

HOUSE BILL NO. 311

IN THE LEGISLATURE OF THE STATE OF ALASKA
TWENTY-SECOND LEGISLATURE - SECOND SESSION

BY REPRESENTATIVE WHITAKER

Introduced: 1/14/02

Referred: House Special Committee on Oil and Gas, Resources, Finance

A BILL

FOR AN ACT ENTITLED

1 **"An Act relating to oil and gas leases; imposing a limit on the Department of Natural**
2 **Resources that relates to the issuance or extension of oil and gas leases containing**
3 **natural gas that is capable of production in paying quantities; and establishing tax**
4 **exemptions related to oil and the recovery of oil from oil and gas leases; and providing**
5 **for an effective date."**

6 **BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:**

7 *** Section 1.** AS 38.05.180(m) is amended to read:

8 (m) An oil and gas lease must cover a reasonably compact area not exceeding
9 5,760 acres, and may be for a maximum period of 10 years, except that the
10 commissioner may issue a lease for a period not less than five years upon a finding
11 that it is in the best interests of the state. An oil and gas lease shall be automatically
12 extended if and for so long thereafter as oil **and** [OR] gas **are** [IS] produced in paying
13 quantities from the lease or if the lease is committed to a unit approved by the

1 commissioner, but the commissioner shall deny an automatic extension of the
 2 lease and may not extend the lease unless the lessee agrees to an amendment of
 3 the lease to include a provision by which the lessee is required to contract to sell
 4 the gas that is produced from the lease and delivered, in good and merchantable
 5 condition and pipeline quality, on the lease or at another mutually agreed
 6 location to a qualified bona fide purchaser. A lease issued under this section
 7 covering land on which there is a well capable of producing oil and [OR] gas in
 8 paying quantities does not expire because the lessee fails to produce oil and [OR] gas
 9 unless the lessee is allowed reasonable time to place the well on a producing status. A
 10 lease issued under this section on which there is a well capable of producing oil
 11 and gas in paying quantities must include a provision by which the lessee is
 12 required to contract to sell the gas that is produced from the lease and delivered,
 13 in good and merchantable condition and pipeline quality, on the lease or at
 14 another mutually agreed location to a qualified bona fide purchaser. Upon
 15 extension, the commissioner may increase lease rentals so long as the increased rental
 16 rate does not exceed 150 percent of the rate for the preceding year. If drilling has
 17 commenced on the expiration date of the primary term of the lease and is continued
 18 with reasonable diligence, including such operations as redrilling, sidetracking, or
 19 other means necessary to reach the originally proposed bottom hole location, the lease
 20 continues in effect until 90 days after drilling has ceased and for so long thereafter as
 21 oil and [OR] gas are [IS] produced in paying quantities. An oil and gas lease issued
 22 under this section that [WHICH] is subject to termination by reason of cessation of
 23 production does not terminate if, within 60 days after production ceases, reworking or
 24 drilling operations are commenced on the land under lease and are thereafter
 25 conducted with reasonable diligence during the period of nonproduction. For
 26 purposes of this subsection,

27 (1) a "qualified bona fide purchaser" is a public or private entity
 28 that enters into a gas purchase agreement or agreements with a lessee or lessees
 29 and has obtained the requisite rights-of-way, licenses, and permits to construct
 30 and operate a natural gas transmission system; and

31 (2) if two or more qualified bona fide purchasers offer to purchase

1 **the gas, the commissioner shall issue or extend the lease only if the lessee enters**
 2 **into an agreement with the qualified bona fide purchaser that, in the judgment of**
 3 **the commissioner, provides the greatest long-term return to the state.**

4 * **Sec. 2.** AS 43.20 is amended by adding a new section to article 1 to read:

5 **Sec. 43.20.046. Exemption for business income of certain taxpayers**
 6 **engaged in the production of oil.** The provisions of this chapter do not apply to the
 7 business income from the production of oil of a taxpayer engaged in the production of
 8 oil from a lease or property in this state

9 (1) for a period of 10 years following the first date of production for
 10 income based on the production that qualifies for an exemption under this section;

11 (2) if the taxpayer earns the income on or after the effective date of this
 12 section;

13 (3) if the taxpayer is a new producer; for purposes of this paragraph, a
 14 taxpayer

15 (A) is a new producer if the taxpayer does not, at the time of
 16 the taxpayer's first claim of the exemption under this section, produce more
 17 than 5,000 barrels of oil a day from the taxpayer's leases or properties;

18 (B) may not be allowed an exemption for the production
 19 activity of

20 (i) a person acquired by the taxpayer by merger or
 21 acquisition unless the production activity independently qualifies for an
 22 exemption under (A) of this paragraph; or

23 (ii) a taxpayer qualifying under this section that is sold
 24 or transferred to a producer that does not qualify for the exemption
 25 authorized by this section; and

26 (4) if the taxpayer increases production from a lease or property by not
 27 less than 25 percent and maintains production at not less than that amount of
 28 production; if, during the 10-year period allowed for an exemption under (1) of this
 29 section, the production falls below the amount of production required under this
 30 paragraph to maintain the exemption, the taxpayer may not claim and obtain the
 31 exemption under this section for any portion of the production for that or any later tax

1 year.

2 * **Sec. 3.** AS 43.55.011 is amended by adding new subsections to read:

3 (e) Except as limited by (f) of this section, if the total amount of oil produced
4 by the producer from a lease increases

5 (1) between the previous tax year and the current tax year, 50 percent
6 of the increase in the total amount of oil produced from the lease during the current tax
7 year is exempt from taxation under this chapter;

8 (2) between the second preceding tax year and the current tax year, 50
9 percent of the increase in the total amount of oil produced from the lease during the
10 current tax year is exempt from taxation under this chapter;

11 (3) between the third preceding tax year and the current tax year, 50
12 percent of the increase in the total amount of oil produced from the lease during the
13 current tax year is exempt from taxation under this chapter;

14 (4) between the fourth preceding tax year and the current tax year, 25
15 percent of the increase in the total amount of oil produced from the lease during the
16 current tax year is exempt from taxation under this chapter; and

17 (5) between the fifth preceding tax year and the current tax year, 25
18 percent of the increase in the total amount of oil produced from the lease during the
19 current tax year is exempt from taxation under this chapter.

20 (f) Exemption from taxation authorized under (e) of this section

21 (1) may be claimed and allowed for each lease only once and for not
22 more than five successive tax years; and

23 (2) may not be computed based on production of an amount of oil from
24 the lease that is less than the amount produced during the first tax year in which the
25 exemption under (e) of this section is claimed and allowed.

26 * **Sec. 4.** AS 43.55 is amended by adding a new section to read:

27 **Sec. 43.55.022. Exemption for certain producers engaged in the**
28 **production of oil.** (a) The provisions of this chapter do not apply to the production
29 of oil from a lease or property in this state by a producer

30 (1) for a period of 10 years following the first date of production that
31 qualifies for an exemption under this subsection;

1 (2) for oil production from a lease or property on or after the effective
2 date of this section;

3 (3) if the producer is a new producer; for purposes of this paragraph,

4 (A) a producer is a new producer if the producer does not, at
5 the time of the producer's first claim of the exemption under this section,
6 produce more than 5,000 barrels of oil a day from the producer's leases or
7 properties;

8 (B) may not be allowed an exemption for the production
9 activity of

10 (i) a person acquired by the taxpayer by merger or
11 acquisition unless the production activity independently qualifies for an
12 exemption under (A) of this paragraph; or

13 (ii) a taxpayer qualifying under this section that is sold
14 or transferred to a producer that does not qualify for the exemption
15 authorized by this section; and

16 (4) if the producer increases production from a lease or property by not
17 less than 25 percent and maintains production at not less than that amount of
18 production; if, during the 10-year period allowed for an exemption under (1) of this
19 subsection, the production falls below the amount of production required under this
20 paragraph to maintain the exemption, the producer may not claim and obtain the
21 exemption under this subsection for any portion of the production for that or any later
22 tax year.

23 (b) A producer may not be allowed an exemption under this section for
24 production for which the producer obtains an exemption under AS 43.55.011(e) and
25 (f).

26 * **Sec. 5.** The uncodified law of the State of Alaska is amended by adding a new section to
27 read:

28 **APPLICABILITY OF AMENDMENT TO AS 38.05.180(m).** The provisions of
29 AS 38.05.180(m), as amended by sec. 1 of this Act, apply to an oil and gas lease entered into

30 (1) on or after the effective date of sec. 1 of this Act; and

31 (2) before the effective date of sec. 1 of this Act and in effect on that date to

1 the extent permitted under the United States Constitution and the Constitution of the State of
2 Alaska.

3 * **Sec. 6.** Sections 2 - 4 of this Act take effect January 1, 2003.