</td>
<td>1,896</td>
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</tbody>
</table>

* Estimated
Production Tax Credits Applied Against Tax Liability (Fiscal Year)

* Estimated pending final true-up of 2010 tax filing and estimated capital spending for FY 2011.
Overview

- Types of Production Tax Credits
- Credits Applied Against Production Tax Liability
- Transferable Tax Credit Certificates
- Cash Refunds History
Timeline for processing of Transferable Credit under AS 43.55.023 (a)

- Taxpayer Incurs Expenditures
- Apply for TTCC 1st Qtr
- Apply for TTCC 2nd Qtr
- Apply for TTCC 3rd Qtr
- Apply for TTCC 4th Qtr
- DOR Processing of application
- Apply for Cash
Timeline for processing a Transferable Tax Credit Certificate under AS 43.55.023(b)

- Producer/Explorer Incurs Expenditures
- Tax credit application processed
- Producer/Explorer Applies for Cash
Timeline for Application for AS 43.55.025 Alternative Credit for Oil and Gas Exploration

- Explore / seismic
- Apply
- Audit / Issue Certificate
- Apply to Tax Liab
- Apply for Cash
Transferable Tax Credit Certificates

Companies may also claim tax credits by applying for a Transferable Tax Credit Certificate (TTCC)

- Available to companies (explorers) with no tax liability to which credits can be applied
- Tax Credit Certificates under 43.55.023(a) and (b) must be split or applied over two years (except credits issued for expenditures incurred south of 68 degrees North latitude effective July 1, 2010)
- May be transferred to another taxpayer or cashed with the state
## Production Tax Credits Under AS 43.55 Claimed by FY ($M)

<table>
<thead>
<tr>
<th>Credit Type</th>
<th>Pre-2007</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011*</th>
<th>Total</th>
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<tbody>
<tr>
<td>Capital Expenditure</td>
<td>68.2</td>
<td>91.7</td>
<td>109.6</td>
<td>168.0</td>
<td>72.8</td>
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<td>510.3</td>
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<td>-.023(a)</td>
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<tr>
<td>Net Operating Loss</td>
<td>38.1</td>
<td>148.5</td>
<td>153.5</td>
<td>138.7</td>
<td>.2</td>
<td></td>
<td>479.0</td>
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<td>.023(b)</td>
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<tr>
<td>Well Lease Expenditure</td>
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<td></td>
<td>5.8</td>
<td>5.8</td>
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<td>-.023(l)</td>
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<tr>
<td>Exploration -.025</td>
<td>48.3</td>
<td>44.9</td>
<td>38.5</td>
<td>56.6</td>
<td>99.5</td>
<td>2.4</td>
<td>290.2</td>
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<tr>
<td>Total</td>
<td>48.3</td>
<td>151.3</td>
<td>278.6</td>
<td>319.7</td>
<td>406.2</td>
<td>81.3</td>
<td>1285.3</td>
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* Applications received through January 4, 2011.
Transferable Tax Credit Certificates

Tax Credits Claimed by FY ($M)

Note: Applications received through January 4, 2011
## Transferable Tax Credit Certificate Activity by Fiscal Year ($M)

<table>
<thead>
<tr>
<th></th>
<th>Pre-2007</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011*</th>
<th>Total</th>
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<tbody>
<tr>
<td>Issued</td>
<td>16.2</td>
<td>99.9</td>
<td>130.8</td>
<td>308.2</td>
<td>361.3</td>
<td>191.5</td>
<td>1,107.9</td>
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<tr>
<td>Refunded</td>
<td>(54.6)</td>
<td>(54.1)</td>
<td>(193.1)</td>
<td>(250.5)</td>
<td>(299.3)</td>
<td>(851.6)</td>
<td></td>
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<tr>
<td>Transferred/</td>
<td>(12.3)</td>
<td>(40.0)</td>
<td>(46.6)</td>
<td>(20.0)</td>
<td>(1.2)</td>
<td>(62.7)</td>
<td>(182.8)</td>
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<td>Applied to Taxes</td>
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<tr>
<td>Activity by year</td>
<td>3.9</td>
<td>5.2</td>
<td>30.1</td>
<td>95.1</td>
<td>109.6</td>
<td>(170.4)</td>
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<tr>
<td>Transferable</td>
<td>3.9</td>
<td>9.1</td>
<td>39.2</td>
<td>134.2</td>
<td>243.9</td>
<td>73.4</td>
<td>73.4</td>
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<td>Tax Credit</td>
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<tr>
<td>Outstanding</td>
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</table>

*Payment activity through February 4, 2011.
Overview

- Types of Production Tax Credits
- Credits Applied Against Production Tax Liability
- Transferable Tax Credit Certificates (TTCC)
- Cash Refunds History
Cash Refunds History

Cash Refunds Governed by AS 43.55.028:
• To cash must be usable against tax liability
• Must show subsequent (24 months) QCEs or lease bids equal to cash sought (repealed in 2010)
• Have a zero tax owed in current and past years
• Have no more than 50,000 BOE/d
Cash Refunds History

Tax Credits Purchased

By fiscal year ($M)

- 2007 $ 54.6
- 2008 54.1
- 2009 193.1
- 2010 250.5
- 2011 (thru 02/04/11) 299.3

TOTAL $851.6
Cash Refunds History

Oil & Gas Tax Credit Fund

Appropriations - $ 904 M
Tax Credit Purchases (TC Fund) (772) M
Tax Credit Purchases (GF) (79) M
Interest Earned 22 M
Balance $ 75 M
Impact of Production Tax Credits
Total State Stimulus

* Estimated

Includes $67.5M estimate for Cook Inlet Jack-Up rig credit
Capital Expenditures by Year ($M)

- 2006: $1,837
- 2007: $2,011
- 2008: $2,044
- 2009: $2,233
- 2010*: $2,523
- 2011*: $2,761
- 2012*: $3,137

*Estimated based on forecast data.