



THE STATE
of ALASKA
GOVERNOR MIKE DUNLEAVY

Department of Natural Resources

DIVISION OF OIL & GAS

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The Honorable Josh Revak, Chair
The Honorable Peter Micciche, Co-Chair
Senate Resources Committee
Alaska State Capitol
Juneau, Alaska 99801

February 17, 2021

Re: Senate Bill 61 Oil/Gas Lease: DNR Modify Net Profit Share, Response to and information on follow-up questions from Senate Resources Committee

Dear members of the Senate Resources Committee:

My colleagues at the Commercial section of the Division of Oil and Gas appreciate the opportunity to have provided testimony and information on Senate Bill 61 last Wednesday, February 10, 2021. Below, you will find information addressing the questions you have asked during that presentation.

1. *Provide information on the royalty modifications that were granted by DNR including information on the performance of the projects under consideration of the modification.*

Below is a table summarizing key information on the three applications for royalty modification which were granted by Department of Natural Resources (DNR). For each case, DNR publishes a Preliminary Best Interest Finding, which is subject to a public comment period, offers the opportunity to present these findings to the Legislative Budget & Audit Committee, and then publishes a Final Best Interest Finding on its decision while addressing the comments from the public.

Table 1
Information on the Requests for Royalty Modification that DNR has granted

Year of application	Applicant or lessee	Field or Pool subject to the royalty modification request	Scenario for eligibility under AS 38.05.180(j)(1)	Outcome after modification decision
2005	Pioneer Natural Resources Alaska and Eni Petroleum Exploration	Kuparuk and Nuiqsut pools in the Oooguruk unit	Scenario A: the pool has not previously produced	Projects sanctioned. Production realized.

2008	Eni US Operating Co. Inc.	Schrader Bluff pool in the Nikaitchuq unit	Scenario A: the pool has not previously produced	Project sanctioned. Production realized.
2014	Caelus Natural Resources Alaska	Nuna Torok pool in the Oooguruk unit	Scenario B: to prolong the life of a field or pool as per barrel costs increase to make future production uneconomic	Project not sanctioned. Production not realized. Modification decision automatically rescinded.

- The cumulative production from the Kuparuk and Nuiqsut pools as of December 2020 is 9.4 and 30.3 million barrels of oil, respectively.
- The cumulative production from the Schrader Bluff pool as of December 2020 is 62.6 million barrels of oil.
- For the Nuna Torok case, the project was not sanctioned by the time established in the Best Interest Finding as one condition for the granting of royalty modification. The applicant requested an extension of such agreed-upon investment sanction date, and DNR denied the request for such extension. As a result, the 2014 decision to grant modification was automatically rescinded. In June 2019, the leases represented by this project were assigned by Caelus Natural Resources Alaska to ConocoPhillips Alaska, Inc. Also, in June 2019, these leases were contracted out of the Oooguruk unit to become part of the Kuparuk River unit.
- The Division maintains in its website copies of the Best Interest Findings for some of the prior royalty modification decisions.

Oooguruk (Approved):

https://dog.dnr.alaska.gov/Document/88E628FF86AA4B9BB7A3947ED62C08F0/2-3-2006_Royalty_Modification_-_Final_Findings_-_Approved

Nikaitchuq (Denied):

https://dog.dnr.alaska.gov/Document/E7B3D847BFD44A2DB591B0028F64B87/8-29-2006_Royalty_Modification_-_Preliminary_Decision_-_Denied

Nikaitchuq (Approved):

https://dog.dnr.alaska.gov/Document/EBCF16B57AD94AA0A9EF372D86F0D673/1-11-2008_Royalty_Modification_-_Final_Findings_-_Approved

Nuna-Torok (Approved):

https://dog.dnr.alaska.gov/Document/8924C66C16704ED9A395EF29B413EF13/1-20-2015_Nuna_Royalty_Modification_-_Final_Findings

2. *Of the three cases where DNR granted royalty modification, would any of them have continued without the royalty modification? How much revenue the State received since the modification which would otherwise not have occurred in the absence of the modification?*

Based on the technical and commercial information then available to the applicants and DNR, for each of the requests for royalty modification, the lessees claimed that the future production under consideration would not be realized but for the modification in royalty.

As indicated in the answer to the previous question, for two of the three decisions granting royalty modification, the proposed projects were sanctioned, and production was realized. As a direct result from such production, the State, in its role as lessor, received revenues from royalty and net profit sharing from the net profit leases (NPSLs) associated with some of these projects.

In addition to royalty, it is possible that the State realized revenues from oil and gas property tax, oil and gas production tax, and state corporate income tax for the lessees which are C corporations. However, such confidential tax-payer information is not readily accessible to DNR as it is under the purview of the Department of Revenue. Moreover, as oil and gas production tax and state corporate income tax are assessed at the company level, it could be difficult to provide a reliable measure of the contribution of these pools subject to the royalty modification to these tax revenues. Below is a table with information on the revenues from royalty and net profit sharing, where applicable, from the projects associated with the royalty modifications which were granted.

Table 2
Revenues to the State from royalty and net profit sharing

Year of application	Applicant or lessee	Field or Pool subject to the royalty modification request	Royalty revenue	Net-profit-sharing revenue
2005	Pioneer Natural Resources Alaska and Eni Petroleum Exploration	Kuparuk and Nuiqsut pools in the Oooguruk unit	\$142.31 million (Jun 2008 – Dec 2020)	\$12.4 million since some of the net profit share leases associated with this project reached the “payout” stage.
2008	Eni US Operating Co. Inc.	Schrader Bluff pool in the Nikaitchuq unit	\$567.56 million (Feb 2011 – Dec 2020)	No net-profit-sharing revenue yet because the net profit share lease associated with this project has not yet reached the “payout” stage.
2014	Caelus Natural Resources Alaska	Nuna Torok pool in the Oooguruk unit	No royalty since the project was not sanctioned.	No net-profit-sharing revenue, associated with this project, since it was not sanctioned.

Sincerely,

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