PPT Effects in Cook Inlet

Presentation to

South Central Alaska Energy Forum

William Nebesky and Greg Bidwell
Division of Oil and Gas

September 20, 2006

Alaska Department of
Natural
Resources

Major Points Covered In Presentation

A. PPT Basics
B. Cook Inlet Provisions
C. Cook Inlet Example
D. Conclusions

PPT Basics (#1)

- Tax on a producer's net upstream Alaska income
  - Net upstream income = "Production tax value" = "gross value at point of production" minus "lease expenditures"
- *Base PPT Tax* is 22.5% of production tax value
- *Minimum Tax* based on percentage of gross value at point of production
  - Floor applies to North Slope, only

PPT Basics (#2)

- *Supplemental "Progressive" Tax* on production tax value assessed at higher oil prices
  - Above $40/ bbl production tax value
- *Credits* reduce tax liability or generate tradable tax benefits

Production Tax Value

- Destination Market Price (downstream)
  - Prevailing Value or Proceeds in Cook Inlet
  - Royalty Barrels deducted prior to tax calculation
  - ANS West Coast spot price

- *Gross Value at Point of Production (netted back)*
  - Or at lease boundary
  - Royalty barrels deducted prior to tax calculation
  - Subtract cost of pipeline and marine transportation

- Subtract *Lease Expenditure (*upstream)
  - Capital Expenditures (less 30 ¢ per Bbl)
  - Operating Expenditures
  - Property and Conservation Surcharge Taxes

PPT Differs by Area, Taxpayer

- PPT in North Slope is a combined oil and gas upstream profits tax
  - No separate oil and gas tax rate
  - Tax on a company basis, not a field basis
- PPT tax liability in Cook Inlet capped for oil and gas separately
- PPT in new areas gets its own distinct credit
- It pays to be small: Producers with less production get a distinct credit

Summary of Main Elements

- *Gross Value at the Point of Production*
- *Lease Expenditures*
- *Production Tax Value*
- *Minimum Tax* or *"Capped" Tax* (in CIB)
- *Progressive Supplemental Tax*
- *Credits*
  - *Transferable*
    - *Qualified CapEx Credit*
    - *Loss Carry-forward*
  - *Non-Transferable*
    - *Small Producer*
    - *New Area Credit*
    - *Transition Investment Credit*

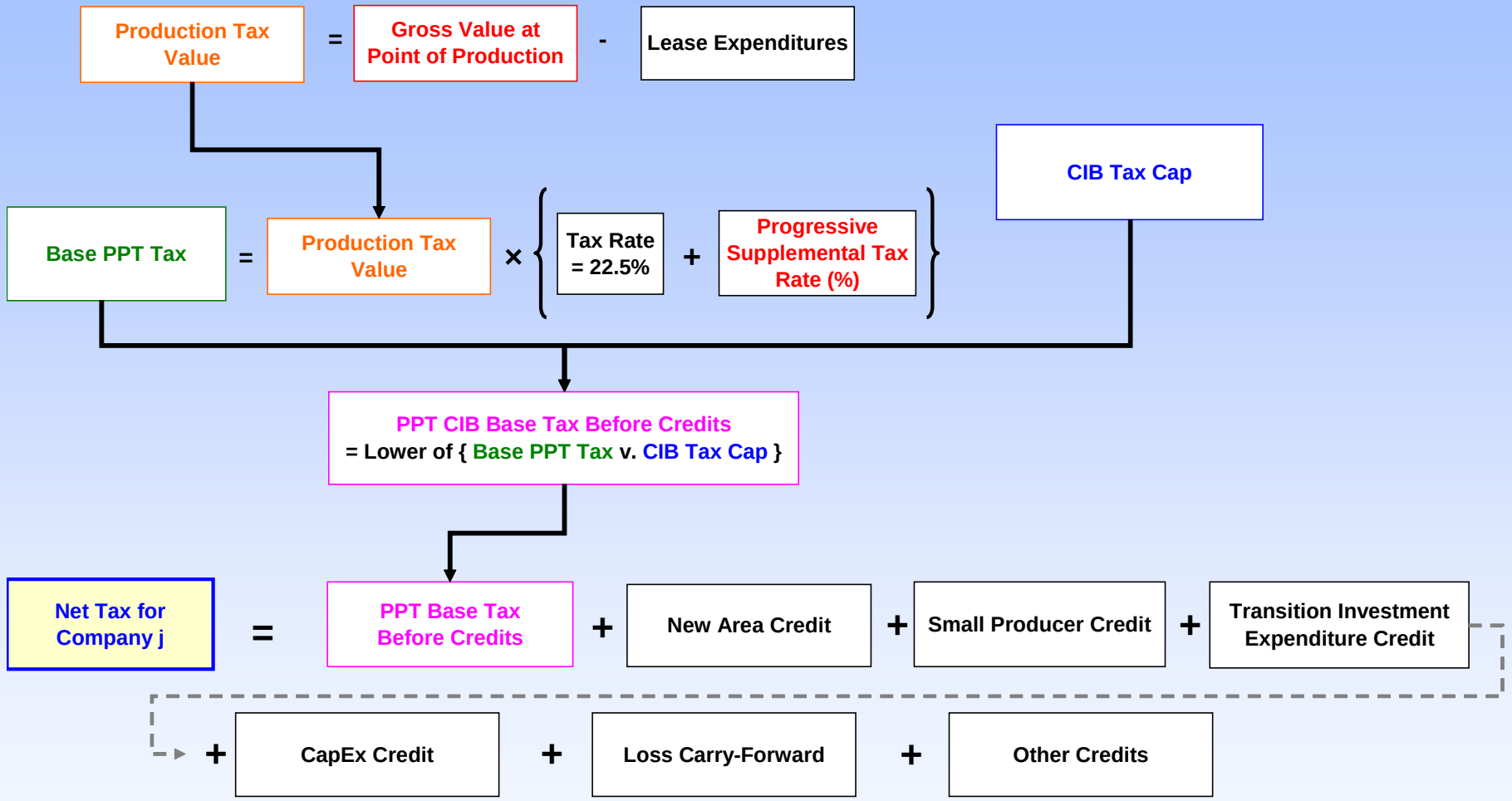
PPT "*Tax Cap*" for Cook Inlet

- Fossilized ~2005 per-unit Tax Liability
  - ELF oil tax cap
  - ELF gas tax cap
- Cap applied to oil and gas separately
- Cap applies to *Base PPT Tax* liability plus *Progressive Supplemental* element
- CIB Cap replaces *Minimum Tax* provisions

Cook Inlet Producers Benefit from Credits Despite "Capped" Tax

- PPT *Transferable Tax Credits* not limited by operation of the "Cap"
  - Qualified CapEx Credit
  - Loss Carry-forward Credit
- Other *Transferable Tax Credits* are limited by *Tax Savings* caused by operation of the *Cap*
  - AS 43.55.025 (20/40% Exploration Credits)
- *Small Producer Credit* could be limited
  - Non-Transferable
  - Allocated to field based on volume
    - Can't apply a field's unused credits to another field's tax

PPT Flow Chart – Cook Inlet



Cook Inlet Example - The Setup

- One Producer, Four Fields
- One-Year Time Period
- Gas Only, ELF range = 0 – 0.68
- 2005 Price Received = $3.50 per mcf
- Transition Investments – None
- Three Cases Depending on Following in Current Year
  - Price
  - CapEx
  - Volume

Table 1. Tax Cap Calculation

Fields	ELF	Effective Tax Rate	$Q_{INITIAL}$	Q_T	$P_{INITIAL}$	Tax Cap per Unit	Tax Cap
		10%	Mmcfd	Mmcfd	$ per Mcf		$ Millions
				5	$3.50		
A	0.68	6.8%	20	25		$0.24	$5.9
B	0.45	4.5%	15	20		$0.16	$3.1
C	0.00	0.0%	5	10		$0.00	$0.0
D	0.20	2.0%	10	15		$0.07	$1.1

CASE #1

Table 2. Production Tax Value and Base PPT Liability per Field

$P_{CURRENT}$ = **$8.00** $ per Mcf

		Lease Expend					
Fields	**GVPOP**	**$CapEx_T$**	**OpEx & Other**	**PTV[1]**	**Base Tax Liability**	**Supp Tax**	**Total PPT Liability**
	$ Millions	$ Millions	$ Millions	$ Millions	$ Millions	$ Millions	
					22.5%	**2.0%**	
A	**$73.0**	**$7.5**	**$3.8**	**$62.21**	**$14.0**	**$1.2**	**$15.2**
B	**$58.4**	**$7.5**	**$3.8**	**$47.52**	**$10.7**	**$1.0**	**$11.6**
C	**$29.2**	**$7.5**	**$3.8**	**$18.13**	**$4.1**	**$0.4**	**$4.4**
D	**$43.8**	**$7.5**	**$3.8**	**$32.82**	**$7.4**	**$0.7**	**$8.0**
	$204.4	**$30.0**	**$15.0**	**$160.68**	**$36.2**	**$3.2**	**$39.4**

[1] **Adjusted for 30¢ per barrel CapEx exclusion.**

CASE #1

Table 3. PPT CIB Base Tax Before Credits

Fields	Tax Cap	Total PPT Liability	PPT BC	Cap Tax Savings
	$ Millions	$ Millions	$ Millions	$ Millions
A	$5.9	$15.2	$5.9	$9.3
B	$3.1	$11.6	$3.1	$8.5
C	$0.0	$4.4	$0.0	$4.4
D	$1.1	$8.0	$1.1	$7.0
			$10.1	$29.3

CASE #1

Table 4. Allocation of Small Producer Credit by Field

Fields	Q_T	Q_T % by Field	Amount of Potential SPC	PPT BC	Tax Liability After SPC
	Mmcfd	%	$ Millions	$ Millions	$ Millions
	5				
A	25	35.7%	$4.3	$5.9	$1.6
B	20	28.6%	$3.4	$3.1	$0.0
C	10	14.3%	$1.7	$0.0	$0.0
D	15	21.4%	$2.6	$1.1	$0.0
	70		$12.0	$10.1	$1.6

CASE #1

Table 5. PPT Credits

CapEx Credit		
$CapEx_T$	Credit %	Credit
$ Millions	20%	$ Millions
$28.7		$5.7

20/40 Transferable Credit		
	$ Millions	
	"Gross"	"Net"
	$0.0	$0.0

Loss Carry Forward Credit	
PTV Loss	Credit 20%
$ Millions	$ Millions
$0.0	$0.0

Small Producer Credit
$ Millions
$8.5

CASE #1

Table 6. Tax Cap Calculation

Fields	ELF	Effective Tax Rate	$Q_{INITIAL}$	Q_T	$P_{INITIAL}$	Tax Cap per Unit	Tax Cap
		10%	Mmcfd	Mmcfd	$ per Mcf		$ Millions
				-5	$3.50		
A	0.68	6.8%	20	15		$0.24	$3.5
B	0.45	4.5%	15	10		$0.16	$1.6
C	0.00	0.0%	5	0		$0.00	$0.0
D	0.20	2.0%	10	5		$0.07	$0.4

CASE #2

Table 7. Production Tax Value and Base PPT Liability per Field

$P_{CURRENT}$ = **$2.50** $ per Mcf

	Lease Expend						
Fields	**GVPOP**	**$CapEx_T$**	**OpEx & Other**	**PTV[1]**	**Base Tax Liability**	**Supp Tax**	**Total PPT Liability**
	$ Millions	$ Millions	$ Millions	$ Millions	$ Millions	$ Millions	
					22.5%	**0.0%**	
A	**$13.7**	**$15.0**	**$3.8**	**-$4.79**	**$0.0**	**$0.0**	**$0.0**
B	**$9.1**	**$15.0**	**$3.8**	**-$9.44**	**$0.0**	**$0.0**	**$0.0**
C	**$0.0**	**$15.0**	**$3.8**	**-$18.75**	**$0.0**	**$0.0**	**$0.0**
D	**$4.6**	**$15.0**	**$3.8**	**-$14.10**	**$0.0**	**$0.0**	**$0.0**
	$27.4	**$60.0**	**$15.0**	**-$47.08**	**$0.0**	**$0.0**	**$0.0**

[1] **Adjusted for 30¢ per barrel CapEx exclusion.**

CASE #2

Table 8. PPT CIB Base Tax Before Credits

Fields	Tax Cap	Total PPT Liability	PPT BC	Cap Tax Savings
	$ Millions	$ Millions	$ Millions	$ Millions
A	**$3.5**	**$0.0**	**$0.0**	**$0.0**
B	**$1.6**	**$0.0**	**$0.0**	**$0.0**
C	**$0.0**	**$0.0**	**$0.0**	**$0.0**
D	**$0.4**	**$0.0**	**$0.0**	**$0.0**
			$0.0	**$0.0**

CASE #2

Table 9. Allocation of Small Producer Credit by Field

Fields	Q_T	Q_T % by Field	Amount of Potential SPC	PPT BC	Tax Liability After SPC
	Mmcfd	%	$ Millions	$ Millions	$ Millions
	-5				
A	15	50.0%	$6.0	$0.0	$0.0
B	10	33.3%	$4.0	$0.0	$0.0
C	0	0.0%	$0.0	$0.0	$0.0
D	5	16.7%	$2.0	$0.0	$0.0
	30		$12.0	$0.0	$0.0

CASE #2

Table 10. PPT Credits

CapEx Credit		
$CapEx_T$	Credit %	Credit
$ Millions	20%	$ Millions
$59.5		$11.9

20/40 Transferable Credit	
$ Millions	
"Gross"	"Net"
$0.0	$0.0

Loss Carry Forward Credit	
PTV Loss	Credit 20%
$ Millions	$ Millions
-$47.1	$9.4

Small Producer Credit
$ Millions
$0.0

CASE #2

Table 11. Summary of PPT Effects

	Case 1	Case 2	Case 3
Price	$8.00	$2.50	$4.00
CapEx	$30.0	$60.0	$20.0
Volume Delta (Mmcfd)	5	-5	10
Tax Cap Savings	$29.3	$0.0	$9.7
Small Producer Credit	$8.5	$0.0	$8.7
Transf Credits Remaining	$5.7	$21.3	$3.7
Tax Liability	($1.6)	$0.0	($3.7)

Note, Case #3 detailed slides not shown.

Conclusions

- Many interdependent parts
- PPT Tax a major boon for Cook Inlet
- Best of both worlds: Base PPT Tax Liability is Capped and most PPT Credits Apply
- ELF and Price in 2005 Year is Fossilized in determining “Cap”