

ALASKA STATE LEGISLATURE
SENATE RESOURCES COMMITTEE

March 18, 2002
3:38 p.m.

MEMBERS PRESENT

Senator John Torgerson, Chair
Senator Gary Wilken, Vice Chair
Senator Rick Halford
Senator Robin Taylor
Senator Ben Stevens

MEMBERS ABSENT

Senator Kim Elton
Senator Georgianna Lincoln

COMMITTEE CALENDAR

CS FOR SENATE BILL NO. 280(L&C)

"An Act permitting grants to certain regulated public utilities for water quality enhancement projects and water supply and wastewater systems."

MOVED CSSB 280(RES) OUT OF COMMITTEE

CS FOR SENATE BILL NO. 240(STA)

"An Act relating to the crimes of murder, conspiracy, criminal mischief, and terroristic threatening; making conforming amendments; and providing for an effective date."

MOVED CSSB 240(STA) OUT OF COMMITTEE

HOUSE BILL NO. 307

"An Act delaying to June 30, 2007, the last date by which hydrocarbon exploration geophysical work must be performed or drilling of a stratigraphic test well or exploratory well must be completed in order for a person to qualify for an exploration incentive credit."

HEARD AND HELD

PREVIOUS COMMITTEE ACTION

SB 280 - See Labor and Commerce minutes dated 2/19/02 and 3/5/02.

SB 240 - See State Affairs minutes dated 1/24/02, 1/31/02 and

2/12/02.

HB 307 - No previous action to consider.

WITNESS REGISTER

Senator Gene Therriault
State Capitol Bldg.
Juneau AK 99811

POSITION STATEMENT: Sponsor of SB 280.

Mr. Dan Easton, Director
Division of Facilities Construction & Operation
Department of Environmental Conservation
410 Willoughby Ste. 303

POSITION STATEMENT: No position on SB 280.

Ms. Annie Carpeneti
Department of Law
PO Box 110300
Juneau, AK 99811-0300

POSITION STATEMENT: Commented on SB 240.

Representative Fate
State Capitol Bldg.
Juneau AK 99811

POSITION STATEMENT: Sponsor of HB 307.

Mr. Mark Myers, Director
Division of Oil and Gas
Department of Natural Resources
400 Willoughby Ave.
Juneau, AK 99801-1724

POSITION STATEMENT: Neutral position on HB 307.

Mr. Jim Dodson
Andex Resources L.L.C.
Houston TX

POSITION STATEMENT: Supported HB 307.

ACTION NARRATIVE

TAPE 02-11, SIDE A

Number 001
#SB280

SB 280-WATER/SEWER/WASTE GRANTS TO UTILITIES

CHAIRMAN JOHN TORGERSON called the Senate Resources Committee

meeting to order at 3:38 p.m. and announced SB 280 to be up for consideration.

SENATOR TAYLOR moved to adopt the proposed committee substitute (CS) to SB 280.

CHAIRMAN TORGERSON noted that the committee had already adopted the committee substitute.

SENATOR TAYLOR withdrew his motion.

SENATOR THERRIAULT, sponsor of SB 280, said the bill was introduced to allow water and sewer grants to be available to those communities that have made the decision to sell their municipal utility into private ownership. Currently, privately owned public water and wastewater utilities are not eligible to participate in the grants under AS 46.03.030 (b).

The public policy call that the legislature made a couple years ago with regards to low interest loan funds was that the program was to benefit Alaskan constituents and just because of a decision to sell the utility, the constituency is still the same. As long as the availability of the groups that can make access to the loans or now the grants under this bill are regulated by the RCA, to insure that the benefits flow through to the rate payer and don't necessarily accrue to the owners of the utility. We feel comfortable that we should make that public policy call to continue to serve the constituents and we have worked with the Department of Environmental Conservation on the wording and the Labor and Commerce Committee adopted wording that was suggested by the department. The language is not Fairbanks-specific and would apply to municipalities who in the future might want to consider whether they should sell their utility.

SENATOR HALFORD said section 3 limits the private for profit utilities to only those that are the primary utilities for municipalities and asked if that's how it was supposed to read.

SENATOR THERRIAULT said yes.

SENATOR HALFORD said that all the private water systems in his district would be ineligible.

SENATOR THERRIAULT explained that originally it was pretty wide open, but then it would apply to every trailer park that has a system. That would mean a lot more new applicants to the pool who

had not participated in this process before and higher administrative costs.

SENATOR HALFORD said he could see putting a size limitation on the program, but making grants available at a higher rate of eligible cost to smaller municipalities. They would be making smaller grants than would apply to the water system in, for example, the Municipality of Anchorage, which is much larger than those in communities with 1,000 people in them. If they were eligible, they would be under the 50 percent cap because they are in a larger community. He thought this might be discriminatory towards the private sector systems that may be very big systems.

SENATOR THERRIAULT said the committee could consider limiting the grants so that they do not go to small trailer parks, for instance.

SENATOR HALFORD noted that the initial fiscal note had an estimate of 50 private utilities but a more recent fiscal note is zero. He asked if that was the difference.

SENATOR THERRIAULT said it was.

SENATOR TAYLOR said his question regards section 2 that says a public utility is eligible to apply for a grant if the utilities' rates are subjected to regulation by the RCA. Other than some telephone companies in all four of the major communities he represents, none of them are subject to regulation under the RCA because they're home ruled municipalities and they operate their own water, sewer and electrical systems. They would not be able to apply for any of these grants.

CHAIRMAN TORGERSON explained that he was looking at the Labor and Commerce committee substitute and that was now in section 3.

MR. DAN EASTON, Director, Division of Facility Construction and Operations, DEC, said DEC has not taken a position on this bill. It's a policy issue that DEC can implement either way, with or without privately owned utilities.

CHAIRMAN TORGERSON said they would start with Senator Halford's question about limiting municipal eligibility to the primary utility. He asked if there is a better way to word it to include some of the larger users that aren't the primary server, but may serve more than a smaller municipality of 1,000.

MR. EASTON said there is a way to do that. The bill started out including everybody that was RCA regulated and was down to basically 10 customers. That added about 30 utilities to the eligibility pool.

CHAIRMAN TORGERSON asked how many communities are not RCA regulated, such as Ketchikan.

MR. EASTON replied that the municipal systems generally are not RCA regulated; they are exempt.

SENATOR HALFORD asked if private systems within a municipality are regulated.

MR. EASTON replied that they are if they serve more than 10 people.

SENATOR STEVENS said he heard in the Labor and Commerce Committee that 36 communities are regulated now and this bill would add another 50. The concern was that by almost tripling the pool, the size of the grants would go down. He asked how big the grant pool is.

MR. EASTON replied that there are 20 existing non-municipal RCA regulated water and sewer utilities. DEC estimates that another 30 are subject to regulation, but aren't currently regulated by the RCA. The total pool of non-municipal privately owned water-sewer utilities would be about 50. Thirty-six municipalities in the last 10 years participated in the program. He surmised, "So, it involves an increase from 36 to 86 in the eligibility pool."

SENATOR HALFORD asked if the legislature opens it up to cover any private utility, would DEC establish some kind of criteria for rating the proposals. He thought as long as DEC uses criteria to rate them, all of their constituents should be in the same pool and have the same opportunity.

MR. EASTON responded that if you increase the pool of applicants and shift it toward the small grant recipients, it creates work for his division and that would require another position.

CHAIRMAN TORGERSON asked how many utilities serve 10 to 50 customers.

MR. EASTON replied about 20 of the total 50 are larger ones and about 30 serve less than 100 customers.

SENATOR HALFORD asked how they choose between the grant applications now.

MR. EASTON explained that they are ranked and scored on the basis of public health impact, environmental impact, community operation maintenance capacity and a number of lesser factors. DEC assigns a numerical rank based on those factors.

SENATOR HALFORD asked if DEC could score the other private

utilities in the same way.

MR. EASTON replied yes.

SENATOR HALFORD said the operational fiscal note will be different if they try to make it apply to everybody. He asked what the operational fiscal note would be.

MR. EASTON said \$94,000.

SENATOR TAYLOR said a lot of trailer courts out there serve more than 10 customers, but if the service is included in the rental fee, they aren't regulated by anyone except DEC, who forces them to check their water and chlorinate and do other things. He asked if DEC expects the pool to expand with those who might wish to be regulated if they had this advantage.

MR. EASTON replied yes. "These grant programs could serve as an incentive to become RCA regulated."

SENATOR TAYLOR said:

That's going to automatically preclude all the systems that I have the most concern about right now. That is Wrangell, Petersburg, Sitka and Ketchikan are not going to be able to apply for any of these funds, whereas those other utilities that are now regulated by RCA would be able to apply. It becomes kind of a separate old boys club over here that the rest of the communities can't get into. I'm wondering if there's some reason why we need to use that as the definition point on who gets access to the funds.

MR. EASTON replied that the municipalities would remain eligible for the grants.

So, Sitka, Ketchikan and Juneau would continue to be eligible for the grants. The reason for requiring RCA economic regulation, I believe, is that any advantage that is earned by virtue of receiving the grant is passed on to the ratepayers. That's a function of RCA regulation.

4:05 p.m.

SENATOR TAYLOR noted that language on page 2, line 17, says that a utility not only has to be the primary utility for a municipality, but "and" is inserted to add, "its rates are regulated." He asked how the communities in his district will

qualify for the grants.

MR. EASTON pointed out that they would qualify under section 1(b), which deals with municipalities. Section 3(i) only applies to privately owned utilities.

SENATOR HALFORD moved on page 2, line 17 to delete "it serves as the primary utility for a municipality and," so it would say, "A public water and sewer utility is eligible for a grant for projects described in (b)(1)-(3) of this section if its rates are regulated by the Regulatory Commission of Alaska."

SENATOR THERRIAULT pointed out that basically takes them back to the original bill.

There were no objections and amendment 1 was adopted.

SENATOR TAYLOR moved to pass CSSB 280(RES) from committee with individual recommendations.

SENATOR WILKEN stated that this bill has an affect on a utility of which he is a shareholder and it also has a positive affect for constituents that he represents.

There were no further comments and CSSB 280(RES) passed from committee.

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4:04 p.m.

#SB240

SB 240-TERRORISTIC THREATENING/PIPELINE DAMAGE

CHAIRMAN TORGERSON announced SB 240 to be up for consideration.

MS. ANNIE CARPENETI, Department of Law, said that most of the bill consists of conforming amendments. She explained:

The bill first makes conspiracy to damage an oil or gas pipeline or a supporting facility or commit other forms of criminal mischief in the first degree a class B felony. It also makes conspiracy to commit terroristic threatening in the first degree, which is added in this bill and which prohibits sending real or imitation chemical or biological substances and causing fear or other harm, a Class C felony. It provides that a person commits murder in the first degree, who commits or attempts to commit intentional damage to an oil or gas

pipeline or supporting facilities and in the course of the offense or in the immediate flight from the offense another person is killed it provides that that person commits murder in the first degree. These levels would probably be murder in the second degree under existing law because it would be committing a knowing act with disregard of the consequences, but this raises them to murder in the first degree. It does the same thing - provides that person commits murder in the first degree or who attempts to commit terroristic threatening in the first degree by sending a real or imitation chemical or biological substance and causing fear or other harm. It raises the crime of intentionally causing damage to an oil or gas pipeline from a class B felony to a class A felony. In those levels, the maximum penalties for a class B felony [are] 10 years incarceration and, for a class A felony, it is 20 years incarceration.

It also raises tampering with an oil or gas pipeline or supporting facility from a class C felony to a class B felony. A class C felony has a maximum term of imprisonment of five years. It adds tampering with the water supply or air, atmosphere, with intent to cause physical injury to criminal mischief in the first degree. Current law prohibits tampering with food supply, cosmetics or drugs with the intent to cause physical injury to another. This adds tampering with water or with air.

It makes a class B felony to send a real or an imitation biological substance with intent to frighten people or cause serious public inconvenience. Depending on the circumstances under current law this would either not be a crime or it would be a class C felony. It also adds to terroristic threatening in current law, which would be changed to second degree terroristic threatening conduct, such as making a false report that anthrax or another type of biological or chemical substance is being mailed and thus causing public inconvenience or fear. It also adds to terroristic threatening in the second degree making threats against an oil or a gas pipeline. So, those are the major highlights of what it does to Title 11.

There are a number of conforming amendments. The bill, when it was originally introduced, made intentional damage to an oil or gas pipeline a separate offense, a

class A felony. Senate State Affairs decided that they preferred making criminal mischief in the first degree all forms of that conduct - changing it from a class B to a class A felony - which then necessitated changing all of the other forms of criminal mischief so that now, under this version of the bill, there are five levels of criminal mischief. Although the main changes are the ones at the high end, making intentional damage to an oil or gas pipeline and similar activities. Under that section, a class A felony rather than a class B felony.

SENATOR TAYLOR asked, regarding sections 21 and 22, if they picked up domestic violence when they notched everything up.

MS. CARPENETI replied that section 21 is for victim and witness confidentiality. It adds terroristic threatening to those crimes where if a victim wants his or her identity and phone number and address kept confidential and the defendant is representing him or herself, they have to have some sort of procedures so that... [THE TELECONFERENCING WAS CUT OFF AT THIS POINT AND SOME TESTIMONY WAS MISSED.]

SENATOR TAYLOR moved to pass CSSB 240(STA) from committee with individual recommendations. There were no objections and it was so ordered.

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#HB307

HB 307-OIL/GAS EXPLORATION INCENTIVE CREDIT

CHAIRMAN TORGERSON announced HB 307 to be up for consideration.

4:20 p.m.

REPRESENTATIVE FATE, sponsor of HB 307, said it extends the sunset provision of exploration incentive from 2004 to 2007 and expands the incentive to other basins outside of Cook Inlet, which the original bill provided. One reason this bill was brought forward is because there is renewed interest in the Nenana Basin, which has now been identified as a basin of high potential for the exploration of gas. He explained that the geological data goes to the Division of Oil and Gas to use for future programs, either leasing or licensing.

CHAIRMAN TORGERSON asked where the expanding language was.

REPRESENTATIVE FATE explained that AS 41.09.010 defines Cook Inlet specifically. This bill has no definition as to where this takes place, meaning it could be throughout the entire state.

MR. MARK MYERS, Director, Division of Oil and Gas, DNR, said DNR has taken a neutral position on this bill. The purpose of the bill was to allow the state to acquire information or data in areas where it had very little data. It allows the state to pay a portion of that data to share risk. The concept was based on what used to be called a cost well where companies would go out in an area prior to a lease sale, drill a well strictly to get geologic information (not necessarily where they think oil would be). Companies would go together and share the cost. In 1994 that kind of activity wasn't occurring very often, particularly in the interior basins.

I think the thought process behind the original bill was to have the state have incentive to pay for part of the cost should a third party go out there and want to drill a well and was extended also for geophysical data, particularly seismic data. The credit was from a pot of money of \$30 million for the maximum extent of the program up to \$5 million per project. That project, again, would have presumably to consist of wells or seismic data. For seismic data it was line miles or so many dollars per square mile. The program has never been utilized. There have been two applications under the program. One was for geochemical data or sampling of surface rock data to try to figure out what the source potential underneath the area was. That was on the North Slope in an area where the state had a lot of seismic data just south of Kuparuk. The director determined at the time that the information really wasn't that critical to the state since we had what we thought was superior seismic data in the area. So, we did not grant that application.

The second case was in the National Petroleum Reserve Alaska where the state does not get the seismic data. In that case the case granted 18% of the cost of seismics to Anadarko. Anadarko, then, decided to decline accepting that because of the state's ability under this program to show that it had third parties. So, they were convinced the confidentiality of the data for the upcoming lease sales was so important they didn't want to use the credit. So, twice it's been applied for. Once it's been granted. It's never been used.

Again, primarily the data could be from state lands, but regulations require it to be from unleased state acreage. So, if you own a lease in the area and it's on

state land and you want to apply for it, you're not eligible to receive this credit.

The second area where it's on private or federally owned lands, they can keep 25%. That credit is against either royalties, taxes, bonus bids for rentals and is transferable. So, it's real dollars for the credit. It doesn't have to be that company's credit. They can sell to a third party.

So, again, just to summarize. The program is designed to encourage acquisition of data and it's stated that the state either would receive, as in the case of wells potentially drilled on Native lands and certainly the seismic data of wells on private or privately owned land, the state does not receive that data.

The second part of it, the state receives the data. There are some cases where it encourages a lease sale or exploration in an area or competition in an area, but the state wants to have the ability to show that confidential data. On wells that data is generally limited to 25 months when the confidentiality is released, but there is extended confidentiality that in some cases can extend that confidentiality beyond that primary term.

On seismic data that is shot on private lands, the state is not entitled to give that data and, of course, couldn't show that data under normal circumstances. So, to summarize again, there are some very clear advantages in certain conditions for the state I think to contribute to the cost of exploration activities. The other important element is discretionary by the Commissioner of Natural Resources' decision prior to the drilling of that well or shooting the seismic, the commissioner can determine the value of the information to the state and offer an appropriate amount not to exceed \$5 million, then, of the 50% on state owned lands and 25% on privately owned lands. Thank you Mr. Chairman.

CHAIRMAN TORGERSON asked Mr. MYERS to stay on line while he talked to Mr. Dodson who was waiting to testify.

MR. JIM DODSON, Andex Resources, L.L.C., said Andex would like to have the exploration incentive credits extended to seismic and drilling. If they were available, they might shoot a much larger program as it allows their dollars to go further and get more

data. "It eases the burden, those high risk exploratory dollars, if the state could grant some exploratory credits to basically help us to push the envelope..."

He supported extending the bill for three years to help encourage exploration in areas that are not explored or underexplored at this point.

CHAIRMAN TORGERSON asked if Andex has land under exploration that is not state land.

MR. DODSON answered yes, it has lands under option 2.

CHAIRMAN TORGERSON informed him that no credits are available for leases on state land.

MR. DODSON replied that Andex is seeking an exploration license, not a lease on state lands.

CHAIRMAN TORGERSON asked if Andex would participate in the shallow gas leasing sale.

MR. DODSON replied that it's not shallow gas leasing. Andex has applied under the exploration license program for an all depth license in the Nenana Basin.

CHAIRMAN TORGERSON asked if it's their interpretation that they are eligible because it's not a lease.

MR. DODSON replied that is correct. He said that licensing usually takes place in under-explored areas and so the exploration incentive credit would be more applicable there than in an area like Cook Inlet where leasing takes place.

SENATOR HALFORD said the existing statute has been on the books for seven or eight years and no one has used it. He asked Mr. Dodson if Andex Resources intends to make application within the next year.

MR. DODSON answered, "Absolutely. We have sent a preliminary letter to the Division of Oil and Gas, Department of Natural Resources, outlining what our plans are.... We'd like to be shooting seismic data in winter '03 - '04 in the Nenana Basin."

TAPE 02-10, SIDE B

CHAIRMAN TORGERSON asked Mr. Myers to brief the committee on the number of potential companies that would qualify under the exploration licensing part of this instead of the leasing part. He asked if shallow gas leasing would get an exemption as well.

MR. MYERS replied that there are four exploration licenses - one is issued at Copper River where Forrest is the primary operator. They might apply if they want to go forward with seismic data. In addition, there are two companies in the Susitna Basin that are in the application process for about 500,000 acres each. DNR also has the Andex proposal for an exploration license in the Nenana Basin. On private lands, there's nothing to say that an applicant couldn't apply for this program on any Native or federally owned land. It's not geographically restricted.

Since the shallow gas lease program is noncompetitive because companies buy leases, he didn't think a company would apply to explore since another company could come in and file a lease. Shallow gas or coal bed methane wells are relatively shallow and cheap to drill. He pointed out, "They're quicker to actually drill than an exploration well with the intent of production."

Realistically with the shallow gas leasing program, there is no way the program could be used because basically you acquire that non-competitive lease first and then go ahead and drill your well. If not, you're proving up potentially someone else's play.

MR. MYERS thought that many companies could use this bill, but the state would be getting the information anyway. He thought the intent in the end was to get enough interest for a competitive sale when legislation was initially passed. The idea was that exploration would be done and the state would follow through with a conventional lease sale. The commissioner would have to look at the value of the information in licensed areas to promote the development of oil and gas.

CHAIRMAN TORGERSON asked if there had been any application for an EIC under the exploration license program.

MR. MYERS said they had only granted one and are in the process of granting three, "So, it's a relatively new program."

He explained under the licensing program they are required to do a work commitment - so many dollars for a work commitment. The work commitment doesn't necessarily include drilling wells or shooting seismic. He remarked, "It's reasonable to say at this point in time the program is early enough in its life that you would not expect to have many applications under a license scenario."

4:42 p.m.

CHAIRMAN TORGERSON said he was trying to understand why the state would want to give this credit on state land. He said he can understand it for off state land and the purpose for the state to

get data but he didn't understand why they would give the credit on state land just because it has a different license arrangement. He stated, "It seems like we're going backwards."

MR. MYERS responded:

I think you bring up a good point. Again, the program was intended so the state could acquire the information under a license agreement that it's going to get the information anyway. We're not going to get the information any sooner if a well or seismic data is shot on state land. What we do do is give the ability to show that well data before it's publicly released, which is typically 25 months to show the seismic data. The main reasons you would want to do that is to get competition in an area. So if there is a competitive lease sale in the area, you would bring more bidders to the table or get more parties interested in the exploration.

The question is what is the advantage in terms of showing that data earlier on. As Mr. Dodson points out the other advantage is to make the exploration dollars go further. I think in some ways that's not the intent of the original legislation, however. That puts the commissioner in the position where he's going to have to weigh all those factors in determining whether or not they grant an exploration incentive credit as well as your determination of intent with the legislature.

CHAIRMAN TORGERSON said there was no doubt that they needed to work on that. He asked if the maximum credit was \$5 million per well.

MR. MYERS replied that the credit is \$5 million per eligible project and "project" is not defined. It could be wells or a series of wells and it could certainly be seismic data.

CHAIRMAN TORGERSON asked if that was offset against corporate taxes.

MR. MYERS replied, "Taxes, royalties, rentals or bonuses and basically severance tax."

CHAIRMAN TORGERSON asked if that could be carried forward.

MR. MYERS replied that it can.

In reality what we've found - this is the second EIC program. There was another program that involved the competitive leasing instead of the lease term that an EIC of so many dollars per foot is granted for an exploration well. What we've found with that program, companies either used it immediately or they sold it to a third party who used it immediately, the North Slope production typically. I believe the state granted about \$54 million or so in these credits in the other program.

CHAIRMAN TORGERSON asked if he had a position on whether they should extend this to land that the state already owns.

MR. MYERS replied that they are neutral on it.

Again, I think there are cases where you look at other basins, areas not under license where the state wants to get that information acquired. The only way to get that information would be to contribute significantly to it. This does provide a vehicle under the original scenarios that were envisioned. I think that original intent is good, certainly the ability to do that. But it hasn't been used. We certainly want to do it. In an area where it might for example is the NPRA where there may be critical seismic data that because we have no random understanding of whether that be [indisc.] that the state badly needs to see that seismic data and is willing to pay for it. Although companies are under no condition to let us see it.

MR. MYERS said there may be cases on the North Slope where it could be used, for instance a well being drilled on Native land with adjoining state land in an upcoming lease sale.

One of Phillips' wells this winter, for example, in Heavenly is being drilled on Arctic Slope Regional Corporation land, which adjoins state land. I'm not saying we would, but we might want to offer credit in those kinds of circumstances. The other kinds of circumstances are very frontier basins like Kolutna or some area where there isn't sufficient data where the state may say if a company is interested in going in and acquiring baseline data, we're interested in contributing to that cause, because we want to have competitive sales and want to see more activity in that area.

CHAIRMAN TORGERSON asked if Mr. Dodson's company had submitted a

request to them already.

MR. MYERS replied that they had submitted an informal request, but the department needed very specific information because the commissioner has to consider the value of that information to the state and you can't unless you actually see the locations of the wells, what they've drilled, what it would provide or where the seismic series are. They can't in good faith do that until they have a license issued..."

He said that Mr. Dodson is right that the bill might expire before they can use it because of the timing of issuing the license and drilling and operational permits. They are optimistic to get things done by 2004, but there are cases where he might not be willing to drill at that point.

A formal application will have to have more detail than his preliminary letter, but he certainly has explored with us the possibility. I will say one of the things we are concerned about in the license areas, since the license is built on a dollar commitment that is the part of the license you will buy and the winner is the one that puts in the largest dollar commitment for work. We want those dollars in the EIC case to not offset those original dollars that remain from the commitment or the variable part of a bid. So, it would be exploration work in addition to, say, a \$2 to \$3 million commitment to get the license. We don't want to double dip on the same program. If it is used in a license scenario and the commissioner deems it appropriate, we would want to see it as additive, not layered on as an additional incentive on top of the exploration license, which is already...

CHAIRMAN TORGERSON said Mr. Myers hit on the two issues he is concerned with. The first one is that it's already state land and the state has never given credit to get data back off of state land. He had heartburn with that. He said, "Even though by the letter of the law we may be able to do it, I'm not sure that it's good policy to start setting up." The other issue is if the incentive bills working their way through the legislature do pass, the state would end up paying folks to drill. He explained, "I'd like a better handle on all of the things that we may end up passing on these incentive bills including what's already on the books."

4:45 p.m.

SENATOR HALFORD said the fiscal note in 2004 says zero to \$30 million, but existing law goes into 2004. He wanted to know if

the fiscal note is accurate.

MR. MYERS explained that DNR made it that way because \$30 million was the maximum amount that could be used. It could be an error on his part if it's before July 1, 2004. The bill doesn't change the total amount of credits for the program.

SENATOR HALFORD said he wanted to see exactly how this program would stack with any other incentive program in the state.

MR. MYERS replied that he would start by explaining the exploration license itself:

An exploration license - basically the state does not go into a lease mode until the company is ready to or until the license expires. So, a typical exploration license would be a 5 to 10 year period. The state foregoes what would be a competitive bonus bid it would get for the acreage. The license could be up to 500,000 acres. It also foregoes a period of license the typical rentals the state would receive, which in the case of a 500,000 acre license, the max, and the companies typically go for that or near that number, and you went ahead and granted for a seven year period, it would be worth about \$10 million differential than if the state had gotten a minimum bonus bid.

It's substantial value to the party. The party then at the end of the license has committed a work permit that is so many dollars. Typically, we're seeing \$2 to \$3 million for a work permit for a license. That's not money the state receives. That's money that's spent by the company on legitimate exploration activity.

SENATOR HALFORD asked if that was covered in this incentive.

MR. MYERS replied that wasn't covered in this incentive. It is built into the exploration licensing, "So, this incentive has the potential, if the state were to grant it in a licensed area, of overlaying on top of that."

He explained if six wells, an extreme case, were drilled and each determined a project in a given license area, they would be granted the maximum of \$10 million. The state could give in that licensed area \$30 million worth of credits.

In theory, those \$30 million could offset some of the costs that were guaranteed in the exploration license, because remember, they are guaranteeing a work commitment. There is the potential for these to

overlay, but again, this program is discretionary and I don't think the commissioner would take a position that would allow there to be that overlay. But it is theoretically possible that the dollars spent in the exploration license could be offset - at least half of those dollars offset - by the EIC.

Other incentives, then, you could do royalty reduction, which of course, if they were to continue on for a successful exploration program and determine that they couldn't commercially develop at the current royalty rate, the state could grant a royalty reduction down to about 3% under current law.

The severance tax is based of course on the productivity factor for gas fields and low production or for oil - low production. That could be severance tax as low as zero, but it's probably in most commercial cases around 5 to 7% severance tax on top of that. In addition, if the licensed area were in the Cook Inlet area, you could be eligible for a discovery royalty, which would give you a royalty rate of 5% from production for the first 10 years from the date of the discovery. So, those are the main overlays that I am aware of in our programs.

He didn't have that much concern over this particular incentive credit, because of the discretionary nature.

CHAIRMAN TORGERSON asked if there is a cap on how many acres one could get under the exploration license.

MR. MYERS replied that 500,000 acres is the cap per license.

CHAIRMAN TORGERSON asked if a company could hold more than one license.

MR. MYERS replied yes; a company could have up to 2 million acres.

CHAIRMAN TORGERSON asked what the rental fee per acre is under this bill.

MR. MYERS replied that there is no rental fee. He explained:

There is a \$1 per acre initial application fee. There is no other fee other than if they convert if they are successful at the end of the license period and they want to convert to leases. They would then convert to a

standard 12.5% lease and then they would pay the normal rentals, but the rentals will start at \$3 per acre, rather than \$1.

CHAIRMAN TORGERSON asked if they can only explore from this license and not produce.

MR. MYERS said they could theoretically, but they wouldn't get the royalties for it. But from a practical standpoint to get the production credit, they would have to convert to a lease prior to commercial production.

CHAIRMAN TORGERSON asked what will happen if they go to production under the exploration license.

MR. MYERS explained, "They don't have a right to the oil and gas under a license until they convert it to a lease."

SENATOR TAYLOR said he didn't mention the ELF and asked if that only applies to oil.

CHAIRMAN TORGERSON replied that it applies to gas, also.

MR. MYERS explained that it depends on the rate of production, but they would expect in a commercial scenario, the wells would have to have high enough rates in this basin to be commercial in the Fairbanks market. It would probably pay between 5 to 10% severance tax.

CHAIRMAN TORGERSON asked if it was 10% maximum on gas.

MR. MYERS said that was right.

CHAIRMAN TORGERSON added that the state gives the first 3,000 MCF for free, so, it's effectively .8%. He said they needed time to figure out how all this was stacking on top of each other. He asked Mr. Myers if he could put a flow chart together of how this works.

4:55 p.m.

MR. DODSON said it was important to point out that exploration licenses can only be applied for areas outside of the known producing regions in Alaska.

CHAIRMAN TORGERSON said:

My biggest heartburn is that this program was set up to pay for data off of state land. I'm not too sure this isn't oversight that we don't get the data as part of

the license agreement or the lease or something. It's almost mixing oranges and apples. It's like a loophole in the law that lets you take credit for us to get the data. If you want to change the scope of the law, that's a different subject entirely than what we have before us. It seems counterproductive for us pay for our own data off our own land.

REPRESENTATIVE FATE asked if it costs us to get data off our state land and if we wouldn't be able to get it otherwise.

CHAIRMAN TORGERSON said that right now we get the data off the state land. "This program was initially credited to get data off of non state land."

MR. MYERS added, "There are cases where the state, I think, and the intent when this bill was created, [indisc.] to pay for data on leased state land where it could show that data physically to third parties."

He said they also use that data in managing state lands. If they are trying to evaluate that land for its potential on a lease sale, for example, it might be valuable to show that data to other companies and potentially other agencies. He said the original intent of this program was not to overlap with the normal areas like Cook Inlet. He said getting the baseline information in the unleased areas would be important enough to the state that it might want to contribute part of the cost. The state can get the data, but it can't show it to third parties. They might want to promote a lease sale and it would help to get the data out there right away.

CHAIRMAN TORGERSON said the data would eventually be ours, but this is just an accelerated time schedule.

MR. MYERS replied that the state gets their data at the same time either way, but it allows the state to show that data to a third party prior to its being released.

In all cases on wells drilled on state land there's a 25 month period of confidentiality, which can be extended under certain confidentiality circumstances under statute and regulation...For seismic data we get the right again by permit to get the data. That would not be accelerated, but we would be allowed to show that data to a third party. Seismic data is never released by DNR to third parties.

SENATOR HALFORD said, "But the data we're talking about is not fully interpreted. That still is proprietary to the industry."

MR. MYERS replied the data would be the geophysical data from the well. It really depends on what the state is paying for in the data. The state is not going to give a third party its interpretation of the data, but it could if it wanted to.

He clarified that an EIC doesn't allow the state to release the data; it allows them to show the data. "So a company can come into DNR and look physically at the data, but they can't take it with them."

There were no further comments and CHAIRMAN TORGERSON adjourned the meeting at 5:06 p.m.

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