

**ALASKA STATE LEGISLATURE**  
**HOUSE SPECIAL COMMITTEE ON OIL AND GAS**

April 27, 2001

8:10 a.m.

**MEMBERS PRESENT**

Representative Scott Ogan, Chair  
Representative Hugh Fate, Vice Chair  
Representative Fred Dyson  
Representative Mike Chenault  
Representative Vic Kohring  
Representative Gretchen Guess  
Representative Reggie Joule

**MEMBERS ABSENT**

All members present

**COMMITTEE CALENDAR**

SPONSOR SUBSTITUTE FOR HOUSE BILL NO. 190

"An Act levying and collecting a tax on certain North Slope natural gas in place if certain requirements relating to its sale and delivery are not met, and imposing a limit on the Department of Natural Resources that relates to the issuance or extension of oil and gas leases containing natural gas that is capable of production in paying quantities; and providing for an effective date."

- HEARD AND HELD

HOUSE BILL NO. 220

"An Act establishing an exploration and development incentive tax credit for persons engaged in the exploration for and development of less than 150 barrels of oil or of gas for sale and delivery without reference to volume from a lease or property in the state; and providing for an effective date."

- BILL HEARING CANCELED

**PREVIOUS ACTION**

BILL: HB 190

SHORT TITLE:NATURAL GAS PIPELINE INCENTIVE/ GAS TAX

SPONSOR(S): REPRESENTATIVE(S)WHITAKER

Jrn-Date	Jrn-Page		Action
03/16/01	0627	(H)	READ THE FIRST TIME - REFERRALS
03/16/01	0627	(H)	O&G, RES, FIN
03/22/01	0688	(H)	SPONSOR SUBSTITUTE INTRODUCED
03/22/01	0688	(H)	READ THE FIRST TIME - REFERRALS
03/22/01	0688	(H)	O&G, RES, FIN
03/22/01	0688	(H)	REFERRED TO O&G
04/27/01		(H)	O&G AT 8:00 AM CAPITOL 124

**WITNESS REGISTER**

LORI BACKES, Staff  
to Representative Jim Whitaker  
Alaska State Legislature  
Capitol Building, Room 411  
Juneau, Alaska 99801

POSITION STATEMENT: Made a brief state on behalf of the sponsor.

GEORGE FINDLING, Manager  
External Strategies  
Phillips Alaska  
PO Box 100  
Anchorage, Alaska 99510

POSITION STATEMENT: Provided the committee with information and testified in opposition to [SSHB 190].

BARBARA DONATELLI, Executive Vice President  
Cook Inlet Region, Inc.  
PO Box 93330  
Anchorage, Alaska 99509

POSITION STATEMENT:

JACK CHENOWETH, Assistant Revisor  
Legal Counsel  
Legal and Research Division  
Legislative Affairs Agency  
Alaska State Legislature  
Capitol Building  
Juneau, Alaska 99801

POSITION STATEMENT: Provided opinion on state's ability to terminate a lease.

JOE MATHIS, Senior Operations Manager  
NANA Development Corporation

1001 E. Benson  
Anchorage, Alaska 99508  
POSITION STATEMENT: Testified in opposition to [SS]HB 190.

CHRIS JOHANSEN  
Flowline Alaska  
1881 Livengood  
Fairbanks, Alaska 99701  
POSITION STATEMENT: Testified in opposition to [SS]HB 190.

TOM WILLIAMS, Alaska Tax Counsel  
BP Exploration (Alaska), Inc.  
PO Box 196612  
Anchorage, Alaska 99515  
POSITION STATEMENT: Testified that BP opposes [SS]HB 190.

JOHN MINIER, President  
NANA Colt Engineering  
5900 Bluebell Drive  
Anchorage, Alaska 99516  
POSITION STATEMENT: Testified in opposition to [SS]HB 190.

BILL STAMPS, Manager  
Business Development and External Affairs  
Peak Oilfield Service Company;  
President, Alaska Support Industry Alliance  
2525 C Street, Suite 201  
Anchorage, Alaska 99503  
POSITION STATEMENT:

JUDY BRADY, Executive Director  
Alaska Oil and Gas Association  
121 West Fireweed Lane  
Anchorage, Alaska 99503  
POSITION STATEMENT: Testified in opposition to SSBH 190.

LARRY HOULE, General Manager  
Alaska Support Industry Alliance  
4220 B Street, Number 200  
Anchorage, Alaska 99503  
POSITION STATEMENT: Testified in opposition to SSBH 190.

MARY SHIELDS, General Manager  
Northwest Technical Services  
330 Arctic Boulevard, Suite 201  
Anchorage, Alaska 99503  
POSITION STATEMENT: Testified in opposition to [SSHB 190].

SALLY ANN CAREY, Secretary  
[Alaska] Support Industry Alliance  
3264 Montclare Court  
Anchorage, Alaska 99503

POSITION STATEMENT: Testified in opposition to [SSHB 190].

JACK LAASCH, Member  
Executive Board  
Alaska Support Industry Alliance  
3264 Montclare Court  
Anchorage, Alaska 99503

POSITION STATEMENT: Testimony in opposition to [SS]HB 190 read  
by Mr. Carmichael.

BOB CARMICHAEL  
3264 Montclare Court  
Anchorage, Alaska 99503

POSITION STATEMENT: Testified in opposition to [SSHB 190].

BOB STINSON, President  
CONAM Construction Company;  
Vice President, Alaska Support Industry Alliance  
3015 Seawind  
Anchorage, Alaska 99516

POSITION STATEMENT: Testified in opposition to [SS]HB 190.

#### **ACTION NARRATIVE**

TAPE 01-33, SIDE A  
Number 0001

CHAIR SCOTT OGAN called the House Special Committee on Oil and Gas meeting to order at 8:10 a.m. Representatives Ogan, Dyson, Chenault, Fate, and Joule were present at the call to order. Representatives Kohring and Guess arrived as the meeting was in progress.

#### HB 190-NATURAL GAS PIPELINE INCENTIVE/ GAS TAX

CHAIR OGAN announced that the only order of business before the committee would be SPONSOR SUBSTITUTE FOR HOUSE BILL NO. 190, "An Act levying and collecting a tax on certain North Slope natural gas in place if certain requirements relating to its sale and delivery are not met, and imposing a limit on the Department of Natural Resources that relates to the issuance or extension of oil and gas leases containing natural gas that is

capable of production in paying quantities; and providing for an effective date."

Number 0071

LORI BACKES, Staff to Representative Jim Whitaker, Alaska State Legislature, made the a brief statement on behalf of the sponsor as follows:

The sponsor of HB 190 requested at the time this bill was introduced, and has maintained since then, that it not be heard unless, after appropriate testimony, a vote be taken by the committee for passage or against passage.

The sponsor's position has not changed. However, Representative Whitaker recognizes the chairman's prerogative, and therefore does not object to HB 190 being heard.

That concluded my statement. I have not been authorized by the sponsor to answer questions from the committee.

CHAIR OGAN explained that he wanted to hear HB 190 "in response to a number of questions" he had submitted to the producers.

Number 0187

CHAIR OGAN read an excerpt from a talk given by former Senator Bob Bartlett to the Alaska Constitutional Convention on November 8, 1955, which he read as follows:

... [The] various bills for statehood enabling legislation which have been introduced in [the] Congress in recent years have ... uniformly called for large grants of land from the United States public domain to be made to the State of Alaska. The figure mentioned has been in excess of 100 million acres, an area roughly equal to the total land area of the State of California. The 100 million acre figure would appear to be approximately the figure which will finally be adopted.

The State of Alaska would choose almost all this acreage from the lands not included in the present federal reservations and withdrawals, or which is

otherwise unappropriated. The 100 million plus acres represents a veritable empire, a wealth of land and resources never before conferred on any state, saving only Texas which, upon its entry into the Union, was allowed to retain all its public lands. Alaska will receive also, in addition to the 100 million acre plus land grant, an uncounted but tremendous acreage of submerged lands, [land] which under decisions of the Supreme Court of the United States have been held in trust for the future state. These submerged lands include lands under [the] beds of navigable rivers, lakes, [and] streams; the tidelands proper; and the submerged soils of the marginal sea out to the three-mile limit. ...

Two very real dangers are present. The first, and most obvious, danger is that of exploitation under the thin disguise of development. The taking of Alaska's mineral resources without leaving some reasonable return for the support of Alaska governmental services and the use of all the people of Alaska will mean a betrayal in the administration of the people's wealth. The second danger is that outside interests, determined to stifle any development in Alaska which might compete with their activities elsewhere, will attempt to acquire great areas of Alaska's [public] lands in order not to develop them until such time as, in their omnipotence and the pursuance of their own interests, they see fit. If large areas of Alaska's patrimony are turned over to such corporations the people of Alaska may be even more the losers [than] if the lands had been exploited.

Number 0437

CHAIR OGAN remarked that some of those fears haven't come to pass and there has been responsible development of Alaska's lands. However, he felt that the excerpt did contain some wisdom in that not all of Alaska's resources have been developed. The argument could be made that Alaska's natural gas is still in the ground.

CHAIR OGAN noted that a number of questions have been asked of the producers such as the type of contracts they enter into, specifically with Australia and Indonesia. Exxon was asked about Yemen, Qatar, Natuna, and Sakhalin. However, Exxon was nonresponsive and claimed that the terms of their agreements

with other governments contain confidentiality agreement provisions that limit their ability to discuss them. Furthermore, obtaining information from those countries on their regimes is very difficult. Chair Ogan did note his appreciation of the candor of the discussion of Phillips and BP. Some discussions revolved around the petroleum mining code in Australia with Phillips. [That code] includes a "use it, lose it" provision in that if there is no commercial development, then it [the petroleum] is relinquished to the country. Chair Ogan expressed interest in Phillips and BP coming to the table to discuss [the information from the countries].

CHAIR OGAN offered his congratulations regarding how the contracts were let out on the Lower 48 pipeline. He was pleased that Alaskan companies were acknowledged.

Number 0839

GEORGE FINDLING, Manager, External Strategies, Phillips Alaska, announced that a letter detailing the licensing provisions is being developed. Mr. Findling then proceeded to give the committee a quick overview. He explained that there are two kinds of licensing provisions covered in the Timor Sea area. First there are the licensing provisions in the Timor Sea gap, which are under a production sharing contract that is authorized under a treaty that was originally between Australia and Indonesia. Although Mr. Findling noted that he isn't an expert on the exact politics, he understood that Indonesia relinquished Timor to the control of the United Nations who will administer Timor until there is a vote on independence. The United Nations adopted the treaty that was originally developed between Indonesia and Australia and then basically [agreed] to administer the production sharing agreement. Mr. Findling pointed out that new rules have changed inside the Timor gap since [Phillips] obtained its license in 1991 and discovery of the Bayu-Undan field in 1995.

MR. FINDLING turned his discussion to the provision of a production sharing contract in the Timor gap area, the so called "treaty area." In the first three years, these are licenses as opposed to leases, which are achieved through a bonus bid in Alaska. The licenses are achieved through a commitment to a work program. For the first three years, there is a firm exploration, evaluation work program, including necessarily seismic and well drilling. This is a six year contract. He explained that originally there is a bid on the work program that is basically adjusted to the results of the third year.

The production sharing agreement basically ensures that the first three years are executed. Contracts can only be terminated for breach. However, if the work program isn't completed, then there are opportunities for remedies. Mr. Findling pointed out that in the last three years contracts can be terminated by mutual agreement.

MR. FINDLING addressed the Bayu-Undan field for which the original execution of the exploration license was in December 1991. The discovery of the field occurred in 1995, after which Phillips determined that it had a gas and condensate field. The condensate is important because it is liquids that can be recovered at the platform through a gas cycling project. Then Phillips immediately were authorized to develop a condensate recovery plan in February 2000. He pointed out that the costs for the exploration and development of the [Bayu-Undan] field are being recovered through the condensate recovery. He noted that there is a second phase of development for the Bayu-Undan field, which is the gas development plan. However, the decision to proceed with that project will be determined separate from the gas condensate recovery and depends upon securing a gas market and co-owner support of a commercial venture. Mr. Findling said, "In no way is our concession at risk for some lack of development of gas. Gas is completely dependent upon developing a market ... and approval of the co-owners."

CHAIR OGAN related his understanding that the project is now in question due to a dispute between East Timor and Australia over royalty percentages or production sharing percentages.

MR. FINDLING agreed with Chair Ogan's understanding. He pointed out that an entity is receiving a certain percentage of the economic rent from the production sharing. That entity was originally Australia and Indonesia, but will eventually be Timor and Australia, he thought. The dispute is over how the sharing of the rent that's paid from the contractor is going to be [divided]. Currently, there hasn't been any direct indication that the rules of the production sharing contract will be changed.

CHAIR OGAN related his understanding of Phillips' position that (indisc.) intent in the production agreement and thus isn't in jeopardy of being relinquished. The gas is a side production (indisc.).

MR. FINDLING agreed.

MR. FINDLING turned to the Northern Territory Petroleum Act and the area outside of the gap area, specifically in the Sunrise field. The Sunrise field straddles the border of the gap and undisputed Australian water. Therefore, part of the area is covered by the production sharing agreement and part is covered by the Northern Territory Petroleum Act. The act is basically a license in which a work commitment is made and then a series of steps are taken. Under the act there are three contractual positions. First, there is the permit, which is basically the manner in which one enters and explores. The permit term is usually 2-5 years and the regulations provide for a renewal at least twice. The permit time, just for exploration, can be up to 15 years. He posed a typical situation in which a block of land with a 2-5 year lease [with] a 5-year term and if one desires to renew, one must collapse and open the acreage for others. The acreage has to be collapsed in two steps in order to renew. Therefore, one would be down to a quarter of their acreage if renewing for the 10-15 year time period. Mr. Findling pointed out that such is very similar to the discussions regarding the exploration licensing debate in Alaska.

MR. FINDLING moved on to the contractual position of a retention license. The act foresees a situation in which one has found hydrocarbons, but they're not commercially available. He said, "There's a way to hold the acreage position even though there's no way to move forward with actual commercial development in hydrocarbons." He noted that the term of these retention licenses are five years and are indefinitely renewable. However, one must obtain approval from the minister to do so. It seems that there must be a good-faith program in place to continue working in direct field activities or in some commercial activities in order to commercialize the prospect. Mr. Findling felt that the government recognized, through this regulation, that retention licenses are a good idea. Mr. Findling pointed out that there is a notice to apply for a production license, which involves a situation in which the minister is looking at the prospect during either the exploration permit or the retention license. In that situation the minister can request that a development program be presented and the licensee has six months to respond. If there is [no] response, the minister can cancel. However, if this occurs during the exploration permit process, the minister has to consider a retention license application before he can ask for a production license.

MR. FINDLING continued with the production license. If one has a discovery in commercial quantities and there is a proposal to the minister to move forward on a production license that can be related to some of the blocks in the permit area, there is a technical work program commitment. "Basically, this comes out in a term of 25 years," he said. He noted that some literature has indicated that the term is 5 years with a renewal to 25 years. However, he understood that the term is 25 years and can be indefinitely renewed as long as there is production. He also noted that it grants exclusive rights to move forward.

Number 1661

MR. FINDLING addressed cancellations. The primary criteria for cancellations under the Petroleum Act seem to be that one hasn't complied with a permit or licensed condition. Again, there is the opportunity to remedy the situation because the minister notifies the entity hasn't complied. He indicated that cancellations can also be due to noncompliance with the law or a lawful directory by the minister. Therefore, the procedure for cancellations is to serve notice with the reasons and the licensee has a month to respond. The minister has to consider the response and some resolution is achieved.

MR. FINDLING concluded by noting that there are two licensing methods one of which is what he described under the gap and the other is under the Petroleum Act. Under the Petroleum Act, there is no requirement that gas has to be commercialized or it is lost.

CHAIR OGAN asked if Phillips has any holders in Indonesia.

MR. FINDLING answered that he believes so, but he wasn't sure.

CHAIR OGAN mentioned that he has an Indonesian production sharing contract paper that says, "If commercial petroleum discovery is not made by the end of the exploration period, the contract shall be automatically terminated." Chair Ogan expressed the importance for the committee to [compare] Alaska's competitors in the international gas market in order to determine whether anything hurts Alaska's ability.

CHAIR OGAN asked if there was anyone present from BP that would like to comment.

Number 1890

PAUL KANEL(PH), Director, Government Affairs, BP Exploration, related his understanding that today's hearing would be in regard to HB 190. Therefore, he had not asked anyone to be present to answer the specific questions [the chair] asked.

CHAIR OGAN referred to a portion of BP's answer to [question 21] which he read as follows: "Once oil or gas is found, the concessions contemplate that it will be brought into production within a reasonable time. ... certain provisions are imposed that include acreage relinquishments and spending commitments."

Number 2024

BARBARA DONATELLI, Executive Vice President, Cook Inlet Region, Inc. (CIRI), said:

I am here today on behalf of CIRI to testify in opposition to House Bill 190 as proposed. ... as most of you know CIRI is an Alaska Native regional corporation formed under the Alaska Native Claims Settlement Act [of] '71 (ANCSA). We at CIRI operate as a for profit company with the mission of serving the economic, social, and cultural needs of our shareholders. CIRI is interested in House Bill 190, in part, because we are in the oil and gas business, as a lessor and landowner, not only of current producing property, but of large tracts of prospective oil and gas lands which we [the company] would like to see explored in the future. We're also interested in the bill because we are in the oilfield service business ... where the success of such operations, including the employment of many shareholders, is dependent on a strong oil industry in the state, which is incentivized to explore and pursue new oil and gas properties.

The most important reason that CIRI is interested in the bill, however, is not because of its direct impact on these particular lines of business. Rather, we're concerned because CIRI is an Alaskan company with about two-thirds of our seventy-two hundred shareholders living, working, and raising their families in the state. And they understand, as we do, that sending a message to the outside world that Alaska is truly open for business is crucial to the

economic well-being of the state and its people. We believe that this bill sends the opposite message.

The bill, as we understand it, would tax North Slope natural gas reserves in place and will not, and cannot be expected to spur development of natural gas any faster than market forces would otherwise allow. If natural gas cannot be produced and sold for a reasonable profit, it simply will not be produced and sold. This bill, rather than providing an incentive to development, appears to simply place an additional tax burden on the oil industry. Thereby increasing the overall cost of development and exploration in the state. The result, we believe, would be detrimental to all Alaskans in that [it would] inhibit economic growth and the vitality in this crucial sector of our state economy.

Even more directly, we believe the bill would provide a disincentive for producers to explore for new gas reserves because such reserves would become ... immediate liabilities on the producers' books if they were not found in sufficient quantities for near-term development and sale. While the bill purports to limit its effects, in this regard, to the North Slope, we believe it sends a message to producers statewide that they could face a similar fate at the hands of the state in an era when we're facing declining oil reserves. The effect could be to lock up further exploration just at a time when we really need to encourage new discovery and development.

The viability of large scale gas production on the North Slope offers significant opportunities for the state, and it's important that the state government, at all levels, [does] what it can to encourage prompt and responsible development of the resource. We think the state should not rush to judgment with a short-term fix which has the potential to backfire in the end. Rather, the state should proceed carefully considering all options to encourage prompt development of the North Slope gas reserves, while at the same time avoiding any approach that would burden the industry to the point of [dis]couraging future investment.

In summary, CIRI supports prompt and aggressive development of North Slope gas reserves and we do not think that House Bill 190 is the way to ensure that this is accomplished. We respectfully urge you not to advance this bill out of committee.

Number 2246

REPRESENTATIVE DYSON asked if it would be fair to surmise, from CIRI's position, that the oil industry would never warehouse Alaska's gas while commercializing investments elsewhere. Representative Dyson clarified that he was asking if CIRI believes that.

MS. DONATELLI replied:

No, I do not believe that that's been the case. ... my understanding is the development of the gas reserves on the North Slope of Alaska really have been mostly dependent on ... market forces at a time when it would be economically viable to expend the money it would take to develop a pipeline to ... get the reserves to market. And that not so much just a fact of warehousing them, but ... the reserves are there and it's just a timing matter of when it's economically viable to get the resource to market.

REPRESENTATIVE DYSON posed a situation in which ten years from now, the industry that owns the gas on the North Slope had other gas supplies other places in the world. The other gas supplies were close to being the same economic value and commercial potential and the industry developed those gas supplies and was not interested in supplying gas to the people of Alaska. He asked what CIRI would propose to encourage the development of Alaska's gas. He also asked whether CIRI would provide disincentives for leaving Alaska's gas in the ground [so that Alaska could access it when necessary].

MS. DONATELLI related her belief that [Alaska] is in a position such that the development of a pipeline to get the natural gas reserves from the North Slope into other parts of Alaska and the country is approaching a point that looks viable. Therefore, the state continuing to encourage the industry to invest is the best way to ensure that the gas will be available to the state and other markets in the near future. It looks as if the timing is here.

Number 2443

CHAIR OGAN remarked then that this bill is a moot point.

MS. DONATELLI said that she wasn't sure the bill would be a moot point. She related her understanding of the language, which she interpreted as a possible disincentive to exploration and development.

CHAIR OGAN agreed that the bill has a flaw that needs to be fixed. He didn't want anything to discourage [anyone]. However, he understood the bill sponsor's point to be that the gas has been there for 30 years and is still there.

Number 2518

REPRESENTATIVE KOHRING inquired as to the chair's intent with HB 190.

CHAIR OGAN announced that he intends to hold HB 190.

REPRESENTATIVE KOHRING expressed concern that merely having HB 190 before the committee opens the prospects of moving HB 190 from committee, which he strongly opposes.

CHAIR OGAN remarked that a bill doesn't move out of committee unless the chair so desires. If a motion is made, then the chair can [adjourn] the meeting.

REPRESENTATIVE KOHRING commented that he didn't even see the point in having this meeting.

CHAIR OGAN turned to AS 38.05.180(m), which Jack Chenoweth referenced in response to questions posed by Chair Ogan regarding the circumstances under which a lease could be terminated. Chair Ogan characterized AS 38.05.180(m) as a "use it or lose it" clause due to the state's ability to let a lease that isn't producing expire. He understood Mr. Chenoweth's [email] to mean that if production of oil or gas never initiated, then the lease is subject to termination. He asked if that would be a fair interpretation.

JACK CHENOWETH, Assistant Revisor, Legal Counsel, Legal and Research Division, Legislative Affairs Agency, Alaska State Legislature, agreed with Chair Ogan's interpretation. In response to Chair Ogan, Mr. Chenoweth said that leases that haven't had anything commercially shipped or sold could be

terminated. He was sure that there must be procedures in place in the department's own regulations. Mr. Chenoweth clarified that it is a question as to whether oil or gas is being produced. In further response to Chair Ogan, Mr. Chenoweth said that he wasn't familiar with the specifics of leases on the North Slope.

Number 2770

JOE MATHIS, Senior Operations Manager, NANA Development Corporation, testified in opposition to HB 190. Mr. Mathis provided the following testimony:

NANA Development Corporation is a major employer and contributor to the economy in Alaska. We employ 1,500 people who work for NANA's 35 subsidiary companies and business affiliates, 30 percent of which are involved directly with the oil industry. Our businesses are focused on generating profits and providing opportunities for over 10,000 shareholders represented by our parent corporation, NANA Regional.

NANA is a leader in developing resources in our State of Alaska. Our corporation is the owner of the resources at the Red Dog Mine, the largest zinc deposit in the world [and] a partial owner of the Endicott oilfield which, as you know, [also] contains significant gas reserves. Because of our status as a broad resource developer in the state, NANA would be negatively impacted by this legislation, as would the producers that are partners with NANA in generating economic prosperity in Alaska. It is NANA's view that House Bill 190 does the opposite of what the sponsors intend, which is to facilitate [the] commercialization of North Slope natural gas. In fact, the imposition of a tax, if the gas were not commercialized within what seems to be an arbitrary timeframe, would add to the risk of bringing the gas to market. Producers are already trying to get the resource to market as quickly as they can, but certain economics have to be in place for commercialization. As you know, the producers have joined together to determine whether there is a commercially viable project for bringing the gas to market.

The most concerning aspect of the legislation is the dangerous signal its passage would send to all

resource development activities. Any time there is a tax on resource reserves; there is a disincentive to explore. Exploration, already the highest risk dollars, is discouraged because Alaska has decided it is willing to tax people on the product of exploration regardless of their ability to produce it. The legislation would create an environment of fear on the part of producers of all other undeveloped resources, whether it's oil or minerals.

In the case of Endicott, if House Bill 190 becomes law, NANA and other producers are going to be discouraged from exploring for more oil and gas because of the probability of also discovering gas that could be taxed even if it is not commercialized or exempted from the legislation as in the Alaska Statutes 43.58.220, that's for the consumption, field operations, or sold for use in production activities. NANA already pays the state a 20 percent royalty and 80 percent of the net profits from oil production at Endicott. Our analysis is that applying these types of taxes to the existing or new gas reserves [discovered] may absorb most of NANA's profit on that field. This certainly does not encourage us to invest more money.

NANA's position is that it's simply bad public policy to consider carving out a tax on just one resource. We are equally concerned about the potential of a future tax on mineral reserves or other undeveloped resources that the legislature decides should be commercialized. There is a multitude of resources in remote areas that could be of great benefit to the state if developed but, again, the economics must be favorable for the producers to bring those resources to market. ...

I urge the members to abandon this legislation and let the producers group complete their feasibility studies of the gas project.

TAPE 01-33, SIDE B

[The portion of Mr. Mathis' testimony in brackets was taken from the written testimony that he read.]

MR. MATHIS continued:

[Why establish an antagonistic relationship between the state and producers before we even have information about the feasibility of the project? We are in a competitive world; the legislature should be in the] role of providing incentives to develop North Slope gas, instead of disincentives [such] as a gas reserve tax.

Number 2937

CHRIS JOHANSEN, Flowline Alaska, informed the committee that Flowline insulates all the pipe on the North Slope. Mr. Johansen testified in opposition to HB 190. Mr. Johansen informed the committee that over the past couple of years, there's been a tremendous effort to find, develop, and produce oil on the North Slope. This past winter, over 800 Fairbanks residents were directly employed in support of those activities. Flowline Alaska shipped over 1,600 truck loads of pipe to the North Slope this year. Another 1,500 truck loads of materials were shipped in support of drilling, exploration, and construction activities. Mr. Johansen said:

I believe that House Bill 190 will have a profoundly negative effect on future North Slope activities, seriously impacting the jobs of hundreds, if not thousands of working men and women across the state. It is illogical to believe that the producers will continue to spend money to locate and identify reserves on which they will be heavily taxed. Over the past five years, the oil industry has made a serious commitment to buy from Alaskan vendors, hire Alaskan workers, and contract with Alaskan companies to provide services. And this year, the producers will spend an additional \$75 million to study, design, permit, and model an optimum design and route for the gas line. This is a substantial amount of money and clearly shows the intention of the producers to move this project forward. Much of that money will be spent here in Alaska with Alaskan businesses. In spite of the good faith efforts being made by the gas producers, House Bill 190 was introduced in March and many of us in the industry believe that this project is moving along at a very rapid rate. With that in mind, I believe that House Bill 190 is ill-conceived, bad faith, and retaliatory effort to intimidate the

industry that provides a significant majority of the state budget.

We cannot forget that the gas producers have an obligation to their shareholders to perform a detailed [and] thorough analysis of the pipeline route, project timing, and, most importantly, the market. Such a detailed analysis takes time, capital, resources, and the expertise of many people. House Bill 190 could be considered an attempt to compel the producers to minimize or sidestep this obligation to their shareholders.

I'd like to take a moment and ask you to consider the outcome of this bill in a slightly different context. It could easily be interpreted as a means to compel the gas producers to construct a gas line to the Lower 48 regardless of the economic feasibility. If that gas line is not profitable, Alaska's 12.5 percent royalty share could be worth nothing. The concept of taxing in-ground reserves is not a new one; it has been tried for many years around the world, more often than not without success. For example, starting in the early 1900s Canada enacted a tax on in-ground gold reserves. Interestingly enough, there are companies that have mined continuously in Canada for over 100 years and not once did they ever report reserves in excess of two years worth of production.

MR. JOHANSEN concluded with the following excerpt from Don Quixote, which he said came to mind when he read HB 190. He quoted the following:

At day break the two travelers find themselves on a plain dotted with thirty or forty windmills. Don Quixote is jubilant. "Look yonder, friend Sancho," he cries. "Fortune has provided me with thirty or forty giants to encounter. When they are dead, we may claim the lawful spoils of our conquest." The naive squire asks, "What giants?" But Don Quixote covered with his shield, lance couched, has already spurred Rosinante forward. He drives his weapon into the revolving sail of the first windmill, but the motion breaks the lance and roughly hurls the horse and rider a good distance away. "Did I not tell you they were windmills," cried Sancho rushing to his aid. Don Quixote replies, "I am truly unlucky for the same cursed sorcerers who

carried away my books and study, have now deprived me of victory by changing these giants into windmills."

Number 2709

CHAIR OGAN informed everyone that he has spent many hours in committees reviewing ways to do incentives. He noted the Pedro van Meurs report and the Stranded Gas Act, which is about to expire. Chair Ogan remarked that one of the motivations for hearing HB 190 is to see the reaction it would generate. He expressed concern that the largest threat to the oil industry in Alaska is the lack of this legislature's discipline in regards to the budget. He estimated that this session, the legislature is going to pass about \$100-\$125 million in new spending. He expressed embarrassment in regard to where [the legislature] is heading. Furthermore, the leaders of the fiscal planning caucus are advocating for a \$250 million income tax that may offset the next two years of spending. However, there will still be a \$500-\$600 million budget gap. He asked, "Where is the outrage?" Therefore, he requested that the [oil industry] work on the biggest threat to the industry, uncontrolled state spending.

Number 2558

REPRESENTATIVE JOULE agreed with Chair Ogan on some points. However, he pointed out that for five years [the legislature] has attempted to cut the budget. In those five years, it illustrated that cutting the budget without reviewing ways to generate revenues merely exacerbates the problem. Therefore, cutting the budget to cut state spending doesn't get "us" anywhere and thus there needs to be review of generating revenues as well because the state is growing as is its needs.

CHAIR OGAN agreed.

Number 2478

TOM WILLIAMS, Alaska Tax Counsel, BP Exploration (Alaska), Inc., noted that the committee packet should contain his written testimony that he will summarize. Mr. Williams informed the committee that AS 43.58 used to be the state's reserves tax and he is one of four people who worked on it. He also informed the committee that he was the director of the Petroleum Revenue Division in the Department of Revenue, which had the responsibility of implementing that reserves tax. Therefore, he expressed his desire to share his experiences from that because there are some technical problems with HB 190.

MR. WILLIAMS pointed out that when he helped pen the legislation that became the original reserves tax, it included an early development incentive credit. He explained that the early development incentive credit was a way for the reserves tax to function as a pre-payment of future production taxes from Prudhoe Bay. Therefore, every dollar paid in reserves tax would provide a dollar of credit and thus when the field came into production, the dollars could be cashed in. The only limitation was that each month only half of the liability could be eliminated and thus it took about a year-and-a-half for the credits to be used up. Mr. Williams expressed concern that that early development incentive credit may create the impression that that reserves tax had or could have had an effect on the timing of when the resources in Prudhoe Bay and the North Slope were developed. Mr. Williams stated that it [the name] didn't have a impact. The companies were doing much to try to get the pipeline built and Prudhoe Bay on line. Mr. Williams said, "I can guarantee that there was no development on the Slope that was accelerated by an hour as a result of that credit."

MR. WILLIAMS pointed out that there is a major difference between the enactment of the reserves tax then and now. Then it was enacted because the state had spent \$900 million, five years of state budget, on the big lease sale in 1969 and it was still going to be two years before the pipeline would be completed. Therefore, the reserves tax allowed the state to stay in business until the revenues and production from Prudhoe Bay could begin. Today, the concern with the reserves tax seems to lie with the desire to [achieve] the development that is expected to accelerate the commercialization of the gas.

Number 2253

MR. WILLIAMS turned to the technical problems with HB 190. He directed attention to page 4, lines 13-16, subsection (a), of SSHB 190, which says that the "tax is levied each calendar year on the full and true value of taxable property ...." However, subsection (b) says, "The annual rate of levy is 2 cents per 1,000 cubic feet." Mr. Williams pointed out, "This reflects the fact that the original version of the bill was either two cents or whatever millage would produce a billion dollars a year, whichever was higher. The percentage of value thing, the millage, has disappeared in the sponsor substitute. So, all you have left is the cents per mcf flat amount, but by keeping the two things together you create ambiguity in the bill." He also pointed out that throughout Section 4 there is reference to full

and true value, although it will have nothing to do with the amount of the tax, which is only [based on] the amount of mcf. Therefore, Mr. Williams recommended that section be rewritten and eliminate all the language referring to value if this is to simply be a volume-based reserve tax. He turned to the language on page 4, line 16, which says "The annual rate of levy is 2 cents per 1,000 cubic feet." "But, it doesn't say of what," he pointed out. Therefore, he suggested specifying what [is being measured].

MR. WILLIAMS, as a former tax official, noted that there are already two tax appeals processes on the book, one of which is for the other property tax the state has. In 1996 an office of tax appeals was created to handle all other state tax cases. Therefore, he inquired as to why [SSHB 190] uses the general administrative law provisions instead of using one of the procedures that is already in place and works well for tax.

Number 2088

MR. WILLIAMS then made the following points on behalf of BP. He said, "Contrary to the apparent premise that underlies this bill, North Slope gas is not stranded because any producer wants to keep it in the ground." The North Slope gas is stranded due to its remote location and the fact that it can't be marketed at its location. Furthermore, wherever the gas goes, it must be deliverable at a price that is competitive with the available alternatives. Mr. Williams pointed out that both HB 190 and SSHB 190 do not address the competitiveness issue of North Slope gas in any of the markets. The [bill] only punishes BP and the other owners for the fact that commercialization hasn't occurred. Mr. Williams informed the committee that the industry has spent over a billion dollars in an attempt to find a way to overcome the economic obstacles of North Slope commercialization. "This year BP, alone, is in the process of spending over \$110 million trying to develop North Slope gas," he specified. He informed the committee that \$86 million [will be spent] on the gas-to-liquids (GTL) plant, which will be a way to send the gas down the existing oil pipeline if it works. Furthermore, BP is paying its third of the \$75 million to move forward on a gas pipeline to the Lower 48. The route is being studied as well as ways in which to build and fabricate a cheaper pipeline. Such improvements will also help LNG (liquefied natural gas) because any LNG project has an 800-mile tail that would cost billions. Therefore, progress is being made in all three areas: LNG, GTL, and a pipeline to the Lower 48.

MR. WILLIAMS pointed out that the more cubic feet of gas there is, the better the economics. Mr. Williams posed a situation in which BP looks for gas, but the project is delayed by litigation and the tax comes into place; all the reserves that were found or may have been found would be taxable. Therefore, such a risk could deter the type of exploration that would be crucial with regard to whether the project [proceeds or not].

MR. WILLIAMS then highlighted [BP's concern] with destabilization. He said, "It's not good to destabilize a fiscal regime. It's an asset that Alaska has. It hasn't changed the rules of the game for over 10 years and that's a big plus, especially now while we're looking at gas commercialization and the billions of dollars of new investment that that will require."

Number 1830

MR. WILLIAMS pointed out that the provisions in Section 3 would prevent DNR from further extensions of the lease unless the lessee makes certain concessions about commercializing the gas. However, this overlooks the fact that the leases are contracts between the state, as the landlord, and the companies, as the tenants. In that sense, it's the same as a building lease. The terms and conditions of the contract establish the legal obligations of each side to the other. Once [those legal obligations] are set, they aren't changed. Although the law under which the leases are issued can change, conditions for new leases will have to be amended to reflect the legislature's changes. However, [the legislature] can't impair the obligations and rights that already exist under existing contracts. He cited language from the Alaska Constitution and the United States Constitution that specify that no law impairing the obligations of contracts shall be passed. Mr. Williams related his belief that the purpose of Section 3 is to reach the current leases. Therefore, he suggested that there will be a legal problem.

MR. WILLIAMS concluded by summarizing that the bill is technically flawed in terms of how the tax would work. Furthermore, it will punish the innocent for circumstances beyond their control and will worsen or harm the economic climate and reach farther than only the oil industry. Also, there is the aforementioned constitutional issue. Therefore, BP opposes this bill and urges the committee not to advance it.

Number 1747

CHAIR OGAN related his belief that it's imperative that the producers and the working group have an announcement regarding the route as well as an upcoming project. He acknowledged that there has been discussion [of such] occurring in December or at the latest, 60 days into session. He asked if such an expectation is realistic.

MR. WILLIAMS remarked that such advice is taken seriously. He said, "I think it's fair to say that we are doing our best and we don't expect to waste our shareholders' money, but I can't judge the outcome of the process until we've gone through the process."

CHAIR OGAN expressed his curiosity as to whether there is any timeline for liquidated damages with some of the contractors that BP is working with.

MR. WILLIAMS replied, "We're doing the best we can. ... We intend to produce results. The only thing is: We can't guarantee it until we know what the results are."

CHAIR OGAN asked if there are timelines in the contracts.

MR. WILLIAMS answered that he didn't know.

CHAIR OGAN requested that someone provide that answer to him at some point.

Number 1552

JOHN MINIER, President, NANA Colt Engineering, testified in opposition to [SS]HB 190. Mr. Minier testified as follows:

NANA Colt Engineering is equally owned by NANA Development Corporation and Colt Engineering. We're one of many NANA's companies heavily involved in the oil sector. We provide engineering services to Phillips Alaska for engineering procurement and construction management services for their Western North Slope operations; and we do a considerable amount of project engineering for BP. I personally have lived in Alaska for over 25 years, and for the past 20 years have been heavily involved in the development of North Slope oil and gas reserves. I strongly oppose House Bill 190. However, I do

appreciate and laud the legislature's efforts to facilitate the commercialization of North Slope natural gas. But forcing the producers to commercialize the gas through a tax is not the way to accomplish what the producers are already trying very hard to do and spending hundreds of millions of dollars to do it.

... why would we, the oil support industry, be in here opposing a bill whose purpose is to facilitate the development of North Slope natural gas when we'd seem to be the obvious benefactors of this bill. Secondly, if we really believe that the oil companies are doing all that they can to market this gas and will continue to do so and when they prove the economics, will market the gas, why are we against the bill. It would be, as you mentioned earlier, ... moot and there would be no onerous taxes or lease implications. But we think the answer to that is fairly simple. This bill is flawed. It is a disincentive for the reasons already mentioned. ... It could potentially reduce the activity [of] the company. Secondly, it's unnecessary .... Third, it changes the playing field yet again. ... What it says to companies is "If you're looking for a stable place to do business, look elsewhere."

MR. MINIER stressed:

The owners have a long and proven track record of trying to pursue every avenue to market their gas. Early on they've looked at natural gas pipelines, ... spike and super-spike options, ... LNG facilities, ... gas pipeline ..., and projects such as gas-to-liquids conversions. They have literally spent hundreds of millions of dollars. Hence, the bill being unnecessary. Recently, conceptual engineering contracts were awarded to various contractors by the North American Natural Gas Pipeline Group (NANGPG). NANA Colt ... and our partners in the "AlasCan Group" joint venture were awarded one of those contracts to move the gas from the North Slope to the Lower 48. This is yet another example of their aggressiveness and their strong desire to market the North Slope gas. So, in short, as business men and women, we're here to request a better approach to incentivizing the North Slope gas for the producers. As citizens, we demand

it because we think our friends and our partners, the North Slope producers and owners of the gas, have earned it and deserved it.

CHAIR OGAN congratulated the in-state industry for rising to the challenge.

REPRESENTATIVE KOHRING expressed his concern about the dangerous message this bill may send to the industry even if it isn't forwarded from this committee.

Number 1238

MR. FINDLING informed the committee that he has provided the committee written testimony [that is included in the committee packet]. He noted that he joined the comments in opposition to [SSHB 190]. Mr. Findling then turned to how the market impacts gas development. As mentioned earlier, oil was developed by pushing ahead. The reason for that was because it was known that oil was a commodity and was fungible; it didn't depend upon identifying a specific market. However, a gas market has to be identified. In regard to Chair Ogan's desire to see an announcement that this project is moving forward, Mr. Findling expressed the need to consider whether such is prudent. He explained that if one is under an "artificial gun" that an entity has to develop a project, then the entity is in a "down position" in comparison to the buyer of the gas. Alaska should want to be in the strongest position, he thought, in order to have the highest well-head and revenues. Mr. Findling said that he didn't believe Alaska should place itself under an artificial mandate that would be known to the market and thus place [the state] at a disadvantage. Mr. Findling noted opposition to [SSHB 190].

CHAIR OGAN pointed out that the natural gas pipeline discussion has been going on since 1975, and therefore many Alaskans are frustrated as gas in other markets is being developed. He indicated his frustration upon hearing of the [development of gas] in Timor. He related his belief that the only way gas will go to the [Lower 48] is if it piggybacks on a Lower 48 project. He reiterated, "I sincerely hope that there's an announcement in time for this legislature to act appropriately because I think its in all of our best interests to do that."

MR. FINDLING acknowledged what the legislature has done in terms of partnership over the years. Mr. Findling recalled a meeting with [Phillips Alaska's] Chairman of the Board, Jim Mulva (ph),

who, in comments relating to Alaska, expressed the need to get [Alaska's] gas project moving fast. Mr. Findling said, "I never get any impression that our company is, in any way, warehousing gas or ... delaying gas development." In regard to the Timor project, Mr. Findling didn't believe that the Timor project and the Alaska project are mutually exclusive. "I think Timor is going to a big market in the North American continent; that's exactly the purpose of the Lower 48 gas pipeline project, ... to deliver to that same market. I want to see both projects happen. I want to see Alaskan gas commercialized," he stressed.

CHAIR OGAN noted that he recognized how important it is for Phillips to look at gas.

Number 0826

BILL STAMPS, Manager, Business Development and External Affairs, Peak Oilfield Service Company; President, Alaska Support Industry Alliance, provided the committee with his written testimony [that was included in the committee packet]. He noted that he is speaking on behalf of both of the above-mentioned groups. Mr. Stamps testified as follows:

Peak is an Alaskan-based general contractor with offices in Anchorage, Prudhoe Bay, Nikiski, and Valdez. We provide construction, fabrication, facility and equipment maintenance, heavy hauling and equipment support for the oil, gas, and chemical industry. We currently employ approximately 1,100 people. All of our business is dependent on the oil and gas industry.

The Alliance membership includes nearly 400 businesses that contract directly with producer companies to provide products and services in support of oil and gas activity. Collectively, we employ about 30,000 people in Alaska and 25,000 are permanent residents. The Alliance mission is to advocate safe and environmentally sound oil and gas exploration, [development] and production for the benefit of all Alaskans. The Alaska Support Industry Alliance is extremely disappointed and alarmed over the introduction of House Bill 190 .... We believe this bill is the most onerous of the session, with provisions and messages that put our industry's health and future in jeopardy.

Sponsors reference the HB 190 assessment as an incentive. This takes a myopic view of a very global and very competitive oil and gas industry. Alaska may be rich in natural gas, but so are many, many other areas of the world: areas with infrastructure already in place; areas with less harsh environments; areas that cost less to do business [in]; and areas that welcome oil and gas developers with tax relief, not additional tax burdens.

Alaska gets approximately 80 percent of its unrestricted revenue from the oil and gas industry so we clearly are a state dependent on natural resource development. Yet with a bill such as this, the legislature is conveying a message to developers and potential developers around the world that Alaska has no stable tax base. When developers are deciding where to invest their money in resource development they will see ... the tax structure in Alaska as a moving target. A gas reserves tax only increases the risks and reduces the benefits for gas owners. Let's call HB 190 what it is. HB 190 is all about the "T-word" - in fact, "tax" is noted in the bill about 40 times. This bill is a disincentive. It's also unfair and irresponsible.

Is it even legal? Original North Slope oil and gas leases were not sold with the promise, assumption, or expectation that new taxes on undeveloped resources would be levied as part of the lease agreement. If that was the case, we can safely assume that far fewer leases would have been sold. How can we justify placing additional fiscal provisions on an already agreed-upon contract between the state and the leaseholders? At best, this brands Alaska with an image of instability. We cannot afford that, especially as the potential [for] commercializing gas comes closer within our grasp.

Natural gas development will have a huge, positive impact on the State of Alaska, all of its residents, and closer to home, to Peak as a company and to our employees and their families, as it will to other members of the Alliance [and] their employees and families. However, this development must be done when the companies who will be investing in that development believe the time is right and not when

members of the Alaska Legislature believe it is right. A bill such as this sends a very negative message to potential investors in Alaska resource development. It also sends a very negative message to the voters in Alaska who depend on having a healthy oil and gas industry to continue to help provide a good environment in which to live and prosper.

While potential gains with natural gas development are profound, Alaskans also have a lot to lose if our lawmakers handle matters poorly, creating a business environment that is risky, not responsive. If Alaska is to bank on our natural gas, we had better project an image of stability. As business people we urge government to leave the economics of business to business people. We urge you to carry out your constitutional duty to "encourage the development of state resources by making them available for maximum use consistent with the public interest."

CHAIR OGAN reiterated that the biggest threat to the industry is the budget.

Number 0412

JIM PLAQUET testified via teleconference. He informed the committee that he is a former business agent for the Operating Engineers Local 302, and is currently a heavy equipment operator member of Local 302. He noted that he worked in Prudhoe Bay this past winter. Mr. Plaquet testified as follows:

This winter organized labor had many Prudhoe Bay projects with BP Exploration and Phillips Alaska. Prudhoe Bay projects this past winter employed over 500 plus Fairbanks workers that helped support their families financially. Besides creating job opportunities, supporting local businesses, and bringing business to Fairbanks companies, it further strengthened our community.

It took Alaskans working with the industry to build the Trans-Alaskan Pipeline (TAPS) and bring Prudhoe Bay oil to market. Many Alaskans worked very hard to make the pipeline a reality. Future opportunities such as gas commercialization can only happen if there is a commitment from Alaskans and the industry to achieve our goals by working together. We, as

Alaskans, should be looking for ways to make development of our gas more economical, rather than seeking ways to thwart future development. Alaska should be open and ready for business and willing to provide a regulatory and tax climate in which we can compete in the global market.

I'm optimistic that as long as we make production of oil and gas in Alaska economically attractive the industry, like any for profit corporation, will aggressively pursue development of new oil fields in Alaska as well as commercialization of North Slope gas. Economically, Alaska and its residents need this continued investment from the oil industry. Working together we have seen projects recently such as Alpine, Tarn, Badami, Northstar, and, the most recent, the Meltwater oilfield development. Thousands of Alaskans have worked on these projects to support their families. The industry has invested billions of dollars in Alaska. Working as a partnership with Alaskans, I think they'll invest billions more. House Bill 190's proposed tax will not help in achieving our common goal of commercializing North Slope gas. Working together as a partnership we will achieve our common goal and Alaskans will continue to have a bright future.

REPRESENTATIVE DYSON inquired as to who contacted Mr. Plaquet about testifying before the committee.

MR. PLAQUET replied, "No one. I came on my own." In further response to Representative Dyson, he said that no one helped him prepare his testimony.

Number 0045

HAROLD HEINZE testified via teleconference. He informed the committee that he has held responsible positions within the oil industry in Alaska as well as the state government. However, he noted that he was appearing as a citizen today who has basically attended every House Special Committee on Oil and Gas that has occurred this session via teleconference. Although Mr. Heinze shared the frustration of many Alaskans regarding the wait to get gas to market, ...

TAPE 01-34, SIDE A

MR. HEINZE remarked that the committee seems to be struggling with the choice between "carrot and stick." He identified [HB 190] as "the stick." Furthermore, he didn't believe the stage had been set to use the "stick" now. Mr. Heinze voiced the need for the committee to do a better job in providing the information that it gathers. For example, at the beginning of the hearing there was reference to a series of questions posed to the oil companies and their responses, which is not readily and easily available to the public in Anchorage or elsewhere. If the desire is to have Alaskans support something like [HB 190], then they need the information. Mr. Heinze also expressed the need for the committee to review what things are important and under their control and would allow gas commercialization to move forward. In particular, the Alaska Oil and Gas Conservation Commission (AOGCC) has exclusive authority over the field rules of Prudhoe Bay, which currently prohibit the sale of gas from Prudhoe Bay. He noted that the [commission] has the right to review those rules and hold hearings. However, since there has been no such action, it would seem to excuse anyone from not marketing the gas at this point. Furthermore, [AOGCC] seems to have been somewhat lax in their timing. He noted his surprise that when [AOGCC] appeared before the committee, there was no further investigation of the timeline under which [the commission] was conducting its business.

MR. HEINZE related his belief that [the legislature] has neglected [the fact] that the governor signing the charter with BP and Phillips provided a standing offer to sell gas by BP and Phillips. "If that isn't a market test, to offer up 1.2 billion cubic feet of gas, I don't know what is," he said. He expressed his desire to have someone questioned in regard to why no one has come forward for the 2.4 billion [cubic feet of gas] in a fixed deal. Mr. Heinze said, "If there is an easy market for this gas, I don't understand why someone hasn't come forward and more importantly, I don't understand why this committee hasn't explored that." Mr. Heinze concluded by saying that at this time, it is premature [to consider HB 190].

CHAIR OGAN announced that he would ensure that the legislative information offices [LIOs] would have the aforementioned written responses. He also announced that he didn't intend to move HB 190 today.

Number 0474

JUDY BRADY, Executive Director, Alaska Oil and Gas Association (AOGA), informed the committee that AOGA is an industry trade

association whose 16 members represent the majority of the petroleum industry in Alaska. The 16 members of AOGA are as follows: Alyeska Pipeline Service Company; Anadarko Petroleum Corporation; BP Exploration (Alaska), Inc.; Chevron U.S.A., Inc.; Cook Inlet Region, Inc.; Cross Timbers Oil Company; ExxonMobil Production Company; Forest Oil Company; Marathon Oil Company; Petro Star, Inc.; Phillips Alaska, Inc.; Shell Western E&P, Inc.; Tesoro Alaska Company; TotalFinaElf E&P USA; UNOCAL; and William Alaska Petroleum, Inc. Ms. Brady provided the following testimony:

I am here today to present AOGA's opposition to Sponsor Substitute for House Bill 190. We strongly oppose this bill as both poor economic policy and poor public policy. We consider this legislation to be a direct disincentive to the commercialization of North Slope natural gas. And one of our big concerns is that this bill, even the fact that it was introduced, will also be the view of market analysts who track and report local actions affecting gas commercialization on a worldwide basis for the specific purpose of informing potential lenders about project viability.

Number 0608

MS. BRADY continued:

HB 190 represents a radical departure from sound economic policy by substituting "pain" for "gain" as the reason to invest in the commercialization of North Slope natural gas. The bill apparently presumes that if shareholders and management are threatened, they'll be more likely to invest, and invest sooner in the commercialization of this gas. [The bill] seems to be based on the premise that an ANS gas project has already been found [to be] commercially viable and that free market incentives have failed when it comes to decisions to invest in the commercialization of North Slope natural gas. This bill represents an odd and disruptive counterpoint to the building public/private momentum now underway as the result of industry commitment to and investment in the commercialization of the North Slope gas reserves. Of greater concern from a competitive market perspective, by signaling a significant move away from Alaska's stable public tax policy, HB 190 actually threatens to

slow the momentum for commercialization of North Slope gas.

... Since the '60s, the oil and gas industry and others have spent about \$1 billion on trying to commercialize this gas. You've heard from the various producers today, what kinds of money they're investing to try to make this gas commercial. You know their boards are interested, their stockholders are interested, their management is interested. The whole world, right now, is looking to see which gas projects are actually going to make it because that's where the lending institutions are going to put their money. ... Some people have said that this is an incentive to speed up the development. It's not, it does add additional expense and it does give this odd message to the people who are looking to see where they're going to put their money.

As proposed tax legislation, [HB 190] sends a signal to the market that the State of Alaska's public policy of stable taxation is eroding. Just as the market has considered a stable tax policy to be critical to attract investment to the ... new commercial oil projects in the past ten years, so will the market consider continued stable tax policy to be critical to attract the additional billions of dollars in financing necessary for new commercial gas projects. You've heard about the concern of the other ... resource groups with long lead times, we share those concerns.

Since, in the final analysis, the deciding factors will be commercial and market vitality which is most improved by reducing costs and risks, both the industry and the state must focus their efforts on those factors that make Alaska's fiscal regime for gas more competitive against those elsewhere in the world.

Number 0834

MS. BRADY concluded:

This present legislature and the legislatures for the past ... 12 years have strongly conveyed the message that Alaska is "open for business." Let's not change that message now when we are in the middle of our best

opportunity in almost two decades, in a very competitive market, to commercialize this gas. Let's work together to do what's necessary to make it happen and hope ... that this is finally it.

CHAIR OGAN turned to Ms. Brady's comment that [HB 190] signals a shift [away] from a stable public tax policy. He asked if AOGA is concerned with the legislature's change in course from budget cutting to now adding dollars. He reiterated that such seems to be more of a threat.

MS. BRADY answered, "I think every organization in the state has been concerned with making sure Alaska has a fiscal policy." She noted that she ran the fiscal summit for Governor Hickel for the last seven or eight years and she was co-chair of the Long-Range Fiscal Planning Commission five years ago. She pointed out that the tools are there, the question is how to put them together. Over the last five years, the legislature did its part by cutting. Now, she sees everyone reevaluating and thus she hoped another plan would result.

CHAIR OGAN expressed his hope that the [oil] industry would come together en masse on that issue as it has on this issue.

Number 1040

LARRY HOULE, General Manager, Alaska Support Industry Alliance, informed the committee that the Alaska Support Industry Alliance is made up of 400 contractors, suppliers, and individuals that provide products and services to the oil and gas industry. The Alliance's membership represents over 25,000 people that work in Alaska and live in Alaska year around. Mr. Houle provided the following testimony:

None of the oil producing companies are members of the Alliance. Instead, we are the 25,000 working men and women that weld pipe, clean the rooms, [drill wells], drive the machinery, day in and day out in Alaska's oil patch.

I am here today to confirm the Alliance's opposition to Sponsor Substitute [for] House Bill 190, a bill that proposes to tax Alaska's proven gas reserves on state leases that have already been purchased by private companies. [House Bill] 190 represents a huge disincentive; in fact, [it is] a deterrent to those

producer companies [that are today working to commercialize North Slope natural gas].

MR. HOULE summarized:

In the Mat-Su Valley alone, the oil and gas industry directly employs 353 people [representing] \$36 million in payroll. Indirectly, the oil and gas industry in the Mat-Su Valley represents almost 16 percent of the total [regional] payroll. In [the] Fairbanks North Star Borough, the [industry directly] employs 565 people, [pays out] \$40 million in annual payroll. Also, almost 16 percent of the nonmilitary payroll in the Fairbanks industry.

We believe that this legislature should be considering true incentives and this bill is not a true incentive ... toward development of North Slope gas. Natural resource legislation is good public policy when it reduces costs and minimizes risks while protecting our environment.

In quick summary, the short title [of SSHB 190] makes reference to a Natural Gas Pipeline Incentive Act. We do not read incentive into this substitute bill. In fact, the word ... "tax" appears over 40 times in the 10-page document. We see the bill as punitive and destabilizing, with the potential to erode any competitive advantage [in the world markets that we have gained in the last decade in Alaska]. We have had a very certain and ... stable tax basis in this state and we would like to see that continue. Basically, our men and women in the oil patch are what I call "meat and potatoes" constituents and those constituents all live in your districts. And we ask you to provide incentives for those people to remain working and House Bill 190 does not do that.

CHAIR OGAN announced that the committee would recess and return at 5:00 p.m. to continue hearing testimony. The committee recessed at 10:00 a.m.

[There is no further recording on Tape 01-34, Side A or B. Recording resumes on Tape 01-35, Side A, when the meeting reconvenes.]

TAPE 01-35, SIDE A

CHAIR OGAN reconvened the House Special Committee on Oil and Gas at 5:09 p.m. Those present upon reconvening were Representatives Ogan, Dyson, and Fate. Representatives Kohring and Chenault joined the meeting as it was in progress.

Number 0110

MARY SHIELDS, General Manager, Northwest Technical Services, testified via teleconference. Ms. Shields provided the following testimony:

Northwest Technical Services provides long- and short-term contract and temporary employees in the State of Alaska both within and outside the oil industry. In fact, last night we held our 20th Anniversary celebration. And we have been actively involved in many work- and civic-related activities in Alaska for all of these years.

Upon reading this proposed piece of legislation, I became very concerned that the tax stability we have fought so hard to achieve in Alaska could be seriously eroded. How can we expect companies to invest in projects when the risk, a gas reserves tax, outweighs the probable benefit? I believe that this is a lose-lose situation. It is certainly a disincentive for any firm to move forward with new exploration until a guaranteed method of transporting the gas to market is operational, and it is not the way to keep Alaskans working.

The companies involved in exploration and development in Alaska have not shied away from high-risk projects. If they had, the North Slope fields would have never been developed; exploration would have stopped before the discovery of Prudhoe Bay. Over the years companies have spent millions of dollars in the search to find a way to commercialize our gas resources and are now in the process of spending \$75 million or more to determine whether there is a commercially viable project which will bring the North Slope gas to the marketplace.

Many of the arguments I could present have already been laid before you this morning. Obviously, as an Alaskan business person, I want the gas line project

to go forward as quickly as possible. Equally obvious is the simple fact that no for-profit company, particularly those answering to shareholders, would slow down a process that would generate revenue for the company. With that in mind and considering the destabilizing effect this bill could have, I humbly submit that this bill is fatally flawed and urge you to defeat it in committee.

Number 0386

SALLY ANN CAREY, Secretary, [Alaska] Support Industry Alliance, testified via teleconference. Ms. Carey read the following testimony:

I appear before you today to offer my negative thoughts on further consideration of HB 190. If the State of Alaska is open for business, this bill doesn't reinforce that message to the long-term developers of our oil and gas fields. Nor does it foster their intent or desire to expand the enormous amount of funds they currently are spending and have spent providing jobs for workers, buying Alaskan goods from vendors, and of services. ... also it does not send a message to other developers or businesses, who we would like to have coming to Alaska to pursue operations and businesses. If this [bill] is to persist, let's not confine this Quixotic, punitive tax to only the major oil industry (indisc.), but let's talk about ... maybe harvested timber, ... the fish we haven't caught yet, ... the tourists that might come, .... This tax is not an incentive, this tax is quite the opposite.

CHAIR OGAN remarked that a recurring theme [of the testimony] seems to be that [SSHB 190] sends a negative message. Chair Ogan reiterated his concerns regarding the budget and asked Ms. Carey if she viewed that as an equal, if not greater problem.

MS. CAREY reminded everyone that the Alliance's goal is to cut the budget.

Number 0629

JACK LAASCH, Member, Executive Board, Alaska Support Industry Alliance, had his testimony read into the record by Bob Carmichael. Mr. Laasch's testimony is as follows:

The Alliance represents those companies in Alaska that depend on a healthy oil and gas industry to provide employment for Alaskans and the sale of goods and services within Alaska. I am writing this letter to express my views on HB 190, which proposes to enact an ad valorem tax on natural gas reserves on the North Slope. I am opposed to HB 190 because it increases the risks that producer companies already face in developing Alaska's gas resources. It is important that companies that are instrumental in building the foundation of Alaska's economy be given every opportunity to succeed.

Alaska's oil and gas support contractors and vendors depend on a healthy industry to provide employment and opportunities to generate revenues. These contractors and vendors also have a significant investment in Alaska. In the past, the major producers have been willing to invest in Alaska's high-risk projects. Successful development has resulted in many benefits to the communities of Alaska through contributions to charitable organizations and community enhancement projects. In addition, Alaskan companies have been contracted to provide manpower and equipment for services such as construction, maintenance, drilling, fabrication, module assembly, and many others. Since the initial discovery of North Slope gas, many hundreds of millions of dollars have been spent to commercialize this gas. Recently, the producers have committed to spend an additional \$75 million on a study to determine how to bring North Slope gas to market. Many Alaskan companies will participate in this study and the subsequent contracts leading to the construction of a gas pipeline project.

I feel that the State of Alaska needs to present itself as a good partner with the industry in striving for a win-win situation on both sides. In doing so, the state needs to create incentives for producers to pursue commercialization of gas, and hence create opportunities for Alaska's residents and the companies doing business in Alaska. The gas reserve tax does not create this incentive.

BOB CARMICHAEL, on his own behalf, testified via teleconference. Mr. Carmichael noted that he has worked in Alaska's oil

industry. He said that [SSHB 190] is not the best solution for the problem and thus he recommended that it not pass.

Number 0868

BOB STINSON, President, CONAM Construction Company; Vice President, Alaska Support Industry Alliance, testified via teleconference. [His written testimony is included in the committee packet.] Mr. Stinson noted that he does not support [SSHB 190] for many of the reasons already mentioned today. Mr. Stinson provided the following testimony:

If this bill is an attempt to provide an incentive to current producers of gas on the North Slope to accelerate the Alaska gas pipeline project, I think it is at least premature, and at most maybe you could cancel the project. And I'll be more specific. If there were a tax on gas reserves that are imposed by a certain date if a pipeline didn't get built, why would the current Alaskan producers spend the money to try to find more gas in the interim to increase the reserves? Why would new companies look to Alaska to explore for oil and gas if they knew they might be taxed for any newly discovered reserves without the certainty of getting it to market? Increasing reserves helps the overall economics of the project. The more gas you have, the more money you make, and the more the state makes.

I think the best way to ensure that a pipeline gets built is to work with the producers and assist in doing the things they need to do to make the project work, not to work against them in an adversarial role. What if ANWR opened? Would prospective leaseholders there assume there might be the threat of similar taxes, and decide not to invest in exploration and production of oil and gas in a place that is already one of the most expensive places in the world to produce it? I think they might look elsewhere.

This issue is premature because the feasibility process the producers are going through now has to be done regardless of the implications of a gas reserves tax. As an Alaskan pipeline contractor, who has recently designed, built, and permitted a pipeline project, I know how long it takes to go through the process. For an 8-mile project, it took me 16 months

and \$2 million to work through the permitting process. The current group of Phillips, BP, and Exxon has committed to doing it roughly in nine months for a 1,900-mile project, with the largest gas conditioning plant in the world, compressor stations, a natural gas liquids plant, and more pipelines from there to the Lower 48. I ... think we need to be patient and work with the producers through this process ....

CHAIR OGAN noted his agreement that the bill as written would be a disincentive for additional exploration.

Number 1115

TOM MARSHALL (PH) testified via teleconference and informed the committee that he is a retired petroleum geologist. He noted that he has been connected with the oil and gas business for over 50 years. Mr. Marshall (ph) read the following testimony [that was sent to the committee via e-mail]:

I'm very much opposed to this bill. It will certainly discourage gas exploration at a time when prudent reserves on the North Slope are grossly insufficient to supply either the highway pipeline or the Valdez LNG schemes. Proponents of this bill say the gas owners are warehousing North Slope gas, but never mention that every day gas liquids worth \$1.5 million are recovered from the reinjected gas produced with oil at Prudhoe Bay. And the natural gas base press maintenance project has increased ultimate recovery 35 percent, yielding a \$95 billion increase in the market value of oil production. Gas in the ground at Prudhoe Bay is far better for the state than money in the bank. Nationwide, natural gas sold, during the first quarter of 2001, averaged \$6.45 mcf; that's two-and-a-half times the average price of \$2.46 in the first quarter of the year 2000.

... I worked for an independent gas producer in Wyoming in the early '50s when a reserve tax was proposed by the livestock interests after a heavy, late, spring snow that decimated the lamb and calf crop. The proposed tax was dropped when the ranchers realized that counting reserves was not at all like counting sheep because there can be a wide difference of opinion among qualified reservoir engineers and

geologists due to uncertain well control and interpretation of gas in place and reservoir continuity. The ranchers withdrew the bill after deciding it could be a reservoir engineers job security act.

CHAIR OGAN reiterated his intention to hold the bill after determining that no one else wished to testify.

Number 1351

REPRESENTATIVE KOHRING thanked all those who testified today as well as the industry for its investment in Alaska. Representative Kohring expressed the need to take care when working with the [oil and gas industry] in order to ensure that they are encouraged to make further investments in exploration and development. Perhaps, there could be incentive legislation to encourage [exploration and development].

There was discussion regarding interim endeavors for the committee.

#### **ADJOURNMENT**

There being no further business before the committee, the House Special Committee on Oil and Gas meeting was adjourned at 5:28 p.m.