THE STATE of ALASKA
GOVERNOR SEAN PARNELL

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HCS CSSB 138 (RES): Commercial Production of North Slope Gas
SECTIONAL ANALYSIS: 28-GS2806\H

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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 31.25.020(a), the composition of the AGDC board of directors, to remove a provision which would have allowed the governor to appoint the commissioner of natural resources and the commissioner of revenue to the AGDC board after a project under AS 43.90 (the Alaska Gasline Inducement Act) has been abandoned or the commissioners are no longer signatories on a valid contract under AS 43.90. With this amendment, the commissioner of natural resources and the commissioner of revenue may not be appointed to the AGDC board.

Section 4 amends AS 31.25.020 to add a new section related to appointment of the AGDC board members. A person appointed must be a citizen of the United States, but notwithstanding AS 39.05.100, are not required to be or have been a registered voter, and is not required to reside in the state.

Section 5 amends AS 31.25.040 to add new subsections 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 may appoint separate program directors for the AK LNG project and the in-state natural gas pipeline. A program director reports to the executive director of the corporation.

Sections 6 and 7 amend AS 31.25.050 to adds conforming language and a new subsection that requires the attorney general to be legal counsel for the AGDC for legal services related to development of contracts and agreements by the AGDC that relate to an AK LNG project. The attorney general is to consult with the AGDC when procuring outside counsel for legal services for the AGDC related to an AK LNG project. The AGDC retains the authority to obtain legal counsel to advise the corporation in legal matters and represent it in litigation.

Section 8 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 9 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 10 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 11 amends AS 31.25.090 by adding a new subsection, 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 12 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 13 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 of the state as determined by the commissioner of revenue.

Section 14 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 15 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 16 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 the Alaska Procurement Code (AS 36.30)

Section 17 adds two new paragraphs (47) and (48) to AS 36.30.850(b), related to exceptions to the application of the state procurement code. Paragraph (47) exempts contracts for professional and technical services by the Department of Natural Resources (DNR) to support the development of agreements and contracts under AS 38.05.020(b)(10) and (11). Paragraph (48) exempts contracts of the Department of Law (LAW), with client participation, for legal services related to an AK LNG project, except that to the extent practicable the LAW shall use the procurement process for small procurements (AS 36.30.320) with participation of the client.

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

Section 18 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 20 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).

Bill sections related to the Alaska Land Act (AS 38.05)

Section 19 amends the authority of the DNR commissioner by adding new paragraphs (10) – (12) to AS 38.05.020(b). 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 members of the legislature, including their respective agents and contractors on request, under confidentiality agreements either in committees held in executive session or with any member of the legislature individually. The terms of a proposed final contract, subject to approval by the legislature, would not be confidential and must be made available to the public at least 90 days before the proposed effective date for the terms.

Paragraph (13) directs that the DNR commissioner consult with the AGDC in the development of agreements or contracts for project services related to a gas treatment plant, pipeline, liquefaction facility, marine terminal or transportation services.

Section 20 adds new paragraph (14) to AS 38.05.020(b) 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 21 adds AS 38.05.023, related to terms in an agreement or contract related to a North Slope natural gas project. Subsection (a) details a requirement, to be included in a contract under

AS 38.05.020(b)(11) in which the state is a party, regarding the conditions for state access to data in the event that the commissioner of natural resources determines that a North Slope natural gas project is not making adequate progress towards a final investment decision. Subsection (b) provides that a proposed agreement or contract associated with a North Slope natural gas project may not include a provision that changes a payment in lieu of property tax on property that was previously taxable under AS 43.56.

Section 22 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 23 and 24 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 24 adds an explicit reference to gas delivered to the state as payment for production tax.

Section 25 amends AS 38.05.182(a), related to royalties on natural resources, to state that it is not in the best interest of the state to take royalty in value from a lessee transporting gas in a North Slope natural gas project if the lessee has committed to dispose of or market the state's royalty gas taken in kind on the same terms and conditions as the lessee disposes of or markets the lessee's gas.

Sections 26 through 29 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 30 adds definitions to AS 38.05.965 for "initial project term," "North Slope natural gas project;" and "project services."

<u>Bill sections relating to the in-state gasline project coordinator (AS 38.34)</u>

Sections 31 through 33 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).

<u>Bill sections relating to tax records and general revenue administration (AS 40.25 and 43.05)</u>

Sections 34 and 35 amend AS 40.25.100(a) 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 35 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 36 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 37 and 38 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 38 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 39 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 40 amends AS 43.20.144(d) to clarify that gas delivered to the state as payment of tax under an election made by AS 43.55.014 (or similar provision of other taxing jurisdiction) is excluded from the sales factor of a taxpayer subject to the Alaska Net Income Tax Act. Also, fees paid between entities within the taxpayer's consolidated business for transporting the taxpayer's gas are excluded from the sales factor.

Section 41 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.

<u>Bill sections relating to the oil and gas production tax (AS 43.55)</u>

Section 42 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 43 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. On and after January 1, 2022, 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 44 adds AS 43.55.014, related to payment in gas of tax for gas. Subsection (a) 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 AS 38.05.180(hh) from which the DNR commissioner has determined to take royalty gas in kind. Under subsection (b), 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. Under subsection (c), the DNR would manage the custody and disposition of gas delivered to the state. Under subsection (d), tax deficiencies and interest and penalties on any tax deficiency would be accounted for in an amount of gas or an amount of money. If in money, the assessment is the product of the number of units by which the producer's delivery of gas to the state was deficient, multiplied by the gross value at the point of production for each unit of the producer's gas, other than gas not subject to tax, or delivered to the state under this section. Also, this subsection accounts for an overpayment of gas under AS 43.55.014. Subsection (e) clarifies that gas subject to this provision would not include gas flared, released, or allowed to escape and, under AS 43.55.020(e), considered as gas produced from a lease or property for the purpose of AS 43.55.011 - 180. 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 45 through 47 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 48 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 49 and 50 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 51 and 52 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 53 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 54 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 55 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 56 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 57 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 58 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 59 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 60 through 62 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. The gas point of production is after mechanical separation. Section 62 adds a definition of "gas treatment plant".

Section 63 makes a conforming amendment to AS 43.90.900(18), the definition of the "point of production" for purposes of the Alaska Gasline Inducement Act.

Section 64 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 65 amends AS 43.98.050, related to the duties of the Alaska Competitiveness Review Board, to include written findings and recommendations to the legislature before January 15, 2017 regarding the state's tax structure, rates, and incentives for oil and gas production south of 68 degrees North latitude.

Section 66 repeals AS 31.25.080(f) as unnecessary due to new provisions in 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 67 adds to uncodified law direction for the DNR commissioner to make a report, with recommendations, to the legislature on a plan and alternatives to make North Slope gas available for delivery and use in the state. Also, the DNR commissioner shall recommend means of addressing risks identified in the report. The report and recommendations are required to be available to the legislature on or before the date that a firm transportation services agreement in a North Slope natural gas project to which the state is a party is submitted to the legislature for approval.

Section 68 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. The requested board is to provide reports, including recommendations, to the governor.

Section 69 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 70 adds to uncodified law a direction that the DOR commissioner identify and report to the legislature regarding financing options for state ownership and participation in a North Slope natural gas project. An interim draft report is to be available to the legislature on the first day of the first regular legislative session of the 29th Legislature. Also, the DOR commissioner is to 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 for approval under AS 38.05.020(b)(11).

Section 71 adds to uncodified law a requirement that the parties to a North Slope natural gas project provide briefings to interested legislators, their staff, and consultants on the progress of the project at least once every four months before the first flow of gas. A briefing must include a written report of the amount of money the state may be liable to pay for a North Slope natural gas project if the project is terminated before the first flow of gas.

Section 72 allows the DNR and the DOR to adopt regulations to implement this Act.

Sections 73 through 75 set effective dates for different sections of the bill. Sections 1-19, 22, 23, 30-34, 36, 37, 45, 47, and 63-72 would be effective immediately. The other sections would be effective January 1, 2015 except for section 46 (amending as 43.55.019(a)), which takes effect January 1, 2021.