

ALASKA STATE LEGISLATURE
SENATE RESOURCES STANDING COMMITTEE

January 31, 2005

3:37 p.m.

MEMBERS PRESENT

Senator Thomas Wagoner, Chair
Senator Bert Stedman
Senator Kim Elton
Senator Ben Stevens

MEMBERS ABSENT

Senator Ralph Seekins, Vice Chair
Senator Fred Dyson
Senator Gretchen Guess

COMMITTEE CALENDAR

OVERVIEW: State Gas and Oil by Mark Myers, Director, Division of Oil and Gas, Department of Natural Resources (DNR)

SENATE BILL NO. 69

"An Act making special appropriations to promote the opening of the Arctic National Wildlife Refuge for oil and gas exploration and development; and providing for an effective date."

SCHEDULED BUT NOT HEARD

ACTION NARRATIVE

CHAIR THOMAS WAGONER called the Senate Resources Standing Committee meeting to order at [3:37:23 PM](#). Present were Senators Elton, Stedman and Chair Wagoner. Senator Ben Stevens arrived at 3:43.

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OVERVIEW: by Mark Myers, Director, Division of Oil and Gas, Department of Natural Resources (DNR)

MR. MYERS presented a power point presentation called, "Alaska Oil and Gas Activities." The following are some highlights.

He explained that the state gets money from its land in two ways - as a resource owner through leases and from its powers of sovereign taxation. The department gets its funds from three

different sources - leasing land, rentals from the land and royalty money when production occurs on it. Seventy-five percent of the state's royalty money goes into the General Fund, 25 percent into the Permanent Fund and .5 percent goes into the School Fund. He said the state received about \$1.4 billion in royalties and \$1 billion in taxes this year. The taxes came from being a property owner, corporate income tax and severance tax. About 87 percent of state's general unrestricted fund comes from royalty taxes.

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MR. MYERS said that the state's two large fields are dramatically declining, but more small productive fields have begun producing to offset that decline. Bringing in new parties to explore the Basin is critical to bringing on new undiscovered fields within the declining picture.

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High gas prices are the reason revenues are up for the fiscal year, not declining oil and gas volumes.

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MR. MYERS said that in the last 10 years, 27 percent of North Slope production came from new production. He said that a lot of units were formed in Cook Inlet in the last few years, which has resulted in increased exploration activities and more successes with smaller accumulations of gas. There has also been increased exploration by new players in response to higher gas prices, but the big question is if there are sufficient exploration and discoveries to offset the decline.

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He stated that internal state use of gas is highly variable; more is used in the winter than in the summer. There must be a surplus and some way to store it. In the past, producers always had a surplus in their shut-in wells that were reopened in the winter, but there is barely enough gas to meet needs now and it gets worse every year. Reservoirs can be used for storage, but reinjection will add to costs. The Cook Inlet Drilling Summary for 2004 indicates that it has a nine-year supply, but it is losing ground.

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MR. MYERS said the state is in discussions with three major producers, TransCanada and Midamerican Holding Corporation. Both are progressing, but at various paces. The state made two offers in the producer negotiations. Its initial offer was rejected.

Discussions on the second offer with a different structure are ongoing. Trying to make the state a partner in a pipeline project is complex.

Both parties are affected by who controls the rights to build the pipeline to Canada. There are two possibilities. One is the Northern Pipeline Act, the treaty rights that TransCanada holds through their purchase of Foothills. The second is a new built project through the National Energy Board. It's been reported that the Governor will decide which approach is reasonable and allowable and Mr. Myers said he thought that would have an impact on who actually has the rights in Canada to build this line.

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On the Alaska side, TransCanada has requested a right-of-way from the State of Alaska and that is being looked at now. It's also possible for the state to grant them a non-conditional right-of-way. The state has not had a similar request from the producers for right-of-way.

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CHAIR WAGONER asked for more details on the right-of-way.

MR. MYERS responded that TransCanada already has a conditional right-of-way from the federal government in Alaska, but it does not have a state right-of-way. It applied for and requested a non-conditional right-of-way. In that process, the DNR Commissioner reviews the application and puts it out for public comment, which has occurred. He now has to make a final decision. DNR strongly believes that a non-conditional right-of-way is not an exclusive right-of-way and another right-of-way could be applied for along the same route.

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CHAIR WAGONER asked if that would preclude Alaska Natural Gas Development Authority (ANGDA) from receiving its right-of-way (in addition to TransCanada's).

MR. MYERS replied that Yukon Pacific actually holds a conditional right-of-way permit for an LNG project. ANGDA could have a right-of-way, as well. From DNR's perspective, they are not mutually exclusive.

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SENATOR ELTON asked if a non-conditional right-of-way would allow either TransCanada or the producers to use that right-of-way.

MR. MYERS replied that that particular right-of-way would be TransCanada's in this case. The producers could apply for a separate right-of-way and be granted a separate one - in the DNR's view.

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SENATOR BEN STEVENS asked if they could have the same corridor.

MR. MYERS replied that it could not conflict with TransCanada's rights along that right-of-way, but the producers could apply for a separate right-of-way along the same route. It's not exclusive, but their rights can't be conflicting. This is DNR's view, not the Department of Law's.

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SENATOR ELTON asked if he is suggesting that the state could be establishing a property right that TransCanada could sell to the producers.

MR. MYERS answered that the real question is can the state grant only one highway right-of-way and DNR's view is that it can grant multiple highway rights-of-way. There is nothing in the lease language that is de facto exclusive. The counter argument has been that a conditional right-of-way grants no exclusivity and, therefore, a non-conditional must be exclusive. But that's not logical. He said the Joint Pipeline Office is working on this issue.

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MR. MYERS stated that he is working to get data from the Port Authority to accurately model an economical highway route project, but the department has not done the same level of analysis on LNG projects.

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SENATOR BEN STEVENS asked where the money is coming from for the state to do the modeling on the Port Authority. He also asked if there was any effort by the Port Authority to reimburse the state for its analysis.

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MR. MYERS replied that there are two components to his answer. The Stranded Gas Act assumes that the state will make

significant concessions to the parties in terms of property tax relief, royalty evaluation methodologies or any other of a list of items contained in the Act. The Port Authority has not asked for any concessions, but it has only asked the state to understand the project at this point. In that sense, there was no reason for the Port Authority to be under the Stranded Gas Act and they believe the project stands on its own. To understand whether that's true and to weight the benefits of that versus the benefits of getting reimbursed for its expenses, but ultimately making concessions in the project, DNR felt it was necessary to model it using existing staff and travel time. He needs to acquire as much data as possible from them directly and to do that, he needs some form of confidentiality. For this he used an MOU.

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In addition, he asked the Legislature for \$1.5 million last year that is not reimbursable to help develop the model, but the division will far exceed that before the full analysis is done. If he finds holes in the Port Authority's data, he will need significantly more money.

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He reported that discussions are ongoing with the Federal Energy Regulatory Commission (FERC), both in Anchorage and in Washington, D.C., to be adequate for the new pipeline. "No matter who builds the pipeline, the regulatory structure is incredibly important to protect Alaska's own internal interests."

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The average estimate of undiscovered conventional gas currently exceeds 236 TCF, approximately seven times the amount of known gas reserves on the North Slope. In addition, there are huge amounts of non-conventional gas, particularly natural gas hydrates - 100 TCF of known gas hydrates, alone, in Milne, Prudhoe Bay and Kuparek - all of which is recoverable. Coalbed methane is also present in large amounts. Every exploration well has found gas, a very good indication, and a lot of it underlies existing infrastructure.

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The Legislative Budget and Audit Committee has a joint proposal with the Administration to continue the Methane Hydrate Research Act for another five years with a cost of \$70 million. It would focus on testing the hydrate resources to see if the reservoir

models are accurate in predicting rates. Progress is being made in the Interior basins and the USGS has increased its estimates.

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CHAIR WAGONER asked if anyone has shown interest in exploring in the Gulf of Alaska.

MR. MYERS replied no, but that is an area of potential. There is a lack of source data, because no one has looked hard for gas potential. To promote new investment he has tried to get new players through opening up new areas of land. There is a need for new exploration data and data integration from the new companies as well as the majors. The department is using a Department of Energy grant to work with the Oil and Gas Conservation Commission to get all the well-walking done and to get it on the web so one can simply download it. He mentioned that permitting needs to be streamlined. The state needs success stories so companies can see what is really happening up here.

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MR. MYERS stated that maximizing the use of existing infrastructure and facilities is a critical aspect on the North Slope. New infrastructure is needed in terms of staging areas, roads and new drilling sites - to name a few. New equipment and equipment storage is also needed on the Slope and lighter-weight rigs. A lot of good ideas come from new companies. Innovative technologies are being proposed and they should be considered in Alaska.

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The Nenana Basin exploration license area has good quality partners, Usibelli Energy and Doyon Corporation, who have come in to try to develop it. The Basin has a good amount of commercial gas and coal for the Fairbanks market and good long-term potential. The Copper River Basin has first its new well in 20 years, although it is not on state land.

MR. MYERS related that the division also converted its shallow gas-leasing program to exploration licensing as a result of HB 531 passing last year. The Kenai Peninsula has had a sale and he thought it was one of the most underrated basins in North America. It is gas-prone, but has oil in it also. Opposition from the fishing industry and environmental organizations has slowed exploration there.

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He reported that he had reopened the settlement with Exxon and expects a substantial amount of money would be recovered; he is currently looking at going to arbitration. It is case where there is a difference in the royalty valuation term. Exxon believes that their tanker costs ought to be higher and the state believes the destination value that it receives is significantly higher than the current market value. The division has also entered a protest over the recent raising of the TAPS tariff.

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MR. MYERS recapped that a couple of years ago the Legislature gave audit authority back to DNR and DOR. The numbers on the audits have gone up slightly, but more important is that they are much more timely on getting them done and, therefore, getting caught up with their backlog. In the future, recovered monies should go down because the audits will cover fewer and fewer years.

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On the coalbed methane issue, the Legislature put a lot of protections for surface water and private property owners in HB 531 last year that is simply not there in other states. One significant protection requires the operator, prior to any production, to designate and implement a water well testing program to provide baseline data on water quality for AOGCC approval. Those are statewide protections regardless of land title. The Mat-Su Valley now has enforceable world-class coalbed methane standards.

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HB 531 also required the DNR commissioner to establish set backs and noise mitigation measures for compression stations, which is the largest potential nuisance in coalbed methane operations. The surface impacts standards are exemplary - in terms of noise, visual light shield, solid waste, erosion control permanent erosion and timber harvesting - and production will not be allowed to occur in densely pop areas. The issues are specific and easy to understand.

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CHAIR WAGONER thanked Mr. Myers for his presentation. He noted there was no quorum at this time so he would hold SB 69. He adjourned the meeting at [4:31:37 PM](#).

NOTE: The meeting was recorded. A copy of the recording may be obtained by contacting the Senate Records Office at State

Capitol, Room 3, Juneau, Alaska 99801 or calling (907) 465-2870. After adjournment of the second session of the Twenty-Fourth Alaska State Legislature this information may be obtained by contacting the Legislative Reference Library at (907) 465-3808.