



**Cook Inlet:
Taxes and Other Issues
Ben Schoffmann**

RDC
May 4, 2006

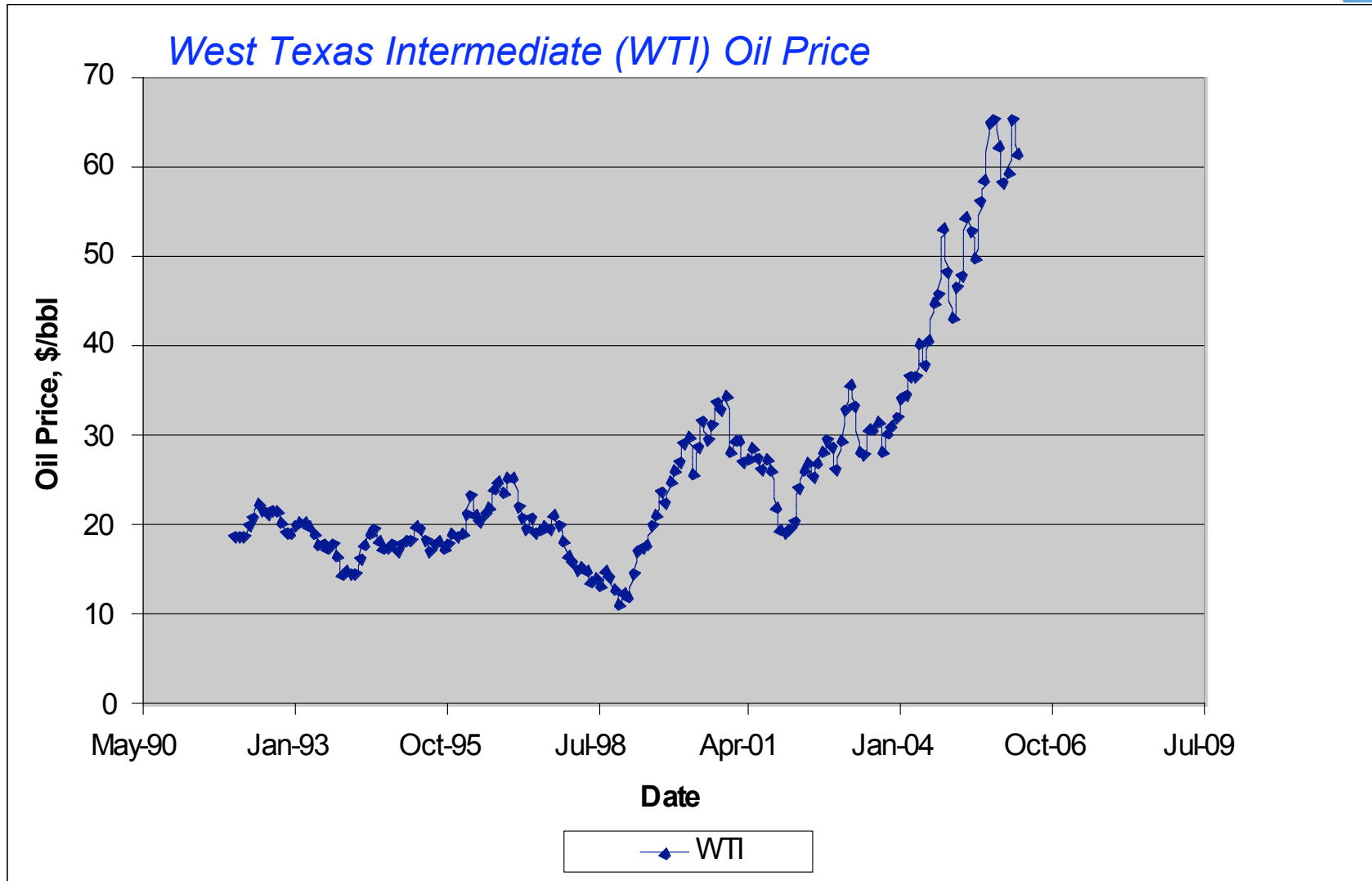
Marathon 

Presentation Topics

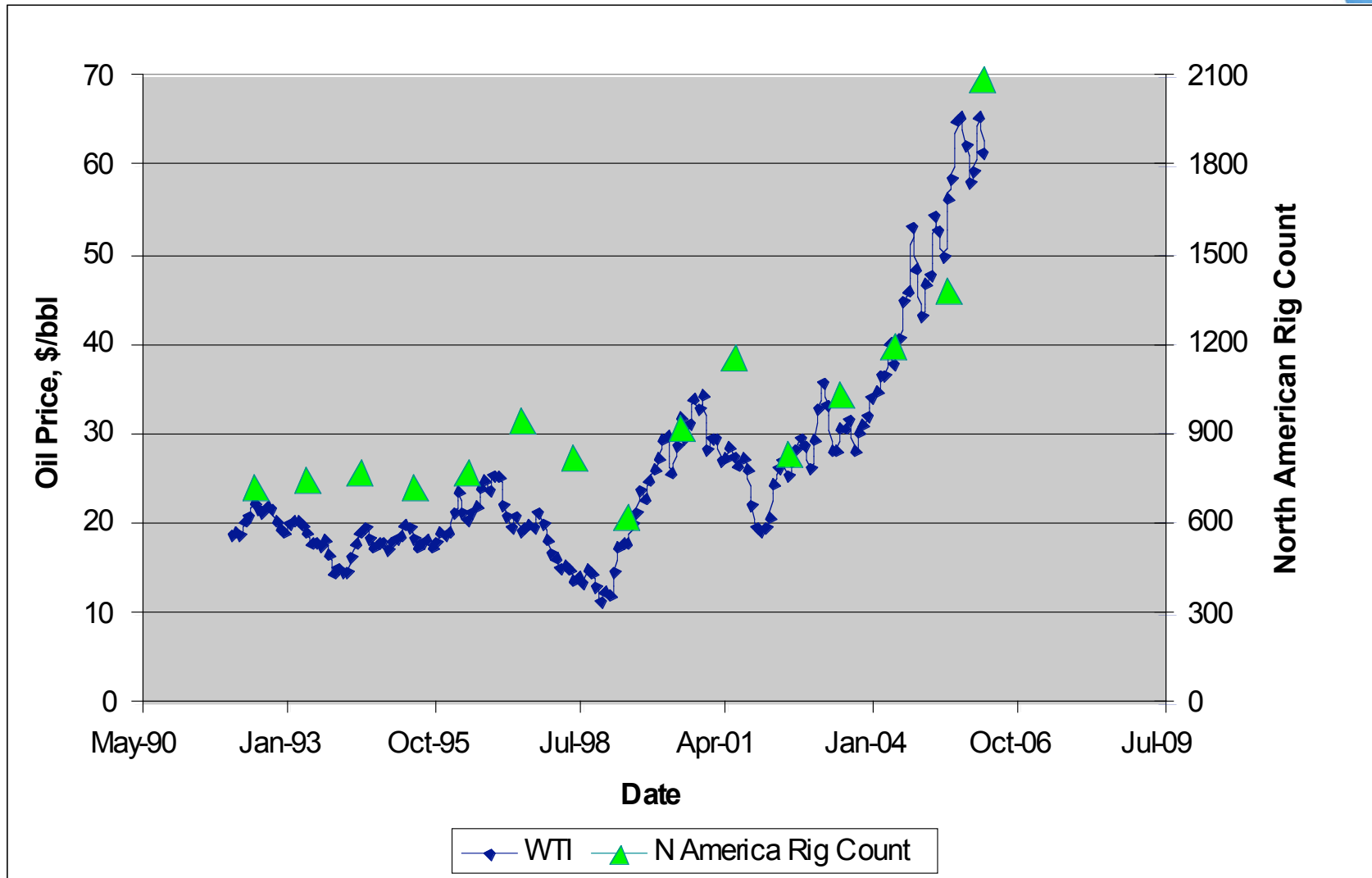
- ◆ Alaska and Cook Inlet Competitive Assessment
- ◆ Potential Impacts of Petroleum Production Tax
- ◆ Marathon Current Activities
- ◆ Cook Inlet Natural Gas: Recipe for Success



How Does the Oil/Gas Market Respond to Increased Prices?



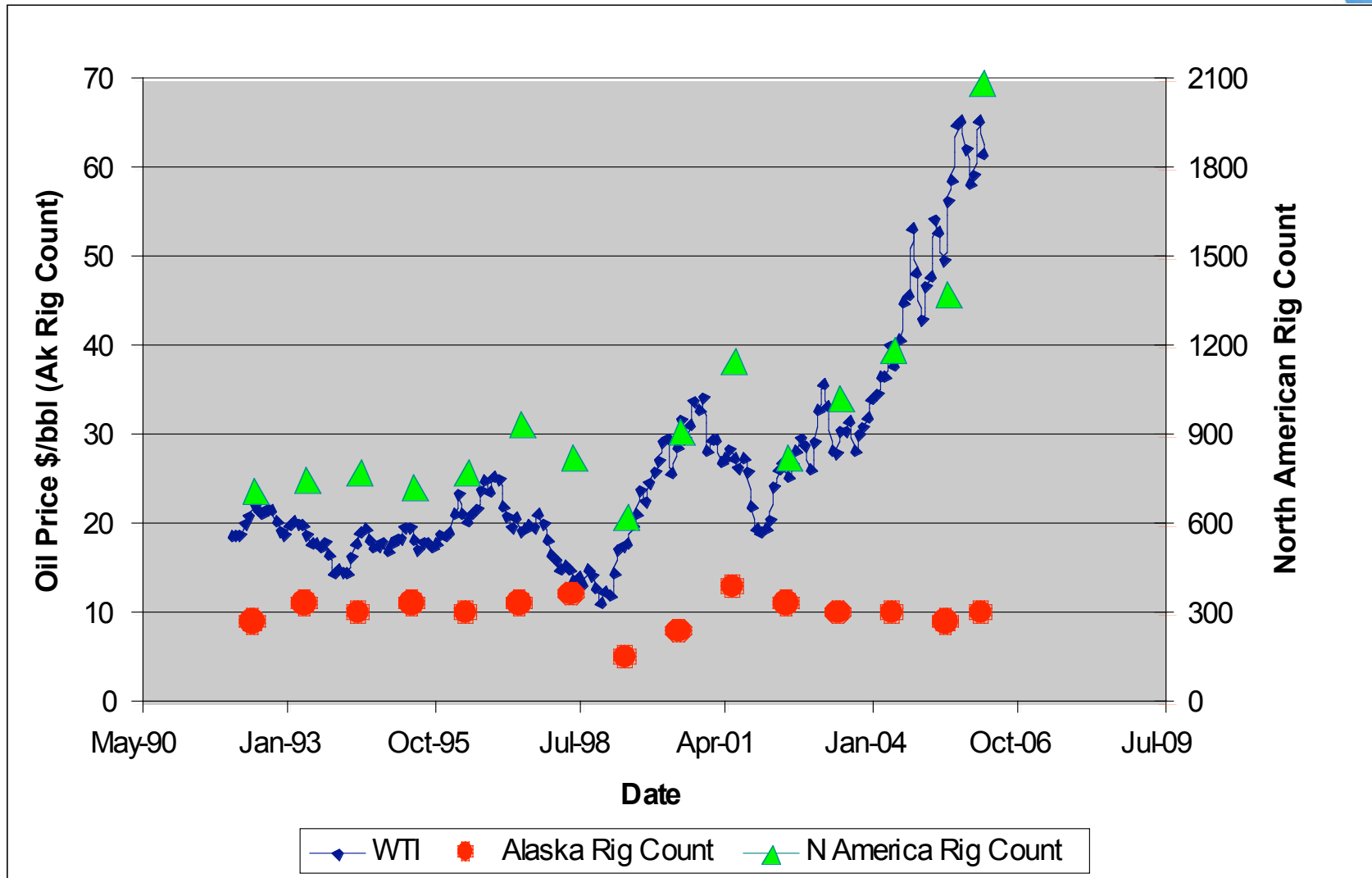
How Does the Oil/Gas Market Respond to Increased Prices?



Date and Tracking Info Here



How Does the Oil/Gas Market Respond to Increased Prices?



PPT – A World Class Tax Structure

- ◆ One “World Class Opportunity in Alaska”
 - North Slope Gas Line tied to PPT
 - Negotiated Settlement with “Producers”
 - Clearly Tied to Overall North Slope Oil and Gas Integrated Development
 - Strong North Slope Industry Benefits State of Alaska as well as Cook Inlet Industry

- ◆ But, the Cook Inlet is not the North Slope...
 - Different issues, players and scale:
 - Last year: Significant discussion on the need to incentivize investments to find and develop more gas to maintain industrial jobs
 - Now: Increased taxes on “windfall profits”



Cook Inlet Natural Gas Summary: Pre-PPT



- ◆ Declining reserves and production rate.
- ◆ Need for additional exploration and development to moderate price increase to consumers and to continue to provide industrial feedstock.
- ◆ Historical price differential to Henry Hub.
 - This continues even with recent Cook Inlet price increases.
- ◆ High operating and capital costs as compared to Lower 48 natural gas provinces.
- ◆ Challenging permitting and regulatory arena.



Cook Inlet Gas Supply and Demand

May 9, 2005

State of Alaska
Department of Natural Resources
Division of Oil and Gas



Alaska Department of
**Natural
Resources**

<http://www.dog.dnr.state.ak.us/oil/products/products.htm>

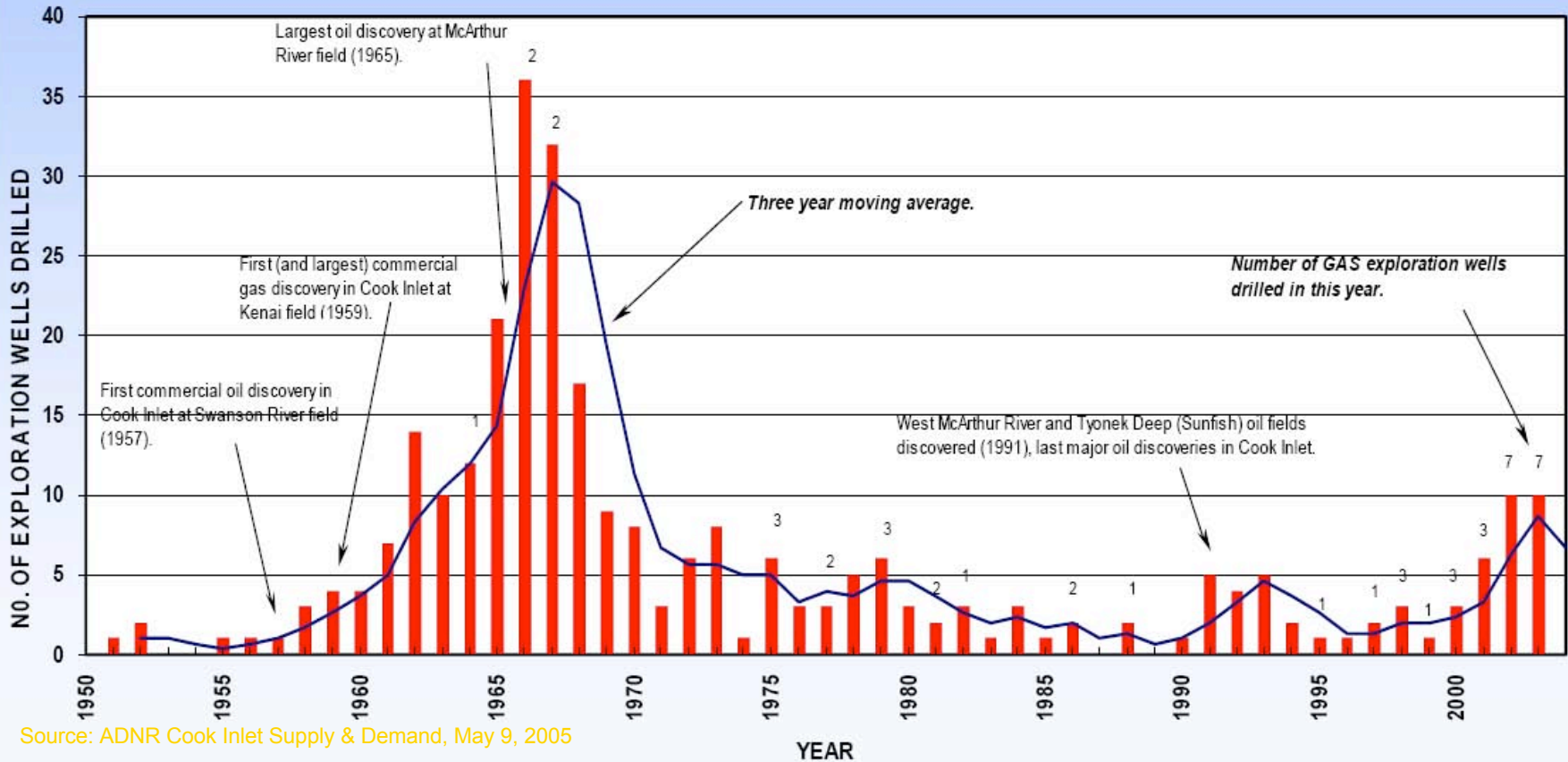
Cook Inlet Areawide Lease Sale Results

	Number Bids Rec'd	Number Tracts Sold	Multiple Bid Tracts	Total Acreage Sold	Total Bonus Rec'd	Avg Winning Bid	Max Bid Rec'd
				<i>Acres</i>	<i>\$</i>	<i>\$/ Acre</i>	<i>\$/ Acre</i>
2000	27	27	0	69,928	\$609,358	\$8.72	\$36.01
2001	31	29	2	102,523	\$928,085	\$9.05	\$22.18
2002	24	21	3	64,923	\$421,840	\$6.50	\$27.03
2003	28	27	1	103,680	\$887,059	\$8.56	\$33.28
2004	77	72	5	363,520	\$2,629,820	\$7.23	\$40.25
TOTAL	187	176		704,574	\$5,476,162		
AVERAGE	37	35	2	140,915	\$1,095,232	\$8.01	\$31.75



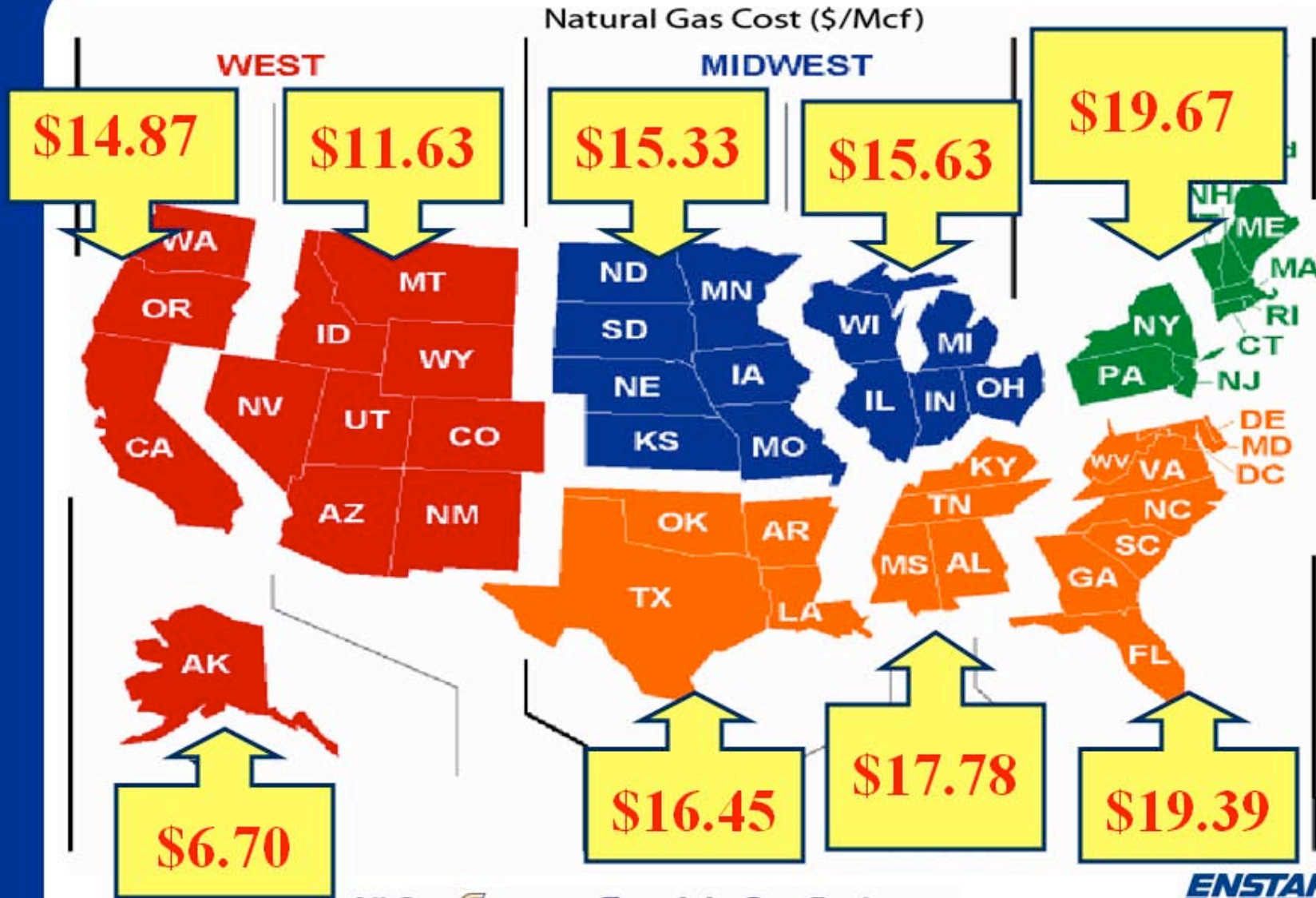
Timeline of Cook Inlet Exploration

COOK INLET EXPLORATION WELL DATA AND IMPORTANT EVENTS



Source: ADNR Cook Inlet Supply & Demand, May 9, 2005

Residential Costs-By Region



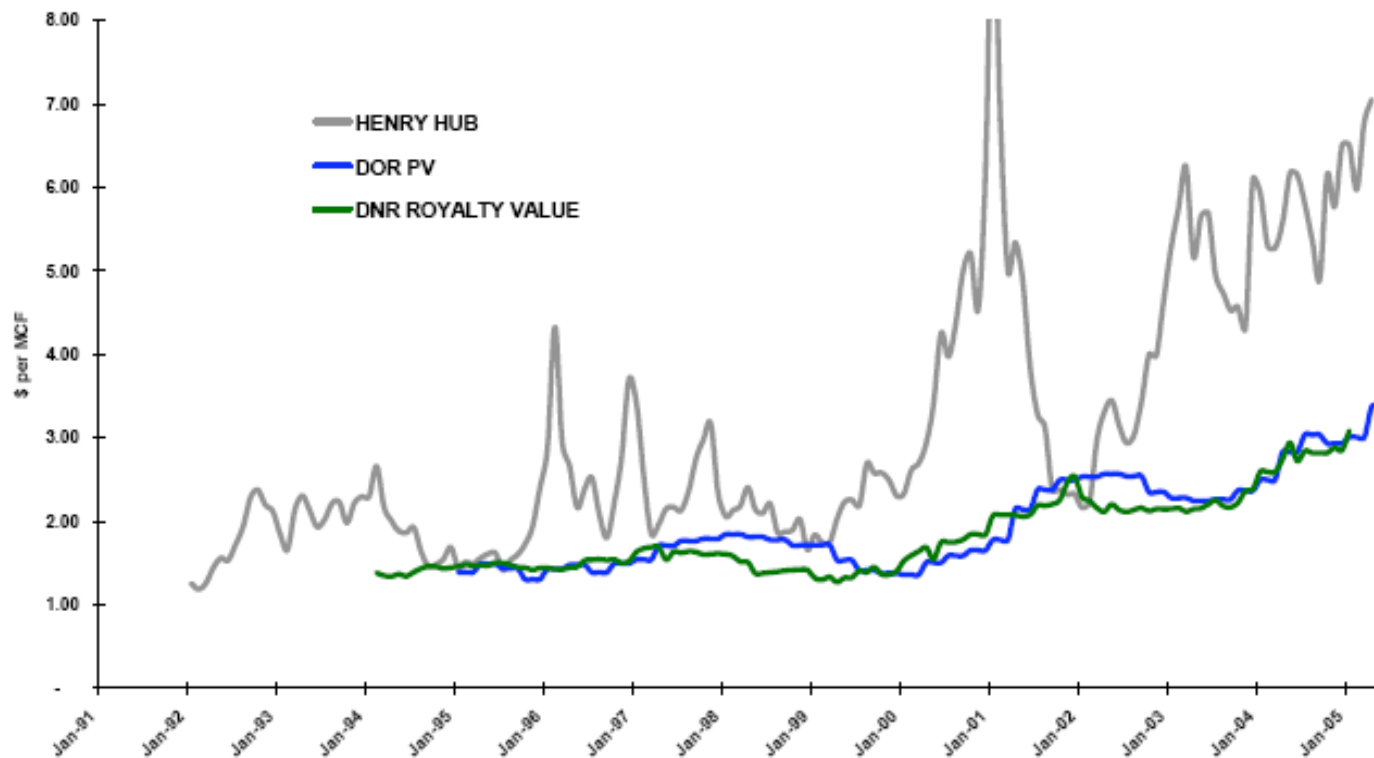
All Our Energy Goes Into Our Customers

Source: Enstar - Energy Supply in South Central Alaska, November 14, 2005

[Date and Tracking Info Here](#)



Historic HH, DOR PV and DNR Royalty Value



Conceptual Competitive Comparison

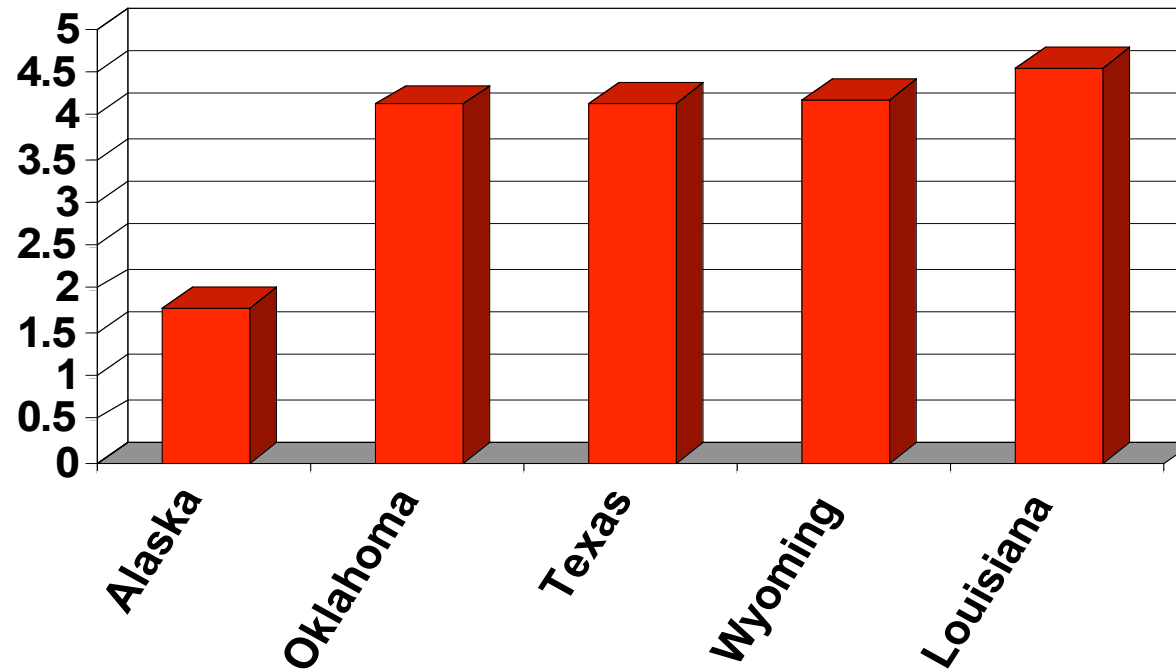
Common Input – Per Well Analysis

Recoverable Reserves	5 BCF
Development Cost (Capital)	\$5 million
Operating Cost	\$0.50/mcf
Sales Price	AK = \$4/mcf L48 = \$7/mcf
Royalty	1/8



Competitiveness Comparison: Cook Inlet Natural Gas Investments Disadvantaged Against Competition

Pre-Tax
Profit to
Investment
Ratio



**Assumes No Alaska Severance Tax due to ELF*



Cook Inlet Competitive Analysis

- ◆ There is a need for gas here (closed market), so how will the market respond?
- ◆ Investors & companies will naturally compare opportunities (i.e., Cook Inlet vs. other N American gas)
 - Reasonable access to lands
 - No world class finds are expected, but smaller fields are likely
 - Disadvantaged by high costs of goods & services
 - Disadvantaged by permitting and regulatory burden
 - Disadvantaged by historically low price
- ◆ Question?:
 - Will fiscal policy incentivize or further disadvantage Cook Inlet in attracting needed investment to meet gas demands?



Potential Impacts of PPT Cook Inlet Gas

- ◆ Existing Fields
 - Nothing wrong with ELF for Cook Inlet natural gas
 - Loss of ELF and higher tax rate in low gas price environment will result in
 - Lower Revenues after tax
 - Earlier abandonment for all, but especially, marginal fields
 - Reserves will be lost
- ◆ New Exploration and Development
 - Higher taxes will result in:
 - Less competitive opportunities compared to N American gas provinces
 - Less Cook Inlet exploration and development activity
 - Cancelled projects
 - **NO NEW RESERVES DEVELOPED**
- ◆ Loss of industrials and jobs
- ◆ **Higher and volatile costs to utility consumers**



Cook Inlet PPT – What is Needed?

- ◆ Must include provision for marginal low rate fields
 - 5/20 Plan for Cook Inlet
- ◆ Gas Progressivity Places volatility and risk on Alaska consumers and industry - undesirable. If progressivity then...
 - Base on net and not gross
 - Base on actual value, not Henry Hub
- ◆ Prioritize efforts to incentivize, not hinder exploration and development
- ◆ Actions by this Legislature will have immediate and measurable impact on Cook Inlet oil and gas industry
 - PLEASE CONTACT YOUR LEGISLATOR AND LET HIM/HER KNOW YOUR VIEWS
 - Thanks to those of you who have already worked to communicate the full picture to our legislators and community.



Current Marathon Cook Inlet Activities

- ◆ Kasilof First Gas (target by year end)
- ◆ Cannery Loop Pad 3 Reactivation (SI for 15 yrs)
- ◆ Gas Storage Project (permitting/lease near final)
- ◆ Continued work in other fields:
 - Kenai (EXCAPE Completion Technology)
 - Ninilchik (5th Production Facility going in this year)
- ◆ Pipeline Update



Cook Inlet Natural Gas: Current Status - Pipelines

- ◆ As of November 2005, 4 major Cook Inlet gas pipelines operated by Marathon are in regulated service
 - Kenai Kachemak Pipeline (KKPL)
 - Very costly and time-consuming RCA approval process
 - 4.2 mile Kasilof Extension in progress
 - Kenai Nikiski Pipeline (KNPL)
 - Final settlement submitted to RCA; approval pending
 - Cook Inlet Gas Gathering System (CIGGS)
 - Settlement negotiations in final stages of RCA approval
 - 4-7 mmcfpd of 3rd party gas moving (40 mmcfpd reserved)
 - Beluga Pipeline (BPL)
 - Petitioned RCA to allow bi-directional service
 - \$0.25/mcf “postage stamp” tariff reduced from \$0.33/mcf



Cook Inlet Natural Gas: Recipe for Success

- ◆ Ingredients on hand:
 - Resource Potential
 - DOE report shows resource potential
 - Available long-term markets
 - Competitive price signals which attract capital
 - Open access pipeline infrastructure
 - Good access to leases
 - State of Alaska incentives



Cook Inlet Natural Gas: Recipe for Success

- ◆ Ingredients missing:
 - Multi-year industrial contracts (LNG, fertilizer, refining, etc.)
 - Acceptance of market price signals
 - Pipeline link to other markets or gas sources
 - Permit and regulatory streamlining
 - Support services and infrastructure spread thin



Take Home Messages

- ◆ Cook Inlet Natural Gas Industry
 - On the verge of something; Boom or bust?
 - Outcome will be determined by how challenges are met
 - By Industry
 - By State of Alaska Administration and Legislature
 - By regulatory and permitting bodies
 - By consumers
 - By outside forces





Thank You!

