

CS FOR SPONSOR SUBSTITUTE FOR HOUSE BILL NO. 28(RES)

IN THE LEGISLATURE OF THE STATE OF ALASKA

TWENTY-THIRD LEGISLATURE - FIRST SESSION

BY THE HOUSE RESOURCES COMMITTEE

Offered: 5/8/03

Referred: Finance

Sponsor(s): REPRESENTATIVES KOHRING AND ROKEBERG

A BILL

FOR AN ACT ENTITLED

1 **"An Act relating to adjustments to royalty reserved to the state to encourage otherwise**
2 **uneconomic production of oil and gas; and providing for an effective date."**

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

4 *** Section 1.** AS 38.05.180(j) is amended to read:

5 (j) The commissioner

6 (1) may provide for **modification of** [AN INCREASE OR
7 DECREASE OR OTHERWISE MODIFY] royalty [, TO ALLOW FOR
8 PRODUCTION THAT WOULD NOT OTHERWISE BE ECONOMICALLY
9 FEASIBLE,] on individual leases, leases unitized as described in (p) of this section,
10 leases subject to an agreement described in (s) or (t) of this section, or interests
11 unitized under AS 31.05 [; THE COMMISSIONER MAY ACT UNDER THIS
12 SUBSECTION TO MODIFY THE ROYALTY]

13 (A) [AFTER JUNE 20, 1995 AND NOT LATER THAN JULY
14 1, 2015, SO LONG AS THE AUTHORITY TO MODIFY ROYALTY

1 UNDER THIS SUBPARAGRAPH HAS BEEN AUTHORIZED OR
 2 REAUTHORIZED BY LAW WITHIN THE TEN YEARS PRECEDING THE
 3 COMMISSIONER'S ACTION TO MODIFY THE ROYALTY,] to allow for
 4 production from an oil or gas field or pool if

5 (i) the oil or gas field or pool has been **sufficiently**
 6 delineated [SUFFICIENTLY] to **the satisfaction of** [ALLOW] the
 7 commissioner [TO CONDUCT THE ANALYSES AND MAKE THE
 8 FINDINGS REQUIRED BY THIS SUBSECTION]; [AND]

9 (ii) the field or pool has not previously produced oil or
 10 gas for sale; **and**

11 **(iii) oil or gas production from the field or pool**
 12 **would not otherwise be economically feasible;**

13 (B) to prolong the economic life of an oil or gas field or pool as
 14 **per barrel or barrel equivalent** costs [PER BARREL OR BARREL
 15 EQUIVALENT] increase **or as the price of oil or gas decreases, and the**
 16 **increase or decrease is sufficient to make future production no longer**
 17 **economically feasible;** or

18 (C) to reestablish production of shut-in oil or gas **that would**
 19 **not otherwise be economically feasible;**

20 (2) may not grant a royalty modification unless the lessee or lessees
 21 requesting the **change** [MODIFICATION] make a clear and convincing showing that
 22 a modification of royalty meets the requirements of this subsection and is in the best
 23 interests of the state;

24 (3) shall **provide for an increase or decrease or other modification**
 25 **of the state's royalty share by a sliding scale royalty or other mechanism that**
 26 **shall be based on a change in the price of oil or gas and may also be based on**
 27 **other relevant factors such as a change in production rate, projected ultimate**
 28 **recovery, development costs, and operating costs**

29 [(A) CONDITION ANY ROYALTY MODIFICATION
 30 GRANTED UNDER THIS SUBSECTION IN ANY WAY NECESSARY TO
 31 PROTECT THE STATE'S BEST INTERESTS;

1 (B) DESCRIBE, IN THE FINDINGS AND
2 DETERMINATIONS REQUIRED BY THIS SUBSECTION, THE
3 RELEVANT FACTORS, INCLUDING PRICE, PROJECTED
4 PRODUCTION RATE OR VOLUME, PREDICTED ULTIMATE
5 RECOVERY, AND DEVELOPMENT, OPERATING, AND
6 TRANSPORTATION COSTS, UPON WHICH THE MODIFICATION IS
7 BASED;

8 (C) FOR A MODIFICATION UNDER (1)(A) OF THIS
9 SUBSECTION, SET OUT THE TERMS AND CONDITIONS, WHICH

10 (i) MUST INCLUDE A MECHANISM FOR
11 ADJUSTING ROYALTY PERCENTAGE BASED ON PRICE;
12 USING FORECASTS OF THE RANGE OF FUTURE PRICES AND
13 THEIR PROBABILITIES, THE MECHANISM MUST PROVIDE
14 THAT THE VALUE OF THE POTENTIAL REVENUE INCREASES
15 RESULTING FROM ROYALTY PERCENTAGE INCREASES
16 MUST EXCEED THE VALUE OF THE POTENTIAL REVENUE
17 LOSSES RESULTING FROM ROYALTY PERCENTAGE
18 DECREASES; AND

19 (ii) MAY INCLUDE, IN ADDITION TO THE
20 ROYALTY PERCENTAGE ADJUSTMENT BASED ON PRICE,
21 WHICH MUST MEET THE CONDITIONS SPECIFIED IN (i) OF
22 THIS SUBPARAGRAPH, A FURTHER ADJUSTMENT BASED ON
23 PRODUCTION RATE OR VOLUME FROM THE FIELD OR POOL;
24 AND

25 (D) FOR A MODIFICATION UNDER (1)(B) OR (1)(C) OF
26 THIS SUBSECTION, SET OUT THE TERMS AND CONDITIONS, WHICH
27 MAY INCLUDE SUBSTITUTION OF A SLIDING SCALE ROYALTY OR
28 OTHER MECHANISM TO MODIFY THE ROYALTY IF THERE IS A
29 CHANGE IN THE RELEVANT FACTORS, SUCH AS PRICE, PROJECTED
30 PRODUCTION RATE OR VOLUME, PREDICTED ULTIMATE
31 RECOVERY, AND DEVELOPMENT, OPERATING, AND

1 TRANSPORTATION COSTS, UPON WHICH THE MODIFICATION IS
2 BASED];

3 (4) may not grant a royalty **reduction** [MODIFICATION] for a field
4 or pool

5 (A) under (1)(A) of this subsection if the royalty modification
6 for the field or pool would establish a royalty rate of less than five percent in
7 amount or value of the production removed or sold from a lease or leases
8 covering the field or pool;

9 (B) under (1)(B) or (1)(C) of this subsection if the royalty
10 modification for the field or pool would establish a royalty rate of less than
11 three percent in amount or value of the production removed or sold from a
12 lease or leases covering the field or pool;

13 (5) [MAY NOT GRANT A ROYALTY MODIFICATION UNDER
14 THIS SUBSECTION WITHOUT INCLUDING AN EXPLICIT CONDITION THAT
15 THE ROYALTY MODIFICATION IS NOT ASSIGNABLE WITHOUT THE PRIOR
16 WRITTEN APPROVAL OF THE COMMISSIONER; THE COMMISSIONER
17 SHALL, IN THE PRELIMINARY AND FINAL FINDINGS AND
18 DETERMINATIONS, SET OUT THE CONDITIONS UNDER WHICH THE
19 ROYALTY MODIFICATION MAY BE ASSIGNED;

20 (6)] shall require the lessee or lessees to submit, with the application
21 for the royalty **reduction** [MODIFICATION], financial and technical data that
22 demonstrate that the requirements of this subsection are met; the commissioner
23 [SHALL]

24 (A) **may** require disclosure of **only** the financial and technical
25 data related to development, production, and transportation of oil and gas from
26 the field or pool that are **reasonably available to the applicant**
27 [NECESSARY TO MAKE A DETERMINATION AS TO WHETHER OR
28 NOT TO GRANT THE REQUEST FOR ROYALTY MODIFICATION]; and

29 (B) **shall** keep the data [DESCRIBED IN (A) OF THIS
30 PARAGRAPH] confidential under AS 38.05.035(a)(9) at the request of the
31 lessee or lessees making application for the royalty **reduction**

1 [MODIFICATION; THE CONFIDENTIAL DATA MAY BE DISCLOSED
 2 BY THE COMMISSIONER TO LEGISLATORS AND TO THE
 3 LEGISLATIVE AUDITOR AND AS DIRECTED BY THE CHAIR OR
 4 VICE-CHAIR OF THE LEGISLATIVE BUDGET AND AUDIT
 5 COMMITTEE TO THE DIRECTOR OF THE DIVISION OF LEGISLATIVE
 6 FINANCE, THE PERMANENT EMPLOYEES OF THEIR RESPECTIVE
 7 DIVISIONS WHO ARE RESPONSIBLE FOR EVALUATING A ROYALTY
 8 MODIFICATION, AND TO AGENTS OR CONTRACTORS OF THE
 9 LEGISLATIVE AUDITOR OR THE LEGISLATIVE FINANCE DIRECTOR
 10 WHO ARE ENGAGED UNDER CONTRACT TO EVALUATE THE
 11 ROYALTY MODIFICATION, IF THEY SIGN AN APPROPRIATE
 12 CONFIDENTIALITY AGREEMENT];

13 (6) [(7)] may

14 (A) require the lessee or lessees making application for the
 15 royalty reduction under (1)(A) of this subsection [MODIFICATION] to pay
 16 for the services of an independent contractor, selected from a list of qualified
 17 consultants to evaluate hydrocarbon development, production, transportation,
 18 and economics [,WHO IS SELECTED] by the commissioner to assist the
 19 commissioner in evaluating the application and financial and technical data; if,
 20 under this subparagraph, the commissioner requires payment for the
 21 services of an independent contractor, the total cost of the services to be
 22 paid for by the lessee or lessees may not exceed \$150,000 for each
 23 application, and the commissioner shall determine the relevant scope of
 24 the work to be performed by the contractor; selection of an independent
 25 contractor under this subparagraph [PARAGRAPH] is not subject to
 26 AS 36.30;

27 (B) with the mutual consent of the lessee or lessees making
 28 application for the royalty reduction under (1)(B) or (1)(C) of this
 29 subsection, request payment for the services of an independent
 30 contractor, selected from a list of qualified consultants to evaluate
 31 hydrocarbon development, production, transportation, and economics by

1 the commissioner to assist the commissioner in evaluating the application
 2 and financial and technical data; if, under this subparagraph, the
 3 commissioner requires payment for the services of an independent
 4 contractor, the total cost of the services that may be paid for by the lessee
 5 or lessees may not exceed \$150,000 for each application, and the
 6 commissioner shall determine the relevant scope of the work to be
 7 performed by the contractor; selection of an independent contractor
 8 under this subparagraph is not subject to AS 36.30;

9 ~~(7)~~ [(8)] shall

10 [(A)] make and publish a preliminary findings and
 11 determination on the royalty reduction [MODIFICATION] application, [; IF
 12 THE PRELIMINARY FINDINGS AND DETERMINATION CONCERNS A
 13 ROYALTY MODIFICATION UNDER (1)(A) OF THIS SUBSECTION, THE
 14 PRELIMINARY FINDINGS AND DETERMINATION SHALL ALSO BE
 15 PRESENTED TO THE GOVERNOR FOR THE GOVERNOR'S APPROVAL
 16 OR DISAPPROVAL; THE GOVERNOR MAY NOT DELEGATE A
 17 DETERMINATION TO APPROVE OR DISAPPROVE A PRELIMINARY
 18 FINDINGS AND DETERMINATION UNDER THIS SUBPARAGRAPH;

19 (B) FOR A ROYALTY MODIFICATION UNDER (1)(A) OF
 20 THIS SUBSECTION, IF THE GOVERNOR APPROVES THE
 21 PRELIMINARY FINDINGS AND DETERMINATION UNDER (A) OF
 22 THIS PARAGRAPH,

23 (i)] give reasonable public notice of the preliminary
 24 findings and determination, [;

25 (ii) CONCURRENTLY WITH THE ISSUANCE OF
 26 THE PUBLIC NOTICE, UNLESS DIRECTED BY THE
 27 LEGISLATIVE BUDGET AND AUDIT COMMITTEE TO DO
 28 OTHERWISE, MAKE AVAILABLE COPIES OF THE
 29 COMMISSIONER'S PRELIMINARY FINDINGS AND
 30 DETERMINATION ON THE ROYALTY MODIFICATION
 31 APPLICATION AND THE SUPPORTING FINANCIAL AND

1 TECHNICAL DATA, INCLUDING THE WORK PAPERS,
 2 ANALYSES, AND RECOMMENDATIONS OF ANY
 3 CONTRACTORS RETAINED UNDER (7) OF THIS SUBSECTION,
 4 TO PERSONS AUTHORIZED UNDER (6)(B) OF THIS
 5 SUBSECTION TO REVIEW THE DATA;] and

6 [(iii)] invite public comment on the preliminary findings
 7 and determination during a 30-day period for receipt of public
 8 comment;

9 [(C) FOR A ROYALTY MODIFICATION UNDER (1)(B) OR
 10 (C) OF THIS SUBSECTION, IF THE PRELIMINARY FINDINGS AND
 11 DETERMINATION APPROVES A ROYALTY MODIFICATION,

12 (i) GIVE REASONABLE PUBLIC NOTICE OF THE
 13 PRELIMINARY FINDINGS AND DETERMINATION; AND

14 (ii) INVITE PUBLIC COMMENT ON THE
 15 PRELIMINARY FINDINGS AND DETERMINATION DURING A
 16 30-DAY PERIOD FOR RECEIPT OF PUBLIC COMMENT;

17 (9) SHALL ADDRESS IN ANY FINDINGS AND
 18 DETERMINATIONS REQUIRED UNDER THIS SUBSECTION THE
 19 REASONABLY FORESEEABLE EFFECTS OF THE PROPOSED ROYALTY
 20 MODIFICATION ON THE STATE'S REVENUE;]

21 **(8)** [(10)] shall offer to appear before the Legislative Budget and Audit
 22 Committee **on a day that is not earlier than 10 days and not later than 20 days**
 23 **after giving public notice under (7) of this subsection,** to provide the committee a
 24 review of the commissioner's preliminary findings and determination on the royalty
 25 **reduction** [MODIFICATION] application and **administrative process** [THE
 26 SUPPORTING FINANCIAL AND TECHNICAL DATA]; if the Legislative Budget
 27 and Audit Committee accepts the commissioner's offer, the committee shall give
 28 notice of the committee's meeting to all members of the legislature; [IF, UNDER
 29 (6)(B) OF THIS SUBSECTION, THE FINANCIAL AND TECHNICAL DATA
 30 MUST BE KEPT CONFIDENTIAL AT THE REQUEST OF A LESSEE OR
 31 LESSEES MAKING APPLICATION FOR THE ROYALTY MODIFICATION, THE

1 COMMISSIONER MAY APPEAR BEFORE THE COMMITTEE IN EXECUTIVE
2 SESSION;]

3 (9) [(11)] shall make copies of the preliminary findings and
4 determination available to

5 (A) the presiding officer of each house of the legislature;

6 (B) the chairs of the legislature's standing committees on
7 resources; and

8 (C) the chairs of the legislature's special committees on oil and
9 gas, if any;

10 (10) [(12)] shall, within 30 days after the close of the public comment
11 period under (7) [(8)] of this subsection,

12 (A) prepare a summary of the public response to the
13 commissioner's preliminary findings and determination;

14 (B) make a final findings and determination [AND PRESENT
15 IT TO THE GOVERNOR FOR THE GOVERNOR'S APPROVAL OR
16 DISAPPROVAL; THE GOVERNOR MAY NOT DELEGATE A DECISION
17 TO APPROVE OR DISAPPROVE A FINAL FINDINGS AND
18 DETERMINATION PRESENTED UNDER THIS SUBPARAGRAPH]; the
19 commissioner's final findings and determination **prepared under this**
20 **subparagraph** regarding a royalty **reduction** [MODIFICATION, IF
21 APPROVED BY THE GOVERNOR,] is final and not appealable to the court;

22 (C) transmit a copy of the final findings and determination
23 [PREPARED UNDER (B) OF THIS PARAGRAPH] to the lessee [OR
24 LESSEES MAKING APPLICATION FOR THE ROYALTY
25 MODIFICATION];

26 (D) with the **applicant's** consent [OF THE LESSEE OR
27 LESSEES APPLYING FOR THE ROYALTY MODIFICATION], amend the
28 **applicant's** lease or unitization agreement [OF THE LESSEE OR LESSEES
29 APPLYING FOR THE ROYALTY MODIFICATION] consistent with the
30 commissioner's [APPROVED] final **decision** [FINDINGS AND
31 DETERMINATION]; and

1 (E) make copies of the final findings and determination
 2 available to each person who submitted comment under (7) [(8)] of this
 3 subsection and who has filed a request for the copies;

4 (11) [(13)] is not limited by the provisions of AS 38.05.134(3) or (f) of
 5 this section in the commissioner's determination under this subsection.

6 * **Sec. 2.** AS 38.05.180(p) is amended to read:

7 (p) To conserve the natural resources of all or a part of an oil or gas pool,
 8 field, or like area, the lessees and their representatives may unite with each other, or
 9 jointly or separately with others, in collectively adopting or operating under a
 10 cooperative or a unit plan of development or operation of the pool, field, or like area,
 11 or a part of it, when determined and certified by the commissioner to be necessary or
 12 advisable in the public interest. The commissioner may, with the consent of the
 13 holders of leases involved, establish, change, or revoke drilling, producing, and
 14 royalty requirements of the leases and adopt regulations with reference to the leases,
 15 with like consent on the part of the lessees, in connection with the institution and
 16 operation of a cooperative or unit plan as the commissioner determines necessary or
 17 proper to secure the proper protection of the public interest. The commissioner may
 18 not reduce [DECREASE] royalty on leases in connection with a cooperative or unit
 19 plan except as provided in (j) of this section. The commissioner may require oil and
 20 gas leases issued under this section to contain a provision requiring the lessee to
 21 operate under a reasonable cooperative or unit plan, and may prescribe a plan under
 22 which the lessee must operate. The plan must adequately protect all parties in interest,
 23 including the state.

24 * **Sec. 3.** AS 38.05.180(s) is amended to read:

25 (s) When separate tracts cannot be individually developed and operated in
 26 conformity with an established well-spacing or development program, a lease, or a
 27 portion of a lease, may be pooled with other land, whether or not owned by the state,
 28 under a communitization or drilling agreement providing for an apportionment of
 29 production or royalties among the separate tracts of land comprising the drilling or
 30 spacing unit when determined by the commissioner to be in the public interest.
 31 Operations or production under the agreement are considered as operations or

1 production as to each lease committed to the agreement. The commissioner may not
2 **reduce** [DECREASE] royalty on leases in connection with a communitization or
3 drilling agreement except as provided in (j) of this section.

4 * **Sec. 4.** AS 38.05.180(t) is amended to read:

5 (t) The commissioner may prescribe conditions and approve, on conditions,
6 drilling, or development contracts made by one or more lessees of oil or gas leases,
7 with one or more persons, when, in the discretion of the commissioner, the
8 conservation of natural resources or the public convenience or necessity requires it or
9 the interests of the state are best served. All leases operated under approved drilling or
10 development contracts and interests under them, are excepted in determining holding
11 or control under AS 38.05.140. The commissioner may not **reduce** [DECREASE]
12 royalty on a lease or leases that are subject to a drilling or development contract except
13 as provided in (j) of this section.

14 * **Sec. 5.** This Act takes effect immediately under AS 01.10.070(c).