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SENATE CS FOR HOUSE BILL NO. 286(RES)

IN THE LEGISLATURE OF THE STATE OF ALASKA

TWENTY-FOURTH LEGISLATURE - FIRST SESSION

BY THE SENATE RESOURCES COMMITTEE

Offered: 5/5/05

Referred: Finance

Sponsor(s): REPRESENTATIVES SAMUELS, Dahlstrom, McGuire, Anderson, Kohring, Chenault

A BILL

FOR AN ACT ENTITLED

1 **"An Act amending the manner of determining the royalty received by the state on gas**
2 **production by directing the commissioner of natural resources to accept, under certain**
3 **circumstances, the transfer price of the gas if established by transfer price order of the**
4 **Regulatory Commission of Alaska; extending and amending the requirements**
5 **applicable to the credit that may be claimed for certain oil and gas exploration expenses**
6 **incurred in Cook Inlet against oil and gas properties production (severance) taxes, and**
7 **amending the credit against those taxes for certain exploration expenditures from leases**
8 **or properties in the state; and providing for an effective date."**

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

10 * **Section 1.** AS 38.05.180(aa) is amended to read:

11 (aa) Within 90 days after the written request of a lessee of a lease issued under
12 this section or of a lessee of federal land from which the state is entitled under

1 applicable federal law to receive a share of the royalty on gas production, the
 2 commissioner shall enter into an agreement with the lessee to use or accept, **as the**
 3 **value of the state's royalty share of gas production,** the price for the gas established
 4 in the contract between the lessee and a gas or electric utility [AS THE VALUE OF
 5 THE STATE'S ROYALTY SHARE OF GAS PRODUCTION] sold by the lessee
 6 under the contract **or the transfer price between the lessee and a gas or electric**
 7 **utility for a transfer by the lessee under an order establishing the transfer price**

8 (1) but only if the primary function of the utility with which the lessee
 9 has entered into the contract **or transfer** is to provide, either directly or by selling at
 10 wholesale to another utility, gas or electricity to the general public, including
 11 residential consumers, within the utilities' service areas, and the utility with which the
 12 lessee has entered into

13 (A) the contract is not an affiliated interest, as that term is
 14 defined in AS 42.05.990, with the lessee or with a subsequent purchaser of
 15 more than 10 percent of the utility's gas or electricity; **or**

16 (B) **the transfer is an affiliated interest, as that term is**
 17 **defined in AS 42.05.990, and the transfer price between the lessee and the**
 18 **utility is established by an order of the Regulatory Commission of Alaska;**
 19 and

20 (2) unless the commissioner makes a written finding, based on clear
 21 and convincing evidence, that

22 (A) the contract price **or transfer price** is unreasonably low;

23 (B) the prospective reduction in royalty receipts would not be
 24 balanced by increased benefits to in-state gas and electric consumers;

25 (C) the lessee and the utility are related in management,
 26 ownership, or other aspect **and, in the case of a transfer price, that**
 27 **relationship is not regulated under AS 42.05;** and

28 (D) the contract price **or transfer price** is not in the best
 29 interest of the state.

30 * **Sec. 2.** AS 43.55.025(a) is amended to read:

31 (a) Subject to the terms and conditions of this section, on oil and gas produced

1 **on or after July 1, 2004**, from an oil and gas lease, or on gas produced from a gas
 2 only lease, [ON OR AFTER JULY 1, 2004,] a credit against the **production** tax due
 3 under this chapter is allowed **for exploration expenditures that qualify under (b) of**
 4 **this section** in an amount equal to **one of the following**:

5 (1) 20 percent of the total exploration expenditures that qualify **only**
 6 under (b) and (c) of this section;

7 **(2)** [,] 20 percent of the total exploration expenditures **for work**
 8 **performed before July 1, 2007, and** that qualify **only** under (b) and (d) of this section
 9 [, OR BOTH, FOR A TOTAL CREDIT THAT DOES NOT EXCEED 40 PERCENT
 10 OF THE TOTAL EXPLORATION EXPENDITURES];

11 **(3) 40 percent of the total exploration expenditures that qualify**
 12 **under (b), (c), and (d) of this section**; or

13 **(4)** [(2)] 40 percent of the total exploration expenditures that qualify
 14 **only** under (b) and (e) of this section [, FOR A TOTAL PRODUCTION TAX
 15 CREDIT THAT DOES NOT EXCEED 40 PERCENT OF THE TOTAL QUALIFIED
 16 EXPLORATION EXPENDITURES].

17 * **Sec. 3.** AS 43.55.025(b) is amended to read:

18 (b) To qualify for the production tax credit under (a) of this section, an
 19 exploration expenditure must be incurred for work performed on or after July 1, 2003,
 20 and before July 1, 2007, **except that an exploration expenditure for a Cook Inlet**
 21 **prospect must be incurred for work performed on or after July 1, 2005, and**
 22 **before July 1, 2010, and except that an exploration expenditure, in whole or in**
 23 **part, south of 68 degrees, 15 minutes, North latitude, and not part of a Cook Inlet**
 24 **prospect must be incurred for work performed on or after July 1, 2003, and**
 25 **before July 1, 2010**, and

26 (1) may be for seismic or geophysical exploration costs not connected
 27 with a specific well;

28 (2) if for an exploration well,

29 (A) must be incurred by an explorer that holds an interest in the
 30 exploration well for which the production tax credit is claimed;

31 (B) may be for either an oil or gas discovery well or a dry hole;

1 and

2 (C) must be for goods, services, or rentals of personal property
3 reasonably required for the surface preparation, drilling, casing, cementing,
4 and logging of an exploration well, and, in the case of a dry hole, for the
5 expenses required for abandonment if the well is abandoned within 18 months
6 after the date the well was spudded;

7 (3) may not be for testing, stimulation, or completion costs;
8 administration, supervision, engineering, or lease operating costs; geological or
9 management costs; community relations or environmental costs; bonuses, taxes, or
10 other payments to governments related to the well; or other costs that are generally
11 recognized as indirect costs or financing costs; and

12 (4) may not be incurred for an exploration well or seismic exploration
13 that is included in a plan of exploration or a plan of development for any unit on
14 May 13, 2003.

15 * **Sec. 4.** AS 43.55.025(c) is amended to read:

16 (c) To be eligible for the [A] 20 percent production tax credit **authorized by**
17 **(a)(1) of this section or the 40 percent production tax credit authorized by (a)(3)**
18 **of this section**, exploration expenditures must

19 (1) qualify under (b) of this section; and

20 (2) be for an exploration well, **subject to the following:**

21 **(A) for an exploration well other than a well that is**
22 **described in (B) of this paragraph, the well must be** [THAT IS] located and
23 drilled in such a manner that the bottom hole is located not less than three
24 miles away from the bottom hole of a preexisting suspended, completed, or
25 abandoned oil or gas well; in this **subparagraph** [PARAGRAPH],
26 "preexisting" means a well that was spudded more than 150 days but less than
27 35 years before the exploration well was spudded;

28 **(B) for an exploration well that explores a Cook Inlet**
29 **prospect, the well must be located at least three miles from any other well**
30 **drilled for oil and gas with all distances measured as the horizontal**
31 **distance between exploration targets, except that the exploration well that**

1 is located within three miles of a well drilled for oil and gas qualifies for
 2 the tax credit authorized by this subsection if the exploration well tests
 3 potential hydrocarbon traps that the commissioner of natural resources
 4 determines, after analyzing evidence submitted by the explorer and from
 5 other information that the commissioner of natural resources determines
 6 relevant, constitute a distinctly separate exploration target.

7 * **Sec. 5.** AS 43.55.025(d) is amended to read:

8 (d) To be eligible for the [AN ADDITIONAL] 20 percent production tax
 9 credit authorized by (a)(2) of this section or the 40 percent production tax credit
 10 authorized by (a)(3) of this section, an exploration expenditure must

11 (1) qualify under (b) of this section; and

12 (2) be for an exploration well that is located not less than 25 miles
 13 outside of the outer boundary, as delineated on July 1, 2003, of any unit that is under a
 14 plan of development, except that for an exploration well for a Cook Inlet prospect
 15 to qualify under this paragraph, the exploration well must be located not less
 16 than 10 miles outside the outer boundary, as delineated on July 1, 2003, of any
 17 unit that is under a plan of development.

18 * **Sec. 6.** AS 43.55.025(e) is amended to read:

19 (e) To be eligible for the 40 percent production tax credit authorized by
 20 (a)(4) [IN (a)] of this section, the exploration expenditure must

21 (1) qualify under (b) of this section;

22 (2) be for seismic exploration; and

23 (3) have been conducted outside the boundaries of a production unit or
 24 an exploration unit; however, the amount of the expenditure that is otherwise eligible
 25 under this subsection is reduced proportionately by the portion of the seismic
 26 exploration activity that crossed into a production unit or an exploration unit.

27 * **Sec. 7.** AS 43.55.025(f) is amended to read:

28 (f) For a production tax credit under this section,

29 (1) an explorer shall, in a form prescribed by the department and
 30 within six months of the completion of the exploration activity, claim the credit and
 31 submit information sufficient to demonstrate to the department's satisfaction that the

1 claimed exploration expenditures qualify under this section;

2 (2) an explorer shall agree, in writing,

3 (A) to notify the Department of Natural Resources, within 30
 4 days after completion of seismic or geophysical data processing, completion of
 5 a well, or filing of a claim for credit, whichever is the latest, for which
 6 exploration costs are claimed, of the date of completion and submit a report to
 7 that department describing the processing sequence and providing a list of data
 8 sets available; **if, under (c)(2)(B) of this section, an explorer submits a**
 9 **claim for a credit for expenditures for an exploration well that is located**
 10 **within three miles of a well already drilled for oil and gas, in addition to**
 11 **the submissions required under (1) of this subsection, the explorer shall**
 12 **submit the information necessary for the commissioner of natural**
 13 **resources to evaluate the validity of the explorer's claim that the well is**
 14 **directed at a distinctly separate exploration target, and the commissioner**
 15 **of natural resources shall, upon receipt of all evidence sufficient for the**
 16 **commissioner to evaluate the explorer's claim, make that determination**
 17 **within 60 days;**

18 (B) to provide to the Department of Natural Resources, within
 19 30 days after the date of a request, specific data sets, ancillary data, and reports
 20 identified in (A) of this paragraph;

21 (C) that, notwithstanding any provision of AS 38, information
 22 provided under this paragraph will be held confidential by the Department of
 23 Natural Resources for 10 years following the completion date, at which time
 24 that department will release the information after 30 days' public notice;

25 (3) if more than one explorer holds an interest in a well or seismic
 26 exploration, each explorer may claim an amount of credit that is proportional to the
 27 explorer's cost incurred;

28 (4) the department may exercise the full extent of its powers as though
 29 the explorer were a taxpayer under this title, in order to verify that the claimed
 30 expenditures are qualified exploration expenditures under this section; and

31 (5) if the department is satisfied that the explorer's claimed

1 expenditures are qualified under this section, the department shall issue to the explorer
 2 a production tax credit certificate for the amount of credit to be allowed against
 3 production taxes due under this chapter; **however, notwithstanding any other**
 4 **provision of this section, the department may not issue to an explorer a**
 5 **production tax credit certificate if the total of production tax credits submitted**
 6 **for Cook Inlet production, based on exploration expenditures for work**
 7 **performed during the period described in (b) of this section for that production,**
 8 **that have been approved by the department exceeds \$20,000,000.**

9 * **Sec. 8.** AS 43.55.025(k) is amended to read:

10 (k) In this section,

11 **(1) "Cook Inlet production" means oil or gas production from the**
 12 **Cook Inlet sedimentary basin, as that term is defined by regulation adopted to**
 13 **implement AS 38.05.180(f)(4);**

14 **(2) "Cook Inlet prospect" means a location within the Cook Inlet**
 15 **sedimentary basin, as that term is defined by regulation adopted to implement**
 16 **AS 38.05.180(f)(4);**

17 **(3) "explorer" means a person who, in exploring for new oil or gas**
 18 reserves, incurs expenditures.

19 * **Sec. 9.** This Act takes effect immediately under AS 01.10.070(c).