

## **Why Oil Severance Taxes Should Change and the ELF should die.**

The Alaska Legislature needs to eliminate the ELF, the Economic Limit Factor, and restore a fair severance tax on our one time oil treasure. The ELF was established in 1989 as an incentive to oil companies to develop marginal fields. Under the ELF, the severance tax rate on oil companies has fallen for over a decade, and will continue to fall if the legislature allows it to remain in effect. That is because under the ELF most new fields are completely or almost completely exempted from Alaska's 15% severance tax. The ELF was not necessary or wise in 1989, and it is absurdly foolish to allow it to continue now. Marginal wells are in production. Alaska shouldn't continue to sell oil at well below the world average rate of taxation. For oil companies, high oil prices mean huge profits. With oil at the fabulous price of \$35 a barrel today, we are giving away much of the value of an irreplaceable resource by not getting a fair severance tax on our oil. Once it is severed from the ground, it is gone forever.

Representative Les Gara (Representative\_Les\_Gara@legis.state.ak.us) has presented an idea for how to remedy this raw deal for Alaskans. It is called the Alaska Fair Share Bill. Under the ELF, the oil severance tax rate on oil companies falls as the fields age. But worse, most new fields, which have come on line since 1989 pay vastly less than the 15% rate of severance tax which state law is supposed to demand. So at \$30 per barrel, oil companies receive \$1.2 billion more in profits than the state receives in total oil revenues. Is this a fair return for our oil?

Representative Gara suggests a minimum severance tax of 5%, and an increasing, graduated severance tax on all oil, based on the world price. His proposal would generate:

- an additional \$110 million at a \$22 per barrel price
- an additional \$400 million at a \$30 per barrel price
- an additional \$500 million at a \$32 per barrel price

If we do not change the ELF now, our effective severance tax rate will continue to fall from a present average of 7.5% (2003), to 6.0% in 2009, and to 4.05% in 2013. The corresponding revenues drop from \$599 million in 2003 to \$180 million by 2013. (Source: Alaska Department of Revenue).

Representative Gara's proposal ties the severance tax to the price of oil, raising it with higher world prices and lowering it when the price is low. The formula is uncomplicated and very clear. It drops the severance tax entirely when the price goes below \$10 a barrel, and caps it at a maximum of 25%.

Oil taxation plans with similar merit have also been presented by Ray Metcalfe for changing the lease bid process, along with other good oil tax policies; oil industry analyst Richard Feinberg has advocated a Windfall Equal Sharing Tax. Progressively taxing high oil prices for the future, however, is a sound means for receiving a fair take for our oil. We must achieve fair economic value for our vanishing oil treasure now. Every day that we don't recover full value for Alaska's oil, means badly needed revenue and Permanent Fund

deposits are lost forever. Continuance of the ELF as it is now, is a clear violation of the State Constitutional mandate to receive maximum benefit to all Alaskans from the states natural resources (Article VIII. Section 2, Alaska State Constitution). More than that, it is a crime against the future. This oil revenue will not come again.

All reasonable Alaskans should ask why these very sensible and fair taxation proposals to fill the fiscal gap aren't dominating the front page of every newspaper in the state. Tapping the Permanent Fund earnings may not be necessary yet, if we just get what every other oil producing government averages for its black gold, and are willing to pay our own way to even out the world oil price fluctuations. The halls of the legislature should be resounding with your loud calls for action on these crucial changes in taxation.

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