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CSSB 138 (FIN) am: Commercial Production of North Slope Gas
SECTIONAL ANALYSIS: 28-GS2806\I.A

House Resources Committee – March 19, 2014

Bill sections related to the Alaska Gasline Development Corporation (AS 31.25)

Section 1 amends AS 31.25.005, related to the purpose of the Alaska Gasline Development Corporation (AGDC), to add new subsections (1) - (2) to direct the AGDC to develop and have primary responsibility for developing natural gas pipelines, an Alaska liquefied natural gas project (AK LNG), and other transportation mechanisms to deliver gas in-state for the maximum benefit of the people of the state, and to provide economic benefits and revenue to the state.

New subsection (3) expands the AGDC's purpose to include assisting the commissioners of natural resources and revenue to maximize the value of natural gas royalty and tax values.

New subsection (5) expands the AGDC's purpose to include advancement of an AK LNG project, including infrastructure related to liquefaction and commercial support; fees for services for commercial support provided to the state may not be greater than the cost of the service to the AGDC.

Section 2 conforms AS 31.25.010, the structure of the AGDC related to dissolution, to include reference to the purpose section, AS 31.25.005 (amended in section 1).

Section 3 amends AS 31.25.040 to add a new subsection to direct the AGDC board, to the maximum extent practicable, to maximize efficient use of state resources, and establish separation with respect to the missions and information for the in-state natural gas pipeline and the AK LNG project. The AGDC board shall appoint a program director for the AK LNG project.

Section 4 amends AS 31.25.080(a), the powers and duties of the AGDC, to add references to the AK LNG project where needed.

New paragraph (23) adds, for the AK LNG project only, authority to acquire an ownership interest in the AK LNG project components (pipeline facilities, treatment and liquefaction) or in an entity or joint venture with an ownership or other interest in an AK LNG project. This power is limited to the entity of the AGDC pursuing the AK LNG project.

New paragraph (24) allows the AGDC, after consultation with the commissioners of revenue and natural resources, to enter contracts for services related to an AK LNG project.

Section 5 is a conforming amendment to AS 31.25.080(e) to explicitly reference the in-state natural gas pipeline open season currently in the AGDC statutes.

Section 6 adds a new subsection to AS 31.25.080 to direct that an entity or subsidiary of the corporation pursuing the in-state natural gas pipeline may not pursue an AK LNG project (AS 31.25.080(23)).

Section 7 amends AS 31.25.090, regarding confidential information held by the AGDC, to expressly direct that the commissioners of revenue and natural resources shall have access to contract information related to the AK LNG project.

Section 8 amends AS 31.25.100 to direct that money appropriated to the in-state natural gas pipeline fund may be used for the in-state natural gas pipeline and for purposes related to transportation mechanisms in the state, including delivery of propane.

Section 9 establishes AS 31.25.110, the Alaska liquefied natural gas project fund in the AGDC. If money is appropriated to advance an AK LNG project, the corporation shall create an account in the fund for that purpose. The money may be used without further appropriation for purposes related to an AK LNG project and for the purpose of transferring revenues related to equity interests, contracts and other activities to the appropriate fund as determined by the commissioner of revenue.

Section 10 related to subsidiaries created under AS 31.25.120, removes a reference to acquiring the state's royalty share of natural gas yet leaves the broad authority to acquire gas from the North Slope. The AGDC may transfer assets between any subsidiaries it creates under this subsection, except that money for the in-state natural gas pipeline and the AK LNG project may not be transferred. A reference which may have been read to limit subsidiary formation to not for profit subsidiaries is removed.

Section 11 makes a conforming amendment in AS 31.25.140(c) on budgetary reporting to the legislature to reference the AK LNG project fund, AS 31.25.110.

Section 12 amends AS 31.25.390 to add a definition of the Alaska liquefied natural gas project and includes an explanation of gas pipeline, gas treatment plant, liquefied natural gas plant, marine terminal, Point Thomson and Prudhoe Bay unit gas transmission lines.

Bill sections related to an Alaska affordable energy fund (AS 37.05)

Section 13 adds AS 37.05.610, an Alaska affordable energy fund as a special non-dedicated account in the general fund to develop infrastructure to deliver energy to areas in the state not expected to have direct access to a North Slope natural gas pipeline. The fund will receive 10 percent of the money received from the state's royalty gas transported in an AK LNG project (net of royalty payments to the Alaska permanent fund).

<u>Bill sections related to the Alaska Land Act (AS 38.05)</u>

Section 14 amends the authority of the commissioner of the Department of Natural Resources (DNR) by adding new paragraphs (10) – (12) to AS 38.05.020(b). Effective upon passage of the bill, the DNR commissioner may enter into commercial agreements of not more than two years duration for project services related to the North Slope natural gas project. In addition, in consultation with the commissioner of revenue, the DNR commissioner may participate in negotiations associated with a North Slope natural gas project, including agreements that include balancing, marketing, disposition of natural gas, and offtake contracts associated with a North Slope natural gas project.

A contract or agreement negotiated in which the state is a party would not be effective against the state without legislative authorization for the governor to execute the contract. Paragraph (12) permits the DNR commissioner to enter into confidentiality agreements related to contract negotiations and implementation. Confidential information obtained under paragraph (12) may be shared with the legislature only in committees held in executive session or under confidentiality agreements. Final contracts subject to approval by the legislature would not be confidential.

Section 15 adds new paragraph (13) to allow the DNR commissioner, in consultation with the commissioner of revenue, to take custody of gas delivered to the state, to manage project services and the disposition of gas delivered to the state under AS 43.55.014(b)(tax as gas).

Section 16 clarifies AS 38.05.180(i) with a conforming amendment that the exploration incentive credit may be applied against the oil and gas production tax levied under AS 43.55.011.

Sections 17 and 18 add new subsections (hh) and (ii) to the Alaska Land Act, AS 38.05.180, which deals with oil and gas leasing, to permit the DNR commissioner to propose modifications to existing leases that: (1) relate to switching between taking royalty gas in kind or in value to ensure that the lessee, state or other person bear proportionate costs for transportation, and to assure the state's actions do not unreasonably interfere with the long-term marketing; (2) provide a method to establish a fair market value for each component of the state's royalty gas; and (3) modify royalty provisions, including net profit provisions, modifications may not result in less than the value the state would have received before a modification.

The DNR commissioner must make written determinations relating to the best interests of the state, including whether the modifications will improve the likelihood of a successful North Slope natural gas project for which sufficient commitment has been shown. Section 18 adds an explicit reference to gas delivered to the state as payment for production tax.

Sections 19 through 22 amend AS 38.05.183, related to sales of royalty oil or gas, by adding references to gas delivered to the state under AS 43.55.014(b), the levy of production tax on gas to be paid in gas for certain North Slope leases.

Section 23 adds definitions to AS 38.05.965 for "initial project term," "North Slope natural gas project;" and "project services."

Bill sections relating to the in-state gasline project coordinator (AS 38.34)

Sections 24 through 26 amend AS 38.34 related to review by state agencies or entities to expedite review or action of a project under AS 31.25 (AGDC) and to direct that state agencies may not include project provisions that the in-state gasline project coordinator determines would prevent or significantly impair a project under AS 31.25 (AGDC).

Bill sections relating to tax records and general revenue administration (AS 40.25 and 43.05)

Sections 27 and 28 amend AS 40.25.100 related to the confidentiality of tax information to clearly establish as confidential information related to contract negotiations for a North Slope natural gas project. Section 28 references new subsection (k) in AS 43.05.230 to except from taxpayer confidentiality provisions the name of each person that makes an election to pay the gas production tax from modified North Slope leases in gas and the amount of gas subject to that election.

Section 29 amends AS 40.25.120(a) to establish an exception in public records for information confidential under the new provisions of AS 38.05.020(b) (related to contract negotiations for a North Slope natural gas project).

Sections 30 and 31 expand the authority of the commissioner of the Department of Revenue (DOR) by adding new paragraphs (16) and (17) in AS 43.05.010. Effective immediately, paragraph (16) provides that the DOR commissioner may consult with the DNR commissioner on negotiations associated with a North Slope natural gas project. Section 31 amends AS 43.05.010 by adding paragraph (17) to provide that the DOR commissioner direct the disposition of revenues received from gas delivered to the state under AS 43.55.014(b) by entering into agreements with the DNR commissioner.

Section 32 adds new subsection (k) to AS 43.05.230 to except from taxpayer confidentiality provisions the name of each person that makes an election to pay the gas production tax in gas and the amount of gas subject to that election.

Section 33 amends AS 43.20.144(f) to clarify that gas subject to an election to pay the oil and gas production tax on gas as gas under AS 43.55.014 is included the extraction factor of a taxpayer subject to AS 43.20.144(f) in the Alaska Net Income Tax Act.

Bill sections relating to the oil and gas production tax (AS 43.55)

Section 34 amends AS 43.55.011(e), the levy of the oil and gas production tax, to add reference to the separate levy under AS 43.55.014 for certain North Slope gas. *For oil and gas produced after January 1, 2014 and before January 1, 2022,* AS 43.55.011(e)(2) would levy on producers of oil and gas produced each calendar year a flat rate tax of 35 percent of the production tax value of taxable oil and gas produced from each lease or property in the state. No change is made to current tax ceilings that apply to Cook Inlet oil and gas, gas produced outside the Cook Inlet basin and used in the state, and oil and gas produced from new fields outside the Cook Inlet basin and south of the North Slope.

For oil and gas produced on or after January 1, 2022, AS 43.55.011(e)(3) would levy on producers of oil produced each calendar year a flat tax rate of 35 percent of the production tax value of taxable oil produced from each lease or property in the state and on producers of gas, and a flat tax rate of 13 percent of the gross value at the point of production of gas produced from each lease or property in the state. The tax on gas for which the DOR commissioner has approved an election to pay in gas would be levied under AS 43.55.014.

Section 35 amends AS 43.55.011(f), the alternate minimum tax on North Slope oil and gas, to retain the current minimum tax until January 1, 2022. After that date, the minimum tax would apply to oil produced on the North Slope. A minor amendment adds the reference to the tax applying to leases or properties "that include land" to ensure that property that straddles 68 degrees North latitude will be considered north of 68 degrees North latitude for purpose of the alternate minimum tax.

Section 36 adds AS 43.55.014 which allows producers to make an election, under regulations adopted by the DOR, to pay the oil and gas production tax on gas in gas for gas produced from oil and gas leases whose terms have been modified under proposed AS 38.05.180(hh) from which the DNR commissioner has determined to take royalty gas in kind. The levy would be 13 percent of the taxable gas when and as the gas is produced. The producer would pay the tax by delivering the gas to the state at the point of production. The DNR would manage the custody and disposition of gas delivered to the state. Gas subject to this provision would not include gas flared, released, or allowed to escape upstream of the point of production, or to gas used in lease operations or for repressuring. Tax deficiencies and interest and penalties on any tax deficiency would be accounted for as if the tax was levied for money under AS 43.55.011(e). This section would take effect on January 1, 2015 to be applied to gas produced from certain North Slope leases on and after January 1, 2022.

Sections 37 through 39 include conforming amendments to the oil and gas producer education credit, AS 43.55.019, to clarify that the credit can be applied to tax liability under AS 43.55.011(e) only. The credit is expanded to include expenditures related to nonprofit regional training centers and apprenticeship programs.

Section 40 amends AS 43.55.020(a), monthly installment payments of estimated tax, to add provisions for payment of tax after January 1, 2022 and to clarify the tax rates that apply to oil and gas produced after a certain date. Monthly installment payments for oil and gas produced on and after January 1, 2022 are in new subsection (a)(7).

Sections 41 and 42 are conforming changes to AS 43.55.020, monthly installment payments. Subsection (g) is amended to account for new tax provisions for oil and gas produced on and after January 1, 2022. A similar conforming change is made in AS 43.55.020(h) to account for interest on overpayments of installment payments.

Sections 43 and 44 amend AS 43.55.020(*l*) and add subsection (m), related to making settlements by a producer with private landowner royalty owner, to account for making a settlement with the royalty owner for gas taxable before January 1, 2022 and under new AS 43.55.014.

Section 45 amends AS 43.55.030(a), annual statements by producers and explorers, to require reporting of the amount of gas produced from a lease or property for which tax is levied under AS 43.55.014 and the amount of gas delivered to the state under AS 43.55.014.

Section 46 amends AS 43.55.160(a), calculation of annual production tax values, to clarify and conform to the levy of tax under AS 43.55.011(e)(2) for oil and gas produced before January 1, 2022.

Section 47 amends AS 43.55.160(e), related to determination of excess lease expenditures for the purpose of calculating a carried-forward loss credit, to account for annual production tax values for oil produced on and after January 1, 2022.

Section 48 amends AS 43.55.160(f), a 20 percent gross value reduction for certain oil and gas produced north of 68 degrees North latitude, so that gas produced on and after January 1, 2022 would not qualify for the gross value reduction in this section.

Section 49 amends AS 43.55.160(g), a 10 percent gross value reduction for certain oil and gas produced from a unit north of 68 degrees North latitude made up solely of leases that have a royalty share of more than 12.5 percent in amount or value of the production removed or sold from the lease so that gas produced on and after January 1, 2022 would not qualify for the gross value reduction in this section.

Section 50 amends AS 43.55.160, calculation of annual production tax values, to add a new subsection (h) for calculation of annual production tax values for oil produced on and after January 1, 2022. On and after January 1, 2022, gas would be taxed at a percentage of gross value. Accordingly, there would be no need to calculate a production tax value (gross value at point of production less lease expenditures) for gas. Producers would still calculate a production tax value of oil taxable under AS 43.55.011(e) for the segments set out in AS 43.55.160(h).

Section 51 makes a conforming amendment to AS 43.55.165, lease expenditures, to exclude as a deduction from lease expenditures the tax levied under AS 43.55.014 (tax paid as gas).

Sections 52 through 55 amend, for purposes of the oil and gas production tax, the definitions of "gas processing plants" and "point of production" for gas to be upstream of either the first point where it is accurately measured, the inlet of a pipeline transporting the gas to a gas treatment plant, or the inlet of any gas pipeline system transporting gas to market. Section 54 adds a definition of "gas treatment plant". A conforming amendment is made to AS 43.90.900(18), the definition of the "point of production" for purposes of the Alaska Gasline Inducement Act.

Conforming amendments and uncodified law

Section 56 makes conforming amendments to AS 43.98.030, the film production tax credit, to limit the applicability of the credit to the tax levied by AS 43.55.011.

Section 57 repeals AS 31.25.080(f) as unnecessary due to new provisions in the AS 31.25. Subsection (f) related to the ability of the AGDC to, without delaying progress on an in-state natural gas pipeline, coordinate with developers of a large-diameter natural gas pipeline related to a certain geographic area.

Section 58 adds to uncodified law a legislative request that the governor establish an interim advisory board to advise the governor on municipal involvement in a North Slope natural gas project.

Section 59 adds to uncodified law a direction to the Alaska Energy Authority (AEA), in consultation with the AGDC, the Alaska Industrial Development and Export Authority, and the DOR, to develop plans relating to the delivery of energy - whether fossil fuel, hydro, tidal or other - to areas of the state not expected to have direct access to commercialization of North Slope gas through a North Slope natural gas pipeline. The AEA will also consider storage options, and recommendations related to means to make energy more affordable. The AEA and the DOR will consider and recommend funding possibilities. The AEA shall provide the plan and suggested legislation by January 1, 2017.

Section 60 adds to uncodified law a direction that the DOR commissioner consider and report, including submission of proposed legislation, to the legislature on options to allow municipalities, residents, or regional corporations to invest in a North Slope natural gas pipeline. The DOR commissioner is directed to consider relevant factors in preparing the plan and report, which is to be presented to the legislature when the DNR commissioner submits contracts to the legislature.

Section 61 allows the DNR and the DOR to adopt regulations to implement this Act.

Sections 62 through 64 set effective dates for different sections of the bill. Sections 1 - 14, 16, 17, 23 - 27, 29, 30, 37, 39, and 55 - 61 would be effective immediately. The other sections would be effective January 1, 2015 except for section 38 (amending as 43.55.019(a)), which takes effect January 1, 2021.