

ALASKA STATE LEGISLATURE
HOUSE SPECIAL COMMITTEE ON OIL AND GAS

February 6, 2003

3:17 p.m.

MEMBERS PRESENT

Representative Vic Kohring, Chair
Representative Mike Chenault, Vice Chair
Representative Hugh Fate
Representative Lesil McGuire
Representative Norman Rokeberg
Representative Harry Crawford
Representative Beth Kerttula

MEMBERS ABSENT

All members present

COMMITTEE CALENDAR

HOUSE BILL NO. 69

"An Act relating to regulation of shallow natural gas leasing and closely related energy projects; and providing for an effective date."

- MOVED HB 69 OUT OF COMMITTEE

HOUSE BILL NO. 16

"An Act amending the standards applicable to determining whether, for purposes of the Alaska Stranded Gas Development Act, a proposed new investment constitutes a qualified project, and repealing the deadline for applications relating to the development of contracts for payments in lieu of taxes and for royalty adjustments that may be submitted for consideration under that Act; and providing for an effective date."

- HEARD AND HELD

PREVIOUS ACTION

BILL: HB 69

SHORT TITLE:REGULATION OF SHALLOW NATURAL GAS

SPONSOR(S): REPRESENTATIVE(S) KOHRING

Jrn-Date	Jrn-Page		Action
01/29/03	0086	(H)	READ THE FIRST TIME -

			REFERRALS
01/29/03	0086	(H)	O&G, RES
01/31/03	0108	(H)	COSPONSOR(S): HEINZE
02/05/03	0135	(H)	COSPONSOR(S): MORGAN
02/06/03		(H)	O&G AT 3:15 PM CAPITOL 124

BILL: HB 16

SHORT TITLE: STRANDED GAS DEVELOPMENT ACT AMENDMENTS
 SPONSOR(S): REPRESENTATIVE(S) FATE

Jrn-Date	Jrn-Page		Action
01/21/03	0035	(H)	PREFILE RELEASED (1/10/03)
01/21/03	0035	(H)	READ THE FIRST TIME - REFERRALS
01/21/03	0035	(H)	O&G, RES, FIN
01/21/03	0035	(H)	REFERRED TO OIL & GAS
02/06/03		(H)	O&G AT 3:15 PM CAPITOL 124

WITNESS REGISTER

JACK EKSTROM, Director
 Government Affairs
 Evergreen Resources, Inc.
 Denver, Colorado

POSITION STATEMENT: Answered questions on HB 69.

MARK S. SEXTON, President and Chief Executive Officer (CEO)
 Evergreen Resources, Inc.
 Denver, Colorado

POSITION STATEMENT: Testified in support of HB 69 and answered questions.

JOHN TANIGAWA, Alaska Projects Manager
 Evergreen Resources Alaska
 Wasilla, Alaska

POSITION STATEMENT: Answered questions on HB 69.

CAMILLE OECHSLI TAYLOR, Chair
 Alaska Oil and Gas Conservation Commission
 Anchorage, Alaska

POSITION STATEMENT: Answered questions pertaining to HB 69.

ROGER MARKS, Petroleum Economist
 Economic Research Section
 Tax Division
 Department of Revenue
 Anchorage, Alaska

POSITION STATEMENT: During hearing on HB 16, provided an extensive history of the Alaska Stranded Gas Development Act; said the department generally supports the bill, but that the administration may submit some amendments about which he didn't have specific knowledge.

JOE MARUSHACK, Vice President
Alaska North Slope Gas Commercialization
ConocoPhillips Alaska
Anchorage, Alaska

POSITION STATEMENT: Urged passage of HB 16; cautioned that any amendments or modifications may unintentionally result in delays; said Version H appears to do what his company needs, which is to remove the date and allow a natural gas pipeline, but expressed concern that Section 2 appears somewhat contrary to commercial negotiations.

KEN KONRAD, Senior Vice President
BP Exploration (Alaska) Inc.
Anchorage, Alaska

POSITION STATEMENT: Testified on HB 16; highlighted the need for the state to work with industry to develop a fiscal framework for gas which provides confidence that the rules of the game won't change later; said reauthorizing the Alaska Stranded Gas Development Act is a good idea and that if the bill advances, it should retain its focus and simplicity.

MARK MYERS, Director
Division of Oil & Gas
Department of Natural Resources
Anchorage, Alaska

POSITION STATEMENT: Answered questions on HB 16, Version H.

ACTION NARRATIVE

TAPE 03-3, SIDE A

Number 0001

CHAIR VIC KOHRING called the House Special Committee on Oil and Gas meeting to order at 3:17 p.m. Representatives Kohring, Chenault, Fate, and McGuire were present at the call to order. Representatives Rokeberg, Crawford, and Kerttula arrived as the meeting was in progress.

HB 69-REGULATION OF SHALLOW NATURAL GAS

CHAIR KOHRING announced the first order of business, HOUSE BILL NO. 69, "An Act relating to regulation of shallow natural gas leasing and closely related energy projects; and providing for an effective date."

Number 0111

CHAIR KOHRING, sponsor of HB 69, informed members that HB 69 is intended to help the shallow natural gas industry in streamlining regulations and making it easier for companies to obtain permits more expeditiously. Typically, it takes about one to two years to be issued a permit to drill for natural gas, he reported; the bill is intended to streamline it to 30 to 60 days, thus reducing paperwork and costs.

CHAIR KOHRING said the bill separates two kinds of permitting that currently are under one umbrella. Now, operators drilling shallow gas wells are subject to the same rules and regulations as for big operators that drill for the "deep oil wells" on the North Slope, for example. Offering his belief that there is no clear comparison between the two, he said the bill separates them by giving the Alaska Oil and Gas Conservation Commission (AOGCC) and other agencies the ability to grant variances and bypass some drilling regulations that aren't applicable to [those drilling for shallow gas].

CHAIR KOHRING offered his belief that the legislation will help to greatly expand the shallow natural gas industry. Mentioning that there are several interested companies in the state, he said Evergreen Resources, Inc., is "very aggressively operating"; he thanked representatives from that company for being on teleconference or present to testify. Citing the coal bed methane potential in many villages throughout Alaska, he said he'd been told that as many as 35 villages could benefit from this; because of the ability to drill wells more expeditiously and tap into those potential gas resources, the net effect would be a much cheaper fuel source than diesel, taking pressure off the power cost equalization program.

CHAIR KOHRING described this as good economic-development bill that encourages more growth in this particular industry and streamlines the process. He pointed out that this particular type of gas drilling is low-impact environmentally, using so-called air drilling that reduces toxic wastes because the wells are drilled at very shallow depths and don't require the use of toxic materials such as drilling mud.

Number 0494

REPRESENTATIVE FATE referred to [paragraph (1), beginning on page 1, line 14], which read in part: "(1) the professional staff member or the commission may approve the variance if". He asked whether this mandates that it has to be a staff member, or whether the language implies that "the commissioner can ... authorize anybody from his staff to do it." He said it is a technical question of procedure.

CHAIR KOHRING offered his belief that the [AOGCC] commissioner would make that final decision, although staff could provide advice and do research. He added that it wouldn't be a decision by one [AOGCC] member, but a decision by a quorum of the three-member [commission], which therefore would require at least two members. Noting that someone in the audience [although not from AOGCC] was nodding, he surmised that he'd answered correctly.

REPRESENTATIVE FATE requested clarification. He expressed concern that in the future, if there were some conflict or misunderstanding, there could be a question raised if the commissioner [had relegated it to a staff member]. He said it's a small thing but could loom large later on.

CHAIR KOHRING requested that a representative from Evergreen Resources, Inc., provide an answer, but suggested the likely need to make the change because it clearly says "the professional staff member or the commission".

Number 0713

REPRESENTATIVE FATE moved to adopt the foregoing as Amendment 1.

REPRESENTATIVE ROKEBERG asked what commissioner [Representative Fate] was discussing.

CHAIR KOHRING clarified that it is the [Alaska] Oil and Gas Conservation Commission. He pointed out that line 14 references "the commission" rather than a commissioner. He recommended that Amendment 1 do the following:

Page 1, line 14:

Delete "the professional staff member"

Thus it would say [if "or" were removed as well] "the commission may approve the variance".

REPRESENTATIVE FATE concurred with having that be Amendment 1.

Number 0775

REPRESENTATIVE ROKEBERG objected for discussion purposes. He asked whether the intention is to have the whole commission vote on something, or whether it is a "sign-off or approval."

CHAIR KOHRING offered his understanding that the commission would have to sign off on it, but reiterated his understanding that a quorum of two members, at minimum, of the three-member commission would have to sign off on a variance.

REPRESENTATIVE ROKEBERG withdrew his objection.

Number 0835

CHAIR KOHRING, hearing no further objection, announced that Amendment 1 was adopted.

Number 0848

REPRESENTATIVE KERTTULA referred to page 2, line 4, subparagraph (B) [which also says "the professional staff member or the commission"]. She requested testimony on whether a similar amendment was needed there.

Number 0960

JACK EKSTROM, Director, Government Affairs, Evergreen Resources, Inc., came forward at the invitation of Chair Kohring. He told the committee that AOGCC's practice typically is to "informally approve this without taking a formal vote," but will hold a formal vote if there is conflict. He offered his belief that [the language on page 2, line 4] should be changed to say "the commission". He added, "How exactly they do it is generally worked out among themselves, but I don't think, in this case, you'd want to designate a staff member ... as a substitute for the commission."

REPRESENTATIVE KERTTULA pointed out [language with regard to the professional staff of the commission designated by the commission] on page 1, lines 9-10. Mentioning consistency, she asked whether the idea envisioned was to allow the professional [staff] member to do the work, which the commission would approve or not approve. She said she wasn't sure whether the

language was correct, and asked to have that clarified on the record along with a recommendation.

CHAIR KOHRING suggested hearing from Evergreen Resources, Inc., before taking further action on amending the bill.

Number 1156

MARK S. SEXTON, President and Chief Executive Officer (CEO), Evergreen Resources, Inc., testified in support of HB 69. He informed members that his company owns Evergreen Resources Alaska as a wholly owned subsidiary. He told members:

Evergreen is a Denver, Colorado-based independent energy company. We are principally focused on developing and expanding nonconventional natural gas properties throughout North America. We are recognized as an industry leader in drilling, completion, and production of ... unconventional natural gas wells such as coal bed methane.

In the Raton basin, Evergreen operates 950 coal bed methane wells, which typically produce around 300,000 to 350,000 cubic feet of gas per well per day at their peak. The company has actually more than 1.25 trillion cubic feet of proven natural gas reserves in the Raton basin of southern Colorado, essentially all coal bed methane, and we've developed all of this just in the last eight years. ...

Evergreen is a public company traded on the New York Stock Exchange under the symbol "EVG." A typical Evergreen well will produce for about 25 to 30 years, making these some of the most long-lived wells in industry.

Number 1223

MR. SEXTON noted that the company's Alaskan operations are focusing on the shallow gas resources, particularly coal bed methane extraction. He said Alaska's coal bed methane resource is almost mind boggling - an estimated approximately 1,000 trillion cubic feet of natural gas, enough to supply all of the United States' natural gas demands for eight years at the present rate of consumption, "if you could get that gas out, of course." He added, "There are additional substantial,

unconventional tight gas sand resources that would also benefit from the subject legislation that we are discussing as well."

MR. SEXTON reported that in 2001 the company acquired a 100-percent working interest in the Pioneer Unit, about a 70,000-acre leasehold near Wasilla, and two months ago completed its first phase of operations: two pilot drilling pods of four wells each, for eight wells total, each in a span of less than two days. Suggesting this may be a record for the number of wells drilled in Alaska in a certain amount of time, he also noted that the company's water-disposal well was recently permitted by the AOGCC. "And we anticipate completing and testing our wells in the spring of this year," he added.

Number 1273

MR. SEXTON reported, however, that permitting and leasing have been a challenge, including unique state and local requirements. In Colorado, for example, permitting requires about 15 pages of documents and usually no more than about 30 days. In Alaska that period is extended significantly, not because of regulators, he said, but because of regulations. He remarked that AOGCC has been most helpful and cooperative, and has gone the extra mile, including visiting the company's operations in Colorado and gaining a great depth of understanding of [the company's] methodology and coal bed methane practices in general; he thanked them for the assistance and the positive relationships. He offered a similar observation regarding the [Department] of Natural Resources, which he said has been cooperative and helpful and has provided constructive and instructive assistance.

Number 1404

MR. SEXTON explained that the core issue - and the reason for the company's vigorous support of HB 69 - is that the permitting regime in Alaska is designed for deep, high-pressure, typically offshore operations, not the shallow, low-pressure resource that his company seeks to develop. He said regulations designed for highly directional, high-pressure wells drilled from offshore platforms and drill sites on the North Slope make no sense for these "modified water wells." He likened it to regulating a pickup truck with rules designed to regulate an 18-wheeler. He further said:

I believe this technology and resource hold tremendous promise for Alaska, both in terms of its potential

and, ... I believe, our ability to extract it. Once established, it can provide an inexpensive and safe method of powering rural Native villages, as well as serving the larger Anchorage and Mat-Su Valley communities. This would obviate the need ... for transporting expensive fuels by hazardous means to Alaska's remote citizens, and would also do quite a bit to help the declines in the Cook Inlet that we've all been seeing over the last few years, which is natural, since these fields have been online for 30, 40 years or more.

Number 1494

MR. SEXTON concluded by offering his view that HB 69 would ensure that the AOGCC and its professional staff have the authority and discretion necessary "to regulate projects like ours" in an appropriate manner that is suited specifically to the nature and characteristics of shallow natural gas development projects, and yet still maintains "the protections for human and wildlife safety and the environmental concerns that are important to all of us."

Number 1534

CHAIR KOHRING noted that one well drilled by the company is down the street from where he lives. He expressed excitement about the potential this kind of drilling represents, and said he would like to see other companies do likewise.

REPRESENTATIVE ROKEBERG asked whether anyone from AOGCC was available to testify.

CHAIR KOHRING said no, although Mark Myers [director of the Division of Oil & Gas] was available to answer questions. He said two [AOGCC] commissioners had hoped to be available but were making a presentation before [the House Finance Committee].

Number 1621

REPRESENTATIVE ROKEBERG returned to the issue of amending the bill. He referred to the legal opinion [dated January 29, 2003] from Jack Chenoweth, Assistant Revisor of Statutes [in committee packets], which he said indicated that the original bill, before that day's amendment, allows a grant of authority by the commission to professional staff. He questioned whether the committee was doing the right thing [by amending the bill].

REPRESENTATIVE FATE indicated that if [allowing the staff to act, which Amendment 1 deleted] is what [AOGCC] would like, the amendment should be reconsidered. He concurred with the need to hear from AOGCC.

REPRESENTATIVE ROKEBERG suggested that nothing prohibits the commission from granting authority to the staff, even with the deletion [in Amendment 1]. He deferred to Representative Kerttula, noting her legal background.

Number 1734

REPRESENTATIVE KERTTULA explained that normally variances are done by delegation to staff, because it is a de minimis thing. Noting that if the references to staff are removed from the bill, the committee could say it doesn't want to foreclose the commission's ability to do this, she proposed the need to clear up exactly what is intended.

REPRESENTATIVE ROKEBERG suggested it would be helpful to find out exactly how [AOGCC operates] and what the commission prefers so that the language doesn't go counter to the commission's current methods of operation or legal requirements.

CHAIR KOHRING noted that lawyers had worked with various folks including Mr. Chenoweth in crafting this legislation, and that there may be a valid reason to have [staff included].

Number 1826

REPRESENTATIVE ROKEBERG indicated to Mr. Sexton that his biggest concern is whether HB 69 will be helpful enough to the company, rather than taking a more detailed look at the regulatory regime; he inquired about that. Emphasizing that Alaska's regulatory design is based on larger, more traditional, deep-hole operations, Representative Rokeberg noted that he was a sponsor of the original legislation and is very sensitive to the company's ability to operate.

MR. SEXTON thanked Representative Rokeberg for that far-sighted question. He responded:

We're really not trying to change, wholesale, the regulatory environment in Alaska. I think the regulators do a good job, but I think they have been hamstrung because of regulations that were designed

for a very different type of drilling, ... and for good reason. And I believe that by giving the regulatory agencies the discretion they need, ... and not simply have to follow cookbook and textbook rules that were written in a very different environment, with a very different mindset, we believe that we can work with the regulators if they have the discretion, because we think they do understand the differences.

Number 1951

MR. SEXTON continued:

I guess our answer is, we'd like to try it this way. We'd like to try working with the regulators, show what a good job we can do, and if for some reason it's not enough, I will be reminded that you made this comment, and I will wish that ... I had listened more carefully to your words. But ... at this time the spirit of this is that we can all get along and work together as long as we give the regulators the discretion ... to apply what makes sense to this particular type of project.

One example I could give you is, ... when we went back into a water-disposal well, we had to use equipment and had to obtain equipment that I haven't seen ... in 20 years, since I ... served on platforms offshore operated by Amoco, and I saw equipment that I have never seen ... in the Raton basin in Colorado, but we had to use it: blowout-prevention stacks and those huge, 10,000-pound-rated manifold of pipes and valves that was, quite honestly, unnecessary, but those were what the regulations specifically required, and the regulators were not able to apply their discretion.

So, ... I guess our answer is, we'd like to try and work with ... the regulators, as long as they have that discretion, and if it is not enough, I'll say, "Mea culpa," and we'll be back asking for something additional.

Number 2039

REPRESENTATIVE ROKEBERG thanked Mr. Sexton for the candid answer; he indicated the legislature would watch the situation.

REPRESENTATIVE KERTTULA thanked Mr. Sexton and his staff for getting to know members personally and providing information up front. Noting that she'd talked to [Evergreen Resources'] Alaskan staff that afternoon, she offered her understanding that what triggers this request for a variance is an undue delay. She asked what Mr. Sexton considers an undue delay, and how long these kinds of projects normally last in Colorado.

MR. SEXTON replied that Colorado certainly isn't without its own extensive regulatory rules and practices, but that a well can be permitted within a 90-day process, even given all potential objections; that certainly cannot happen in the current environment in Alaska. For example, when John Tanigawa prepared permits to drill eight wells [in Alaska], it took enough paperwork to drill eighty wells in Colorado, and the wells were drilled six months later than planned. Mr. Sexton said the company's attitude was to show willingness to work within the rules, but remarked:

We're here to tell you candidly that we can't get our job done with the existing structure. We simply cannot gear up and drill what we would like to be able to drill; we would probably be able to drill 10 or 20 wells a year, but if you would like to see us slowly build that level to 40 wells, 60 wells, 80 wells, 100 wells - as we have done in the Raton basin in Colorado, [where] ... we're up to 160 wells planned this year - we could never attempt to do that in Alaska under the existing regulatory environment.

Number 2228

REPRESENTATIVE KERTTULA remarked that other variances with which she is familiar are from "the other resource agencies," and usually are for small and insignificant projects. She noted that [under the bill], to her reading, there wouldn't be any size restriction because a single field could be very large in acreage. She asked: Will there be any public notice given, or conceivably could there be a very large project that has no public notice?

MR. SEXTON responded:

Well, that's an interesting question in that, I believe, we have already given public notice. If there is anyone in the state that John Tanigawa hasn't met, it would be surprise to me. But ... I think

everyone is aware of what we're trying to do. ... I think one of the things we're particularly proud of is that you can drive through the middle of our field ... in southern Colorado - an area with quite a bit of topography and hills - and not see the field. You don't even realize you're in the middle of it. That would be even easier to accomplish ... in Alaska, ... given the terrain and the topography, and it being fairly flat, and our ability to use trees ... and natural cover, which ... we intend to do.

As far as the public notice, we are required to notify landowners when we drill, and we expect to continue to notify landowners.

Number 2308

REPRESENTATIVE KERTTULA surmised that a requirement of notification to landowners wouldn't be wiped out by this [legislation]. She said her fundamental concern is to ensure that there is some notice.

MR. SEXTON deferred to Mr. Tanigawa for more specific comments.

REPRESENTATIVE KERTTULA explained her concern, that the mineral subsurface is still owned by the state and technically the state - not the person whose property it could be on - is making the deal. She asked whether that is correct.

Number 2353

JOHN TANIGAWA, Alaska Projects Manager, Evergreen Resources Alaska, concurred. He pointed out that the Department of Natural Resources (DNR) has several public-notice provisions for anything that impacts the landowner. [This legislation] refers to something specific such as an exception for something engineering-based. The desire is to be able to accomplish such exceptions relatively easily. Mr. Tanigawa also pointed out that the domain of these exceptions is in the purview of the AOGCC, which is basically how oil and gas wells are operated.

REPRESENTATIVE ROKEBERG said he shares Representative Kerttula's concerns with regard to proper notification of the public. He related his belief that this legislation doesn't change any notice provisions. He asked if there is notification when establishing a unit in which to operate.

MR. TANIGAWA answered in the affirmative.

REPRESENTATIVE ROKEBERG pointed out that generally the primary notice provisions would take place during the unitization hearing, which would alert all landowners to the activity. That would be followed by notification that the pad would be established and [drilling would be done].

MR. TANIGAWA affirmed that.

Number 2445

CHAIR KOHRING noted the arrival of Dan Seamount and Cammy Taylor from the Alaska Oil and Gas Conservation Commission (AOGCC). Chair Kohring pointed out that passage of this bill provides AOGCC with a tool that allows them to better work with the industry and speed the process of issuing permits. He directed attention to page 1, line 14, and asked Mr. Seamount and Ms. Taylor if it's appropriate to strike the language referring to giving authority to "professional staff" to make decisions on granting variances. He asked whether decisions regarding granting variances should be left to the [AOGCC] commission members only.

REPRESENTATIVE ROKEBERG pointed out that [similar] language also occurs on page 2, line 4, and page 2, lines 8-9.

The committee took an at-ease from 3:58 p.m. to 4:01 p.m.

Number 2568

CAMILLE OECHSLI TAYLOR, Chair, Alaska Oil and Gas Conservation Commission, explained that currently AOGCC has a regulatory scheme in which an operator on short notice [may] receive oral approval from the commission. In practice, that has been one of two petroleum engineers who share on-call duties for operations that are ongoing, after hours, and during the weekend. Furthermore, the regulation requires the operator to submit the formal paperwork for commission approval by the following day.

MS. TAYLOR said the commission has a tremendously professional and competent technical staff. Currently, when there is an ongoing situation, the [professionals] have kept the commissioners abreast of what is going on. She explained, "It allows for the opportunity for someone who is out there conducting an operation that, but for time, would cost a lot of money for someone waiting for office hours to open and for all

three commissioners to be together." Therefore, she said she reads the bill as allowing the designation to be by the commissioners and that the commissioners would have the decision-making authority.

CHAIR KOHRING asked if the language "designated" on page 1, line 10, should carry through the entire legislation.

REPRESENTATIVE FATE said he would like that.

Number 2707

REPRESENTATIVE ROKEBERG moved that the committee rescind its action in adopting Amendment 1. There being no objection, it was so ordered.

CHAIR KOHRING asked if the committee wanted to insert the language "designated" [page 1, line 14, page 2, line 4, and page 2, lines 8 and 9] so that any professional staff member would be allowed to make a decision on variances if so designated by the commission.

REPRESENTATIVE ROKEBERG responded that he thought it would be redundant and unnecessary. He then noted that the committee's intention is that they all be designated.

CHAIR KOHRING inquired as to the will of the committee. He then announced his understanding that the committee wished to leave the bill as it is.

Number 2802

REPRESENTATIVE FATE stated that he was fine with it as long as the record reflects [the intent], and so that it "doesn't come back and haunt us" that some professional staff makes a wrong decision and then the public says the job wasn't done properly. Representative Fate added, "Just so the record is clear that you [AOGCC] have the authority to commission any professional staff to make those decisions, I'm happy with it."

REPRESENTATIVE ROKEBERG inquired as to AOGCC's procedure when those [professionals] are designated.

MS. TAYLOR answered that it has been relatively informal. Therefore, having something that specifies the process is important.

REPRESENTATIVE ROKEBERG pointed out that this section requires that AOGCC designate, presumably, a member of staff. Therefore, a more formal action is implied.

CHAIR KOHRING said that was related to his question regarding whether that would carry forward throughout the bill.

Number 2889

REPRESENTATIVE KERTTULA inquired as to the public notice that will be required when variances are granted, and what will be in place for these fields.

MS. TAYLOR responded that generally AOGCC's practice is to provide for the exception for technical issues right in the language of the regulation. The original legislation - the conservation Act - requires AOGCC to issue permits promptly if they comply with all of the regulations. Therefore, the goal of AOGCC has been to clearly articulate the requirements so that operators understand what is required and it is fairly smooth for the approval process. The regulation itself actually articulates the standard for obtaining a variance, and the language of the regulation basically parallels that in this legislation, which says that "there is an equally effective means of accomplishing the same or demonstration that the risk it would have required that particular standard for doesn't exist."

MS. TAYLOR noted that the regulations contain a few areas in which that provision wasn't included, because at the time of drafting there may not have been a need for it due to the technology available. She pointed out that a generic regulation addresses drilling and well-control exceptions for new technology. [Not on tape, but taken from the Gavel to Gavel recording on the Internet, was that the exception didn't go so far as to capture Mr. Tanigawa's example of gas-detection equipment, for instance. Ms. Taylor said some of that can be fixed with this same standard. She added, "I'm not sure if this was intended to apply as an exception where other parties' - other owners' - interests might be impacted. That was not the way we read it." She asked that the committee explain it if that weren't the case, and mentioned that an exception relating to an external boundary might need it, however.]

TAPE 03-3, SIDE B

Number 2980

REPRESENTATIVE KERTTULA surmised, then, that there has already been a public notice and the landowner already knows that this activity is ongoing; therefore, this is an exemption for a variance for something technical that really isn't going to impact the overall operation. She said all she wanted to know was that those who are being effected have some notice early on.

MS. TAYLOR related her understanding that the types of variances being discussed [in HB 69] are technical conservation issues and waivers from general statewide standards - not for those regulations impacting other owners, which would require notice.

Number 2897

REPRESENTATIVE ROKEBERG asked if this legislation goes far enough in overcoming the problems that have developed vis-à-vis the administrative regulations for shallow gas operations versus more typical commercial drilling operations. He asked if the bill provides enough tools for AOGCC to make those distinctions.

MS. TAYLOR mentioned that [AOGCC] just learned of this legislation at the end of last week and hasn't had time to address some other issues. However, AOGCC holds the position with respect to all oil and gas drilling in the state that the commission's regulations should be directly tied to the risk that it's trying to manage, she related. There shouldn't be a requirement that doesn't directly relate to what AOGCC is trying to accomplish. Therefore, the approach in [HB 69] mirrors what AOGCC generally attempts to do. However, she acknowledged that AOGCC's regulations have historically been aimed at conventional oil and gas drilling. "To the extent that we're aware of the problems that have been raised or pointed out to us, we think that this accomplishes that," she added.

Number 2822

REPRESENTATIVE FATE suggested putting the staff issue to rest. He turned attention to AS 31.05.023(a), "The commission shall employ such staff as it considers necessary to carry out its responsibilities" and decisions as may be delegated. He said that takes care of it.

CHAIR KOHRING closed the public hearing.

Number 2767

REPRESENTATIVE FATE moved to report HB 69 out of committee with individual recommendations and the accompanying zero fiscal note(s). There being no objection, HB 69 was reported from the House Special Committee on Oil and Gas.

HB 16-STRANDED GAS DEVELOPMENT ACT AMENDMENTS

CHAIR KOHRING announced that the final order of business would be HOUSE BILL NO. 16, "An Act amending the standards applicable to determining whether, for purposes of the Alaska Stranded Gas Development Act, a proposed new investment constitutes a qualified project, and repealing the deadline for applications relating to the development of contracts for payments in lieu of taxes and for royalty adjustments that may be submitted for consideration under that Act; and providing for an effective date."

Number 2728

REPRESENTATIVE McGUIRE moved to adopt Version 23-LS0101\H, Chenoweth, 2/6/03, as the work draft. There being no objection, Version H was before the committee.

Number 2711

REPRESENTATIVE FATE, sponsor of HB 16, explained that the bill is a reauthorization of the Alaska Stranded Gas Development Act {"the Act"} with amendments. The purpose of the Act is to allow negotiations between producers and the State of Alaska. The legislation proposes new language for what is a qualified project. It allows all forms of natural gas through the pipeline, including gas-to-liquids (GTLs), liquefied natural gas (LNG), and natural gas; the Act, by contrast, allowed just LNG, to his recollection. It isn't route-specific, he noted, since a lot of bills and resolutions from the previous legislature dealt with that subject. Most important, he said, it repeals the deadline for application. He told members that even though the previous version allowed for other investors, the bill specifies that Alaskan businesses or corporations can "go into this pipeline with equity up to 10 percent" [of the estimated cost of constructing a qualified project], and it allows generically for the market to be either domestic or foreign.

Number 2580

REPRESENTATIVE ROKEBERG recalled working on the Alaska Stranded Gas Development Act several years ago in the House Special

Committee on Oil and Gas, and that one bone of contention was what type of product it would cover and the prohibition of GTLs by the Act. Alluding to Section 2 of Version H, he asked Representative Fate about his intention on contract development with regard to Alaska-based businesses, as well as the rationale behind having equity not exceed 10 percent.

REPRESENTATIVE FATE responded that the provision for Alaskan business interests is to encourage Alaskan businesses with the capability and which can become qualified to enter into this. Nothing would prevent a corporation that can qualify from participating, he said, whether it is a Native corporation, a combination of Native corporations, or a combination of Alaska-based banks. With regard to the 10 percent, he said it is not just a negotiating tool, but is simply because he surmises that the producers don't want to exclude anyone but don't want to dilute their ownership to the extent that it becomes unprofitable and inhibits construction of a pipeline.

Number 2445

REPRESENTATIVE ROKEBERG acknowledged the need to hear from witnesses, but said he interpreted that [limit of 10 percent] as restricting the pipe size and companies' ability to participate. He offered his understanding that nothing in the [Act] restricts any Alaska-based company from participating; therefore, the [new] language is redundant and just says such a company couldn't have more than 10 percent of the equity. He asked whether that was Representative Fate's intention.

REPRESENTATIVE FATE answered, "It was the intent to encourage, ... so that there's not too big of ... participation you might see by somebody of the Alaskan -- unless, of course, they can -- you're right: maybe they can come in with more than 10 percent. Maybe they can take all the risk."

REPRESENTATIVE ROKEBERG asked whether, then, [BP Exploration (Alaska) Inc.], an Alaska-based company, could only invest 10 percent.

REPRESENTATIVE FATE agreed with Representative Rokeberg's observation about redundancy, but said he wanted to make it clear that Alaskan businesses can invest in this if they qualify.

Number 2355

CHAIR KOHRING pointed out that part of the Act, AS 43.82.110, stipulates the conditions under any group can be considered a candidate for potential ownership in the gas pipeline. He said he, too, wondered about adding that 10 percent provision.

REPRESENTATIVE FATE again acknowledged the redundancy and said the provision is to encourage Alaskans to participate.

Number 2299

CHAIR KOHRING referred to the fact that [the existing language of the Act set forth in Section 2 of Version H] says the commissioner may develop a contract that includes [various terms, including the new terms of paragraph (5) that discuss Alaska-based corporations or businesses and the 10 percent provision]. He expressed concern that it seems to give the commissioner authority to make those decisions when the owners of the pipeline may not concur with the commissioner's decision.

REPRESENTATIVE FATE responded that at one time he'd planned to take it out, but had decided to leave it in, because it might be a stimulus to help propel the pipeline forward, and because it gives a clear point to start from for negotiating with regard to either an Alaska-based business or even the financiers of the pipeline. "And we've labored long and hard with the staff and other people from the industry to discuss this," he remarked. He concluded, "We'll wait and see at the end of the day ... what we will do with that 10 percent."

Number 2203

REPRESENTATIVE KERTTULA noted that the original Act was to encourage development of North Slope gas and to add a timeline for development. With Version H, however, it appears to be "all gas, anywhere at any time." She questioned whether that broadness is intended, with no expiration date and no sidebars on where [the gas] goes or where it's from.

REPRESENTATIVE FATE agreed that it is broad and leaves the route and types of natural gas open-ended, which he said is intended to stimulate development of the gas pipeline in a more rapid fashion.

Number 2028

REPRESENTATIVE KERTTULA questioned the incentive if there is no expiration date. She expressed concern about when this would

have to occur and what the incentive really would be. She observed that the royalty [may be included in the contract in the Act, Section 2 of Version H] and suggested that may be the only incentive.

Number 2008

REPRESENTATIVE ROKEBERG referred to subparagraph (C) on page 2 [Section 1 of Version H], noting that it mentions "any other technology", which Representative Fate had said may apply to GTLs. Representative Rokeberg recalled the argument in 1998 [when the Act was passed] that it should be restricted because it is a disincentive to build a gas line. He said the bill really opens up that debate, which may be the proper one to have again because of technological changes and other considerations. He requested testimony from witnesses about that.

Number 1928

REPRESENTATIVE CRAWFORD referred to Representative Kerttula's question and said it seems [Version H] is worded so that it could apply to even a very small project, rather than relating to just a gas pipeline from the North Slope. He asked whether that is the intent.

[Representative Fate responded by saying the intent is "to latitude 64 North." He later corrected his statement because the original version of HB 16, not Version H, referred to "the area of the state lying north of 64 degrees North latitude".]

Number 1809

ROGER MARKS, Petroleum Economist, Economic Research Section, Tax Division, Department of Revenue, noted that he'd worked on the Act in 1998 and therefore had some familiarity with its history, intent, and mechanics. He pointed out that the department had provided a three-page overview [in addition to the analysis] as part of its fiscal note [for HB 16].

REPRESENTATIVE ROKEBERG observed that [the fiscal note] is about half a million dollars.

Number 1693

REPRESENTATIVE KERTTULA asked Mr. Marks whether the department had looked at possible loss to the state in terms of royalties. She also asked that he discuss the original intent of the Act.

MR. MARKS, who was participating via teleconference, said he hadn't heard the first question and so began addressing the history. He explained that in 1997 the legislature passed HB 250, which established a North Slope gas commercialization team in the administration to research and recommend changes to the state law to encourage commercialization of North Slope gas; under HB 250, the administration was supposed to issue a report to the governor by February of 1998. That team did the research and concluded that the North Slope gas commercialization project faced considerable risks. Because of the size of the project needed to make the gas commercial, there were big cost risks and gas-price risks to the sponsors.

MR. MARKS told members that, in addition, "we" concluded that the state's fiscal system actually exacerbated those risks because of three general characteristics. The first was uncertainty: a very high-cost project with marginal economics could be feasible under a certain fiscal system and built under that system, but that system could be changed by statute, which would suddenly make the project not feasible after it was built.

MR. MARKS explained the second risk, the so-called regressive tax system for production tax and royalties. When profits are high, [the state] gets a small share of the profits; when profits are low, it gets a large share. That exacerbates the low-price risk to sponsors, he said, because making large payments to the state when prices are low could increase the possibility of losing money or not recovering their investment.

MR. MARKS discussed the third risk. The property tax is payable once construction starts, which could be years before revenue is generated. On a "time value of money" [basis], it lowers the sponsors' rate of return and increases the probability that they won't be able to recover their investment.

Number 1452

MR. MARKS told members that after the team issued its report to the governor, it worked with the major Prudhoe Bay producers to develop legislation to deal with those risks. The result was HB 393, which ultimately became the Alaska Stranded Gas Development Act, AS 43.82. In general, the law provided a mechanism for converting the state's fiscal system from a statutory basis to a contractual basis, which provides for greater fiscal certainty. The fiscal system would be negotiated between the administration and the project sponsors; possibly as

part of the terms of the negotiation, a less regressive fiscal system could be put in place. Mr. Marks noted another problem with a regressive system: at high prices, the state probably gets less money than it could.

Number 1362

MR. MARKS discussed the general mechanics of the process. A sponsor would submit a project plan and application to the administration; if acceptable under the terms of the Act, the administration would then begin negotiating the fiscal terms with the sponsor. Noting that under the Act all tax provisions in the current statutes would be on the table, Mr. Marks explained that because the royalty represents the state's ownership interests, it was the judgment of the administration that the state should keep the one-eighth - which is 12.5 percent - royalty rate for Prudhoe Bay gas, but that some royalty provisions could be negotiated, namely, the timing for taking royalty-in-kind (RIK) or royalty-in-value (RIV)] gas and the provisions for establishing the valuation method for the royalty.

MR. MARKS explained that once a contract was negotiated, preliminary findings would be submitted to the governor; if the governor chose to proceed, those findings would be given to the legislature and the public for a 30-day review period. After that, the commissioner of revenue would modify the contractual terms as appropriate, and if acceptable to the sponsor; a final contract would be submitted to the governor; the governor would transmit the contract to the legislature with the request for authorization to execute the contract; and the legislature would vote on it.

MR. MARKS addressed other provisions. Calling the property tax the bread and butter for municipalities, he explained that municipalities were concerned about their interests' not being represented in a negotiation. As part of the Act, therefore, a municipal advisory group was set up to participate in developing the contract terms. In addition, there are provisions in the Act for making gas available to communities; for local hire; and for dealing with confidential information provided by the sponsors.

Number 1208

MR. MARKS also pointed out that there was a question of the constitutionality of the Act as a whole, and whether this

switching to a contract [basis] by one legislature is binding a future legislature. Noting that Article IX [Section 1] of the state constitution says that the power of taxation shall never be surrendered, suspended, or contracted away, Mr. Marks reported that it was the Department of Law's judgment that [the Act] was constitutional because it was simply putting fiscal terms into a contractual form. Certainly, he said, a future legislature would be able to add tax terms after the contract was in place, but the contract itself would be "a solemn pledge or a moral commitment by the state that once it agrees to this contract, it would not change it." Likening it to "a message to the future from one legislature to another," Mr. Marks said it was the administration's position that it wasn't airtight but was "a strong moral message."

Number 1101

MR. MARKS informed the committee that the Department of Revenue generally supports HB 16. He added that possibly the administration would submit some amendments, although he wasn't aware of what they would be.

Number 1070

MR. MARKS, in response to a question from Representative Rokeberg, said he'd only had [Version H] for about one-half hour and hadn't had time to study it.

REPRESENTATIVE ROKEBERG referred to [Section 1], the proposed amendments to AS 43.82.100 under the heading "Qualified project." He asked whether the new language in subparagraphs (A), (B), and (C) would affect the department's fiscal note.

MR. MARKS said he didn't believe so.

Number 1023

REPRESENTATIVE KERTTULA offered her understanding that part of the intent with the Act was to "try to get the gas going." She asked Mr. Marks whether the lack of an expiration date [in the bill] could actually result in some discouragement, and whether he'd ever looked at the economic picture in terms of whether having an expiration date would provide motivation.

MR. MARKS said [the department] hadn't looked at that question.

Number 0955

REPRESENTATIVE KERTTULA referred to the regressive nature of the tax. She asked Mr. Marks whether [the department] has looked at shifting that tax so that when the return is high, the tax is high, and when the return is low, the state would "shift around."

MR. MARKS said that is exactly what was envisioned to be shifted to. He added, "That's what we call a progressive system, ... which, again, reduces the risk of low prices to the sponsors and gives the state the opportunity to make more money when prices are high."

Number 0917

REPRESENTATIVE KERTTULA asked whether that is what it is envisioned that the commissioner would negotiate for in the contract.

MR. MARKS noted that eight principles to strive for in the Act are listed in existing AS 43.82.210(b). Calling it a blend, he said some of those "sort of counter each other," but that one principle - which is one direction negotiation would take - is that all things being equal, a progressive system is better than a regressive one.

Number 0793

JOE MARUSHACK, Vice President, Alaska North Slope Gas Commercialization, ConocoPhillips Alaska, testified that his company is working hard to commercialize Alaska North Slope (ANS) gas through development of a gas pipeline from Alaska through Canada to the Lower 48. Urging passage of HB 16, he said it is needed so that ConocoPhillips Alaska and others may initiate formal discussions with the state, leading to a fiscal agreement on commercialization for ANS gas.

MR. MARUSHACK reported that ConocoPhillips Alaska has pursued a clear strategy to commercialize ANS gas for more than a year and a half, including federal enabling legislation to provide a more timely and certain U.S. permitting and regulatory framework; federal fiscal legislation that would mitigate the risk of unexpectedly low gas prices; and state fiscal legislation like HB 16 that provides a mechanism for his company, the state, and others to address issues regarding how the gas will be valued, how it will be taxed, how local impacts will be addressed, and how development costs will be treated.

MR. MARUSHACK said that since at least 1973, Alaskans and companies they work for have labored to overcome significant challenges in bringing Alaskan gas to the market. He cited challenges of the natural environment such as terrain, climate, elevation changes, and seasonal construction limits; technical challenges that have required use of new materials and equipment specifically constructed for this project; and the nature of this commodity, with price uncertainty and volatility being at odds with the huge investment and long-term fiscal commitments required. On the other hand, he said, Alaskans have a huge opportunity for additional jobs in construction and operation of the pipeline, and the state treasury has the prospect of a significant new revenue stream, funds for additional services. Suggesting the state's communities have an opportunity to share in the creation of new wealth, he told members:

The project can become a reality, and the time to move forward together is now. Passage of HB 16 is the first step that the Alaskan government could take towards addressing necessary legislation to move the gas pipeline project forward. However, I ask caution regarding any new amendments or modifications that may have unintended consequences and cause further delays. We need a clean bill that opens up the stranded gas Act process, not one that adds challenges. In closing, ConocoPhillips asks that you pass this legislation.

MR. MARUSHACK requested clarification as to whether the committee was addressing HB 16 or [Version H], but said he was prepared to discuss either.

CHAIR KOHRING clarified that before the committee was Version H.

Number 0531

REPRESENTATIVE CHENAULT asked Mr. Marushack for his thoughts on Version H and whether it helps or hinders the project.

MR. MARUSHACK answered that he hadn't studied it in great detail, having received it a few minutes before the hearing, but that it appears to generally work - and provide what his company needs it for - by removing the [application deadline] date and opening up the Act so it addresses a natural gas pipeline. However, he expressed concern that Section 2 may be somewhat contrary to commercial negotiations. He said it seems the state

shouldn't dictate who the parties holding an equity interest in a commercial contract would be. The (indisc.) and the Act already contemplate that any company can participate if it brings value to the table. He added:

Any party that brings value to the table is a party that the companies can probably work with and negotiate with. I also wouldn't see that it makes sense ... for anybody who can create value to be limited to 1 percent, 10 percent, 50 percent. But those are commercial negotiations. ... We've had some discussions with certain individuals like this, and we always give the same message: If there's true value there, we'll probably going to be able to ... bring that to the table. If there's really not true value there, we hate to see activities that would make the negotiations - and have unintended consequences - delay this project ... even further.

Number 0381

REPRESENTATIVE MCGUIRE asked whether there is any harm in keeping [Section 2] in there, though.

MR. MARUSHACK acknowledged that his interpretation may be wrong, but said it appears that individuals may be looking for a commercial advantage through the legislative process. "And we don't think that's helpful at all," he remarked. He indicated, however, that if it lowers the cost and creates a more viable project, then it creates incremental value and is "a negotiation that generally leads to success."

Number 0325

REPRESENTATIVE ROKEBERG asked whether ConocoPhillips is an Alaska-based company.

MR. MARUSHACK answered that Phillips Petroleum Company [which merged with Conoco Inc. in 2002] was a Delaware corporation with "branches, if you will," in various areas including Alaska. "Whether that constitutes an Alaskan company per se, I don't know for sure," he added. "I consider myself to be an Alaskan, but hopefully ... I would not have my ownership interest limited one way or another if I wanted to do this project."

REPRESENTATIVE ROKEBERG remarked that one corporate predecessor of ConocoPhillips was ARCO Alaska, Inc., which at least should

have had an Alaskan business license. Deeming Mr. Marushack to be an expert on it, Representative Rokeberg then asked whether he believes it would be helpful or necessary for the bill to include a provision "allowed by special Act of Congress allowing the Alaska railroad to issue IDB [Industrial Development Bonds]," which he suggested may be applicable to this project.

MR. MARUSHACK answered that for the bonding potential which he believed Representative Rokeberg was talking about, if it went through an Internal Revenue Service (IRS) test and truly passed all the requirements so that people lending money to the project could see that it actually would have a tax-exempt-bond basis, then it absolutely would provide incremental value. To the extent that the strength of the federal government is behind the financing - which he said he understands that the bonds may be able to do - the interest rate could be reduced; that would reduce the tariff, raise the wellhead value, and increase royalties. Mr. Marushack pointed out that he couldn't say whether that particular mechanism would pass an IRS test, and emphasized the need to get an IRS ruling that would allow the people lending money to this [project] to have enough assurance that they would lend under those sorts of terms.

Number 0050

REPRESENTATIVE ROKEBERG indicated there possibly could be 200 basis points as a reduced interest rate. He suggested that a IRS ruling may provide further protection, particularly if related specifically to the project by including it in the Act.

TAPE 03-4, SIDE A

Number 0001

MR. MARUSHACK related [his company's] analysis that it would be perhaps more like 100 basis points. Regardless, he said, if the interest rate really were reduced, it would create incremental value. He also offered the belief that financing doesn't make a bad project good; rather, it is used to make a good project better and actually get it off the ground. "So we would look at this ... on an unfinanced basis to begin with, assuming you had full equity interest in this, and then, if that passed all the tests, so you ... thought you could actually sell that to the financial community, then you'd do that and hopefully make a more economic project at that point in time," he concluded.

REPRESENTATIVE ROKEBERG suggested that this is known to be a good project, but just needs to pencil out.

Number 0121

REPRESENTATIVE FATE asked, if there were a "mix and match" of financial ratings on this project, how the investment bankers would look at it.

MR. MARUSHACK replied:

This happens all the time, and it depends on ... how you want to structure this - whether it's project financed, whether it's financed by the absolute balance sheet of the companies. I don't think we're at a point yet where we know the answer to that, ... and we don't even know who would own this pipeline yet.

Currently, ... or at least last year, we were working with BP and ExxonMobil Corporation, ConocoPhillips; those companies have very strong balance sheets and could get relatively good financing rates. But how that would all blend together, I think, is one of the things that needs to be worked out, which is actually something that I think needs to happen in HB 16.

I believe that one of the real advantages to ... your bill is that it's going to allow people from the state and people from the producers to sit around ... the table for a long period of time and talk about issues just like this: What does financing do to this project? Can you get financing? What if the state needs something that is in conflict with what the financial people think they need to see?

There's a myriad of issues, which is why I think this bill is important to get passed right now, because I don't actually see us getting through this real quickly. I hope we do, but I think it's going to be very complicated and take a lot of work from the state and the producers, and a lot of sharing of information, probably bringing in experts. It's just a very complicated project. There's nothing like it on earth.

Number 0276

REPRESENTATIVE CRAWFORD asked, since this bill apparently opens it up to any project at any time, whether Mr. Marushack sees that as keeping it a clean bill or whether it adds hurdles.

MR. MARUSHACK replied:

Clearly, ConocoPhillips is focused on a Lower 48 pipeline. We've put a lot of time and effort into that. And if this bill passes, we are going to come forward and ask to qualify, and want to negotiate on a Lower 48 pipeline using ANS gas ... as the product for that. But I have no problem with opening this up to other opportunities For instance, ... I'm not sure this works for Evergreen [Resources], but I hope Evergreen is tremendously successful, and if there's other opportunities out there, I think that's a good thing.

I don't know if this is where you're heading or not: there's clearly a problem we face in Washington [D.C.] with the concept of competing projects - a lot of confusion about ... what does Alaska really want, do they really want a Lower 48 pipeline, do they want something else. And ... my message is always, "I think this is about the only project that works right now, and we should absolutely focus on that." But ... I'm not recommending that we limit utilization of this to a Lower 48 pipeline right now. I don't think that's necessary.

Number 0452

KEN KONRAD, Senior Vice President, BP Exploration (Alaska) Inc., noting that he is the company's vice president for gas, offered the following testimony:

Significant time, effort, and money has been dedicated to develop a viable gas pipeline project to commercialize Alaska's enormous gas resource. Through 2002 and continuing into this year, BP has undertaken further technology-and-design optimization work on the project in an effort to reduce the cost of this \$20-billion project. We're working closely with state, federal, and Canadian agency staff around advanced materials and design, and are inviting them to witness key tests BP will be undertaking this year to validate much of the work we've done. Results to date are very

encouraging. However, technical work alone will not be sufficient to make an Alaska gas pipeline a reality.

Before a project can advance to the next stage, three key government actions are needed: a clear and predictable regulatory process with the Canadian government and First Nations, a clear and predictable state fiscal framework around gas in Alaska, and the passage of important U.S. federal legislation. While success is needed on all three fronts, the one thing Alaska itself can do to advance an Alaska gas pipeline is to sit down and work with industry to develop a fiscal framework for gas that provides confidence that the rules of the game won't change later. Achieving this mutually agreed framework will also send a powerful signal to Washington, D.C., that Alaska is indeed ready to see ... a gas pipeline project advance.

Number 0602

MR. KONRAD continued:

We're very encouraged that our new governor has already spoken to his desire to advance the development of a predictable fiscal framework for gas, and are similarly encouraged that the new legislature appears ready to support advancing this important agenda. ... Reauthorizing the stranded gas Act via House Bill 16 is a good idea. We supported the original stranded gas Act when it was debated and continue to do so. House Bill 16 can provide a framework that supports negotiation toward a clear and predictable fiscal regime in Alaska, and as such, will help support forward progress on gas commercialization.

But we don't necessarily need to wait on passage of this bill to begin engaging on the topic. Dialog with a small, experienced, informed, and empowered negotiating team made up of representatives of the state and the producers can commence anytime. Under any circumstance, any agreements worked with the state will require legislative review and approval.

We do believe that if HB 16 advances, it's important that the bill retains its focus and simplicity as it moves through the legislative process. Otherwise, there's potential failure in the event the bill becomes overburdened with extraneous provisions.

Number 0717

MR. KONRAD informed members that he'd just received Version H one-half hour earlier and hadn't had a chance to review it. He said it appears to be "reasonably clean," although he said he'd want to look at the ownership provision more closely to make sure it doesn't inadvertently restrict his company's ability to retain an interest in the project.

MR. KONRAD reiterated that the one thing the state can do to help move a gas line forward is to take tangible steps towards achieving fiscal certainty. "That, combined with U.S. federal legislation and continued regulatory progress in Canada, will allow Alaska to realize the extraordinary opportunities for jobs, revenue, and economic stability, as the gas pipeline can offer for decades and decades to come," he told members. He concluded by saying that "BP stands ready to work productively with the state towards a clear and predictable fiscal regime."

Number 0809

REPRESENTATIVE ROKEBERG inquired about the political situation with regard to "the First Nations issue" in Canada as well as the current position in Ottawa on granting permits and going forward on this project.

MR. KONRAD replied that [his company] continues to have a number of "fairly productive" conversations with both the First Nations people and the Canadian regulators, who "have tabled a concept that we believe can work ... to come up with ... a simple, single regulatory process." He said there is still a little ways to go in terms of actually formalizing that. Mr. Konrad told members that he believes things are encouraging, although clearly the big focus right now in Canada is ensuring tangible progress on the Mackenzie Valley project. He expressed support for that, offering his belief that the two projects are complementary and will sequence naturally, and said the North American market can "certainly use all the gas it can get." He added, "Every indication is that they will be supportive of our project once we get some of these other key government actions in place."

Number 0931

REPRESENTATIVE ROKEBERG asked whether the [Canadian] federal government is actually "in the way" and whether his company is actually able to negotiate with them now.

MR. KONRAD answered that he doesn't think they're standing in the way at all. He said a number of ideas have been tabled, but in general there is concurrence. He added, "However, like everyone else, they have finite resources; they're focused right now on the Mackenzie Valley project. But we certainly have expectations ... that during this year we'll have had tangible ... and complete progress in the regulatory arena."

REPRESENTATIVE ROKEBERG offered his understanding that many sellers of gas in the [Lower 48] fear that when this "bubble of gas" from the Mackenzie River area and Alaska hits the market it will cause the market to be depressed, and that therefore those sellers are lobbying in Washington [D.C.] against incentives to build a line. He asked whether that is one of the biggest problems [the producers] are dealing with.

MR. KONRAD responded that, clearly, a number of parties are saying a number of things, and that it is far from simple. He said that in Canada, however, "things feel ... pretty good," and that the group there is almost ready to file permits; that project simply is ahead of the Alaskan project. He indicated his company continues to tell people in Canada, Washington [D.C.], and Alaska that clearly in the 2010-plus timeframe the market will be able to easily accommodate these volumes of gas. A question on a national policy issue is whether the preference is to have gas from Alaska, import LNG, or burn oil in power-generation plants. He said it isn't a matter of too much gas coming into the market.

Number 1127

REPRESENTATIVE KERTTULA asked Mr. Myers to describe what Version H possibly could apply to, particularly with regard to any other technology or area.

Number 1170

MARK MYERS, Director, Division of Oil & Gas, Department of Natural Resources, answered:

I believe it would qualify for, certainly, any gas-to-liquids projects, basically any statewide project that could produce the volume qualifications of 500 bcf over the 20-year period. It could potentially apply, ... I believe, to natural gas liquids shipped down, say, ... a conventional oil pipeline like we do now on the Slope. So, basically, it would be statewide and certainly would apply to LNG as well as conventional gas. It is conceivable in some basins, like the Nenana basin, there may be sufficiency of gas, assuming there was a way to export it beyond the Fairbanks market, to apply - and possibly for coal bed methane, [although] that would be a large quantity of coal bed methane gas to produce ... over a 20-year period. So, certainly, it's broad and flexible.

Number 1232

REPRESENTATIVE KERTTULA asked if there is a real need for incentives for all possible projects, no matter when or where.

MR. MARKS offered the judgment that given the size of all these projects, they are risky. Fiscal uncertainty adds to the other financial risks, he said, and these projects are marginal or "on the line" now, so any risk reduction is good and will help these projects.

REPRESENTATIVE KERTTULA asked, "How far down would you reduce that risk?"

MR. MARKS answered that he believes fiscal [uncertainty] is a risk that can be reduced, and that he wouldn't characterize it as "going down" because the state wouldn't necessarily come out behind as a result of simply nailing down its fiscal system. He continued:

In addition, this Act provides the opportunities to improve the fiscal system so that, indeed, under certain conditions, especially those of high prices, the state can ... come out much, much better than what it would do ... under the current fiscal system. So I don't believe the state ... is giving up anything by going into this process and, indeed, could ... come out far, far better than what it is now.

Number 1373

REPRESENTATIVE KERTTULA expressed a "lawyer's comment or concern" about opening this up. She asked how difficult it would be to rewrite the statute so that instead of relying on a contract, the provision Mr. Marks was talking about - in terms of making it a progressive rather than regressive tax scheme - would be put in statute; that way, all parties would know what they are getting.

MR. MARKS answered that the statutes could certainly be changed to make a more progressive system, which would reduce the risks associated with a regressive or "front-end-loaded" tax system. However, the issue of fiscal uncertainty would remain. In further response, he explained that the state could establish a statutory fiscal regime and yet a sponsor would question whether to spend \$20 billion without knowing what the tax rate would be, which may make the project uneconomical. Once the project is built, one can't "unbuild it," he pointed out, and so just having it be subject to changes in the [state's] fiscal system adds to the uncertainty and fiscal risk.

Number 1483

CHAIR KOHRING announced that HB 16 would be held over at the request of the sponsor, as well as to deal with questions about Section 2 of Version H and to have discussions with other groups. He expressed support for the concept of the bill and an intent to move it forward soon. [HB 16 was held over.]

ADJOURNMENT

There being no further business before the committee, the House Special Committee on Oil and Gas meeting was adjourned at 5:16 p.m.