

**CS FOR SPONSOR SUBSTITUTE FOR HOUSE BILL NO. 28(FIN)**

IN THE LEGISLATURE OF THE STATE OF ALASKA

TWENTY-THIRD LEGISLATURE - FIRST SESSION

BY THE HOUSE FINANCE COMMITTEE

Offered: 5/17/03

Referred: Today's Calendar

Sponsor(s): REPRESENTATIVES KOHRING AND ROKEBERG, Masek, Lynn

**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 **reduction** [MODIFICATION] under this  
14 subsection without including an explicit condition that the royalty **reduction**  
15 [MODIFICATION] is not assignable without the prior written approval, **which may**  
16 **not be unreasonably withheld, by** [OF] the commissioner; the commissioner shall, in  
17 the preliminary and final findings and determinations, set out the conditions under  
18 which the royalty **reduction** [MODIFICATION] may be assigned;

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

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

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

1 commissioner to legislators and to the legislative auditor and as directed by the  
 2 chair or vice-chair of the Legislative Budget and Audit Committee to the  
 3 director of the division of legislative finance, the permanent employees of their  
 4 respective divisions who are responsible for evaluating a royalty **reduction**  
 5 [MODIFICATION], and to agents or contractors of the legislative auditor or  
 6 the legislative finance director who are engaged under contract to evaluate the  
 7 royalty **reduction** [MODIFICATION], if they sign an appropriate  
 8 confidentiality agreement;

9 (7) may

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

24 (B) **with the mutual consent of the lessee or lessees making**  
 25 **application for the royalty reduction under (1)(B) or (1)(C) of this**  
 26 **subsection, request payment for the services of an independent**  
 27 **contractor, selected from a list of qualified consultants to evaluate**  
 28 **hydrocarbon development, production, transportation, and economics by**  
 29 **the commissioner to assist the commissioner in evaluating the application**  
 30 **and financial and technical data; if, under this subparagraph, the**  
 31 **commissioner requires payment for the services of an independent**

1 **contractor, the total cost of the services that may be paid for by the lessee**  
 2 **or lessees may not exceed \$150,000 for each application, and the**  
 3 **commissioner shall determine the relevant scope of the work to be**  
 4 **performed by the contractor; selection of an independent contractor**  
 5 **under this subparagraph is not subject to AS 36.30;**

6 (8) shall

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

16 (B) FOR A ROYALTY MODIFICATION UNDER (1)(A) OF  
 17 THIS SUBSECTION, IF THE GOVERNOR APPROVES THE  
 18 PRELIMINARY FINDINGS AND DETERMINATION UNDER (A) OF  
 19 THIS PARAGRAPH,

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

22 (ii) CONCURRENTLY WITH THE ISSUANCE OF  
 23 THE PUBLIC NOTICE, UNLESS DIRECTED BY THE  
 24 LEGISLATIVE BUDGET AND AUDIT COMMITTEE TO DO  
 25 OTHERWISE, MAKE AVAILABLE COPIES OF THE  
 26 COMMISSIONER'S PRELIMINARY FINDINGS AND  
 27 DETERMINATION ON THE ROYALTY MODIFICATION  
 28 APPLICATION AND THE SUPPORTING FINANCIAL AND  
 29 TECHNICAL DATA, INCLUDING THE WORK PAPERS,  
 30 ANALYSES, AND RECOMMENDATIONS OF ANY  
 31 CONTRACTORS RETAINED UNDER (7) OF THIS SUBSECTION,

1 TO PERSONS AUTHORIZED UNDER (6)(B) OF THIS  
2 SUBSECTION TO REVIEW THE DATA;] and

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

6 [(C) FOR A ROYALTY MODIFICATION UNDER (1)(B) OR  
7 (C) OF THIS SUBSECTION, IF THE PRELIMINARY FINDINGS AND  
8 DETERMINATION APPROVES A ROYALTY MODIFICATION,

9 (i) GIVE REASONABLE PUBLIC NOTICE OF THE  
10 PRELIMINARY FINDINGS AND DETERMINATION; AND

11 (ii) INVITE PUBLIC COMMENT ON THE  
12 PRELIMINARY FINDINGS AND DETERMINATION DURING A  
13 30-DAY PERIOD FOR RECEIPT OF PUBLIC COMMENT;

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

18 **(9)** [(10)] shall offer to appear before the Legislative Budget and Audit  
19 Committee **on a day that is not earlier than 10 days and not later than 20 days**  
20 **after giving public notice under (8) of this subsection,** to provide the committee a  
21 review of the commissioner's preliminary findings and determination on the royalty  
22 **reduction** [MODIFICATION] application and **administrative process** [THE  
23 SUPPORTING FINANCIAL AND TECHNICAL DATA]; if the Legislative Budget  
24 and Audit Committee accepts the commissioner's offer, the committee shall give  
25 notice of the committee's meeting to all members of the legislature; [IF, UNDER  
26 (6)(B) OF THIS SUBSECTION, THE FINANCIAL AND TECHNICAL DATA  
27 MUST BE KEPT CONFIDENTIAL AT THE REQUEST OF A LESSEE OR  
28 LESSEES MAKING APPLICATION FOR THE ROYALTY MODIFICATION, THE  
29 COMMISSIONER MAY APPEAR BEFORE THE COMMITTEE IN EXECUTIVE  
30 SESSION;]

31 **(10)** [(11)] shall make copies of the preliminary findings and

1 determination available to

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

3 (B) the chairs of the legislature's standing committees on  
4 resources; and

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

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

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

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

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

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

29 (E) make copies of the final findings and determination  
30 available to each person who submitted comment under (8) of this subsection  
31 and who has filed a request for the copies;

1                    **(12)** [(13)] is not limited by the provisions of AS 38.05.134(3) or (f) of  
2 this section in the commissioner's determination under this subsection.

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

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

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

22                    (s) When separate tracts cannot be individually developed and operated in  
23 conformity with an established well-spacing or development program, a lease, or a  
24 portion of a lease, may be pooled with other land, whether or not owned by the state,  
25 under a communitization or drilling agreement providing for an apportionment of  
26 production or royalties among the separate tracts of land comprising the drilling or  
27 spacing unit when determined by the commissioner to be in the public interest.  
28 Operations or production under the agreement are considered as operations or  
29 production as to each lease committed to the agreement. The commissioner may not  
30 **reduce** [DECREASE] royalty on leases in connection with a communitization or  
31 drilling agreement except as provided in (j) of this section.

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

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

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