Tough questions unasked: Slipshod review justifies referendum on SB 21

By Richard A. Fineberg
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In a rhetoric-laden diatribe on behalf of oil industry tax cuts ("Signing off Alaska," Community perspective, July 3), Art and April Hackney claim that those who advocate repeal of the Legislature's recently enacted tax cut bill, Senate Bill 21, "are trying to inflame the public with outright lies" about that controversial measure. My response is based on a fact-based analysis, (subsequently posted as) The Disappearing Chart and Other Questions the Legislature Failed to Consider when the Legislative Majority Signed Off on SB 21 In the Last Days of the 2013 Legislative Session, text accompanied by slides. I presented this analysis at the Noel Wien Library July 1.

The Hackneys' self-proclaimed "irrefutable facts about the creation of SB21" included the following inaccurate and highly subjective adulation of the Legislature's work: "The Alaska Legislature, after unprecedented study and testimony, came to a compromise change to oil tax policy that was certainly not met with unbridled enthusiasm by the oil industry. Alaska's Clear and Equitable Share, the previous system, provided tax credits that SB21 took away. SB21 also created a more fair tax structure to encourage oil-field investment and create jobs for Alaskans."

This statement echoes the Republican Senate majority briefing claim that SB21 "went through an exhaustive committee process in the Senate before going to the House for review." But the legislative record indicates that legislators entertained endless rounds of glittering generalities about the need for tax cuts while ignoring key facts and failing to challenge misleading information.

For example, they ignored the extraordinary profitability record of ConocoPhillips, the North Slope's largest producer. They also failed to question a misleadingly labeled chart on taxes that ConocoPhillips presented to four committees considering SB21. Together with BP and Exxon Mobil, ConocoPhillips is one of the transnational companies that control approximately 95 percent of North Slope production and are expanding their ownership of the trans-Alaska pipeline system from 95 percent to 100 percent.

Contrary to the Hackneys' misinformation, tax credits that SB21 supposedly "took away" were actually revised. But instead of encouraging exploration, SB21 tax credits would go to producers. Since the major producers hold billions of barrels of oil reserves but have not stopped the production decline, the SB21 tax credit provisions may be an ill-advised policy shift away from a competitive situation, where independent investors would be encouraged to explore. Potential independent investors such as Dan Donkel of Florida and Rick Wagner of Fairbanks say that the state handicaps them while favoring the existing producers — and that the legislative committees did not give them sufficient time to testify on their views.

In sum, the Hackneys' supposedly "irrefutable facts:" (1) offered dubious assertions about the legislative process; (2) misinformed readers about a major provision of SB21; and (3) glossed over significant policy questions. The Hackneys followed this erroneous passage with vituperation, stating that “(t)here is simply no truth in the political agenda of (legislators ... whose agenda) could legitimately be called treasonous at a state level.”

North Slope oil production, declining for 25 years, is down to a quarter of its peak, while costs to produce remaining oil continue to rise. Tax cut advocates blame declining North Slope production on the tax code, despite the fact that North Slope producers have profited handsomely since production began in 1977.

The state’s cost-based and progressive production tax system was not adopted until 2006 and was modified in 2007. As a trade-off for allowing producers to recover all costs before the state assessed production taxes, progressivity kicked in after revenues exceeded net costs by $30 per barrel, enabling the state to recoup an increasing share of the gains from high prices. Under this system, since 2006 ConocoPhillips has reported profiting — steadily and mightily — from its Alaska operations.

In adopting SB21, the Legislature has abandoned progressivity without hard-number data to explain:

- Why the major producers need special tax cuts to produce more than 6 billion barrels of existing North Slope reserves.
- Whether oil already discovered should receive credits as new oil.
- Whether the beneficiaries of that tax cut will continue to invest their tax cut revenues in short-term profits elsewhere.
- Whether the state can effectively implement new revenue accounting systems (including distinguishing between new and existing oil and evaluating the new tax regime).
- Whether continued uncertainties and the new tax credit application to existing production will encourage or discourage long-term North Slope exploration and development.

Comment on North Slope Reserves added to this posting [August 5, 2013]

When she rose to speak during the question session near the end of my presentation at Noel Wien July 1, Rep. Tammie Wilson (Republican, North Pole) stressed her concerns about possible North Slope shutdown as she spoke in defense of the legislative adoption of SB21. For review of the dialogue with Rep. Wilson, see *Fairbanks News-Miner* columnist Dermot Cole’s July 2 post (reprinted in that newspaper July 7). Rep. Wilson claimed that she based here support of SB 21 on better information legislators gained from the Juneau legislative hearings, but she did not counter the facts I presented. Nor did she present relevant facts of her own.

During our exchange, I asked Rep. Wilson about North Slope oil reserves – a legacy of past North Slope development and a key factor in continued production. As reported by Dermot Cole, here is a portion of that exchange:

> …can you tell me what we have in North Slope reserves? Can you give me a number?” Fineberg asked.
> “No,” said Wilson.
> “Why not?” Fineberg said.

> “Because we’re still developing the North Slope. We’re drilling more wells, we’re finding more,” Wilson said.

When Rep. Wilson said she could not quantify proved oil reserves, she acknowledged that she was speaking in generalities. Estimates of North Slope reserves vary with factors that include oil prices and technological developments, as well as geologic conditions. Nevertheless, an estimate of proved reserves is a necessary component of assessing the prospects for continued production. The importance of understanding reserve estimates is underscored by recent reports from North Dakota, where industry representatives have threatened to leave that region unless that state grants tax cuts and producers are investigating how to use local reserves to lower the costs of production. This argument suggests that the large quantity of oil already discovered on the North Slope may be of significant benefit to producers holding those reserves – particularly when the major North Slope producers are holding infrastructure already in place.

It is possible that better information on North Slope reserves might have helped Rep. Wilson calm her fears about a possible North Slope shutdown. On the other hand, a look at the reserves picture indicates that we are once again dealing with inadequate information: In its May 29 decision on TAPS valuation for property tax assessment, the State Assessment Review Board (SARB) cites a North Slope reserve estimate of more than 6 billion barrels of proven reserves, based on best evidence in the latest of a series of court cases on TAPS property tax valuation. In issuing that finding, SARB criticized the Department of Revenue for failing to use court decisions to refine its estimates of production reserves. According to SARB, the Department of Revenue ignored the court finding on reserves, valuing TAPS on the assumption of only 3.86 billion barrels of reserves, without explaining the reduction of 2.59 billion barrels or justifying its lower estimate.

In this regard note that the state Department of Natural Resources is no longer making North Slope reserve estimates readily available. In 2010 that department’s Division of Oil & Gas annual report listed 5.1 billion barrels of oil reserves by field, based on the Dept. of Revenue’s 2010 in-house forecast. But the Oil & Gas division’s estimate of North Slope reserves quietly vanished in 2011, replaced by a 2005 U.S. Geological Survey table estimating “Undiscovered, Technically Recoverable, Conventional Oil and Gas.” The shift from proved reserves to older data on undiscovered resources – a very different category – does not seem consistent with the Division of Oil & Gas report’s stated top goal: “to produce high quality data, analyses and interpretations, and decisions that are relevant, consistent, defensible and timely.”

To get the best handle on the future, citizens need the best possible numbers. But in this case, once again the state and the industry have failed to deliver those numbers, creating a condition that further compounds the problems of assessing future assessments that are, by definition, fraught with uncertainty. In sum, although she failed to bring an “A” game to the presentation July 1, Rep. Wilson added another example to the list of inadequate information, oversimplified and sometimes misleading charts that I shared with those in attendance July 1 and subsequently documented in *The Disappearing Chart* and my April 8 report on SB 21.

Richard Fineberg is an independent oil and gas policy analyst who lives in Ester. He has consulted and reported on North Slope development and trans-Alaska oil pipeline issues since 1975.