

ALASKA STATE LEGISLATURE
SENATE RESOURCES STANDING COMMITTEE

April 13, 2005

3:40 p.m.

MEMBERS PRESENT

Senator Thomas Wagoner, Chair
Senator Ralph Seekins, Vice Chair
Senator Ben Stevens
Senator Fred Dyson
Senator Bert Stedman
Senator Kim Elton
Senator Gretchen Guess

MEMBERS ABSENT

All members present

COMMITTEE CALENDAR

SENATE BILL NO. 53

"An Act relating to a credit for certain exploration expenses against oil and gas properties production taxes on oil and gas produced from a lease or property in the state; relating to the deadline for certain exploration expenditures used as credits against production tax on oil and gas produced from a lease or property in the Alaska Peninsula competitive oil and gas areawide lease sale area after July 1, 2004; and providing for an effective date."

HEARD AND HELD

SENATE BILL NO. 163

"An Act extending and amending the requirements applicable to the credit that may be claimed for certain oil and gas exploration expenses incurred in Cook Inlet against oil and gas properties production (severance) taxes."

HEARD AND HELD

SENATE CONCURRENT RESOLUTION NO. 6

Urging the governor to direct the division of oil and gas, Department of Natural Resources, to undertake a comprehensive review of the subject of Cook Inlet oil and gas platform abandonment for the purpose of developing new oil and gas platform abandonment regulations and their adoption and implementation.

MOVED CSSCR 6(RES) OUT OF COMMITTEE

SENATE CONCURRENT RESOLUTION NO. 7

Endorsing the ongoing efforts of the administration to review and revise program regulations with the objective of streamlining the exploratory oil and gas process.

MOVED SCR 7 OUT OF COMMITTEE

PREVIOUS COMMITTEE ACTION

BILL: SB 53

SHORT TITLE: AK PENINSULA OIL & GAS LEASE SALE; TAXES

SPONSOR(s): RULES BY REQUEST OF THE GOVERNOR

01/12/05	(S)	READ THE FIRST TIME - REFERRALS
01/12/05	(S)	RES, FIN
03/02/05	(S)	RES AT 3:30 PM BUTROVICH 205
03/02/05	(S)	Heard & Held
03/02/05	(S)	MINUTE(RES)
04/13/05	(S)	RES AT 3:30 PM BUTROVICH 205

BILL: SB 163

SHORT TITLE: COOK INLET OIL & GAS TAX CREDIT

SPONSOR(s): RESOURCES

04/06/05	(S)	READ THE FIRST TIME - REFERRALS
04/06/05	(S)	RES, FIN
04/13/05	(S)	RES AT 3:30 PM BUTROVICH 205

BILL: SCR 6

SHORT TITLE: COOK INLET OIL & GAS PLATFORM ABANDONMENT

SPONSOR(s): RESOURCES

04/06/05	(S)	READ THE FIRST TIME - REFERRALS
04/06/05	(S)	RES
04/13/05	(S)	RES AT 3:30 PM BUTROVICH 205

BILL: SCR 7

SHORT TITLE: OIL AND GAS REG REVISIONS

SPONSOR(s): RESOURCES

04/06/05	(S)	READ THE FIRST TIME - REFERRALS
04/06/05	(S)	RES
04/13/05	(S)	RES AT 3:30 PM BUTROVICH 205

WITNESS REGISTER

MARY JACKSON

Staff to Senator Wagoner
Alaska State Capitol
Juneau, AK 99801-1182

POSITION STATEMENT: Commented on SB 53, SB 163, SCR 6 and SCR 7 for the sponsor.

MARK MYERS, Director
Division of Oil and Gas
Division of Geological and Geophysical Surveys
Department of Natural Resources
400 Willoughby Ave.
Juneau, AK 99801-1724

POSITION STATEMENT: Supported SB 163, SCR 6 and SCR 7.

LISA PARKER
Agrium Inc.
Kenai AK

POSITION STATEMENT: Supported SB 163.

DAN DICKINSON, Director
Tax Division
Department of Revenue
PO Box 110400
Juneau, AK 99811-0400

POSITION STATEMENT: Supported SB 163.

DAN SEAMOUNT
Alaska Oil and Gas Conservation Commission (AOGCC)
333 W. 7th Ave., Ste. 100
Anchorage, Alaska 99501

POSITION STATEMENT: Supported SCR 6.

MIKE MONGER, Executive Director
Cook Inlet Regional Citizens Advisory Council (CIRCAC)
910 Highland Ave.
Kenai AK 99611

POSITION STATEMENT: Commented on SCR 6.

ACTION NARRATIVE

CHAIR THOMAS WAGONER called the Senate Resources Standing Committee meeting to order at [3:40:35 PM](#). Present were Senators Guess, Ben Stevens, Stedman, Seekins and Chair Wagoner.

SB 53-AK PENINSULA OIL & GAS LEASE SALE; TAXES

CHAIR WAGONER announced SB 53 to be up for consideration.

MARY JACKSON, staff to Senator Wagoner, explained that the companion measure, HB 71, is heading in this direction and they are amendments.

The point of bringing this to your attention is to let you know that all of these are coming. Senator Wagoner's intention is to hold SB 53 in this committee so that when HB 71 comes across, that would be the bill that would be in front of you.

CHAIR WAGONER said there was no public testimony and set SB 53 aside to wait for legislation to arrive from the other body.

SB 163-COOK INLET OIL & GAS TAX CREDIT

CHAIR THOMAS WAGONER announced SB 163 to be up for consideration.

[3:44:15 PM](#)

SENATOR KIM ELTON joined the committee.

MARY JACKSON, staff to Senator Wagoner, explained that exploration incentive credits were extended to regions in Alaska in previous legislation, but not in the Cook Inlet region. She was instructed to work on credits that would apply to the Cook Inlet and that's what SB 163 does. She provided a map to explain positioning for credits and said that the old bill provided that exploration wells must be outside of three miles from the first drill to receive the first 20 percent incentive credit. Any wells outside of 25 miles would receive a second 20 percent credit. "None of it fits the Cook Inlet."

[3:46:32 PM](#)

MS. JACKSON explained that SB 163 says the drill must be within the three miles for the first 20 percent credit and outside of ten miles for the second 20 percent. However, she pointed out that even the 10 mile is too big and very little would be applicable there. It also provides that the producer has to apply for the credits and the department must respond within 60 days, although the department would like 90 days. The credit is capped at \$20 million.

[3:47:40 PM](#)

SENATOR KIM ELTON asked how much incentive would be needed in terms of making production efficient in Cook Inlet at the current price levels.

3:47:56 PM

MARK MYERS, Director, Division of Oil and Gas and Division of Geological and Geophysical Surveys, replied that the chairman asked him what could be done in terms of incentives for Cook Inlet that already has a large number of wells. There are still some legitimate exploration targets that have not been explored.

He explained why saying that the earlier tax EIC used a mechanical mechanism that defined an exploration well via its distance from other wells. That's only one test that may be relevant and while it is simple, it's really artificial. It is irrelevant to the geological and economic risk taken on by a producer or an explorer. A lot of the plays are in deeper horizons near existing infrastructure, but they are no less risky geologically than a frontier area or wildcat in the sense of the geologic risk. The question is in a basin that is relatively mature, how to define viable exploration plays and how to provide incentives for them. Recognizing the three-mile distance criteria doesn't really define an exploration play. This presupposes a geological test - that a company would make its case to the department with seismic and well data or other geological and geophysical data and the commissioner would predetermine if it is a separate target or if it is a development well of an existing discovery.

If they can demonstrate that it is geologically distinct or reasonably estimated with the data to be distinct, the commissioner would pre-certify that they would be eligible for the credit for the well.

The Cook Inlet is seen by the majors as a relatively mature asset and the credit should encourage smaller independent companies to explore. It would assist in their drilling relatively expensive wells or bringing in the expensive jack up rigs or other infrastructure needed to drill in the offshore areas. Capping the amount at \$20 million limits the downside potential to the state.

SENATOR ELTON said he didn't think there was a perfect answer because it's highly speculative.

3:52:00 PM

SENATOR DYSON joined the committee.

SENATOR ELTON asked what the status of the shallow gas leases in the southern Kenai Peninsula are and if this credit would be applicable there.

MR. MYERS replied there is no restriction on the credits as to where they would apply in Cook Inlet - any well as long as it meets the standards would qualify.

[3:53:49 PM](#)

SENATOR SEEKINS commented that a dry hole is still a dry hole regardless of the price of oil.

[3:54:28 PM](#)

LISA PARKER, Agrium Inc., Kenai, said she appreciated the legislature's efforts to encourage development in Cook Inlet. With respect to SB 163, she said section 1 would apply to activity after July 1, 2005 only and she asked if that is the intent or a typing error.

She said section 4 and the five-year program in Cook Inlet with the \$20 million limit would mean that five or six wells could be drilled or one, if it is offshore. She asked them to reexamine the limit.

The programs still contain the usual exclusions, which diminish the attractiveness of the incentive program. These exclusions include administration, supervision, engineering, geological, management and the environmental costs - all of which are significant components and reduce the actual incentive from 20 percent to around 10 percent. With the incentive being at the discretion of the commissioner who usually decides after the work is incurred, potentially these would have little impacts on an oil company's economics.

[3:56:33 PM](#)

CHAIR WAGONER said the July 1, 2005 date was wanted in the bill and that the \$20 million limit could at least get activity started and could be revisited.

At this time I think the \$20 million laying out there gives some certainty to a lot of people that sometimes question an open-ended incentive....

DAN DICKINSON, Director, Tax Division, Department of Revenue (DOR), echoed Mr. Myers' and Ms. Jackson's comments. He said this is a production tax credit that is more attuned to what is going on in Cook Inlet. He corrected Ms. Parker who said that

the credit is capped at \$20 million per well, saying that it is not per well, but each well getting 20 percent credit not to exceed \$20 million total. But, he thought who actually gets the credit could be clarified.

CHAIR WAGONER noted that there was no further public testimony and set SB 163 aside.

SCR 6-COOK INLET OIL & GAS PLATFORM ABANDONMENT

CHAIR WAGONER announced SCR 6 to be up for consideration.

MARY JACKSON, staff to Senator Wagoner, sponsor, said the two resolutions coming before the committee are part of the results of the February Kenai meeting about abandonment of the platforms in Cook Inlet, a serious issue since 1996. This resolution urges the governor to ask the department to promulgate regulations. There was some question about whether the Department of Natural Resources or the Alaska Oil and Gas Conservation Commission (AOGCC) had precedence over that and it was found that the department does.

[4:02:03 PM](#)

MARK MYERS, Director, Division of Oil and Gas, Department of Natural Resources (DNR) said abandonment is really a big deal. Many wells are ending their lives; some have been "lighthoused" and some have been partially abandoned. It involves a lot of stakeholders and has issues like navigability. The leases require full-abandonment - full removal and back to original condition.

However, there are questions of whether there might be better and higher uses for the platforms and who retains the liability at the point of abandonment. The state has historically relied on parent company guarantees and the deep pockets of the original lessee. "It's not a liability you can sign away. That's a very strong incentive, again, a very strong protection in the process."

Smaller companies can take over some of the platforms and that has happened, but the state wants to make sure it's protected from liability. With all that said, the liability becomes an issue when folks want to sell the platforms and they should be entitled to some certainty about how, in fact, and what standard the state is going to hold the lessee to.

In the end, we fully need a process. We need a series of regulations about how we deal with these things and quite honestly, since statehood, really we haven't gone through full abandonment of these platforms. So, we're into new territory. We expect to hold a full set of procedures this year on this issue, but until we have our act together, but until we have all the participants at the table, all the stakeholders involved, we haven't been prepared to do it. This urges us to do it. We recognize in fairness to all parties we need to do it; we recognize there are a lot of stakeholders involved and we are the lead agency.

He supported the resolution, but admitted it is a daunting task.

[4:04:39 PM](#)

DAN SEAMOUNT, Alaska Oil and Gas Conservation Commission (AOGCC), said he really supports the goal of future oil and gas exploration and development. He said there is potential for undiscovered oil within reach of the Cook Inlet platforms because the known reservoirs still have a lot of oil. Recovery of the original oil in place has been relatively slow off a number of the platforms - less than 30 percent compared to other field such as Prudhoe Bay with recoveries of greater than 50 percent of the original oil in place.

We believe there are hundreds of millions of barrels of oil left in the produced fields of Cook Inlet in known reservoirs. With this, motivated and energized production companies such as Crosstimber should be encouraged to use technology to recover more of the known oil - that's the oil that's reachable from the platforms. Also, there's exploration potential left within reach. There are fewer than 300 exploration wells and 1,000 total wells that have been drilled in the entire history of the 10,000 square mile basin.

MR. SEAMOUNT said that he knows of similar size basins such as the San Juan Basin in New Mexico, which has 29,000 wells and discoveries are still being made there.

Leslie Lagoon with the USGS - expert geologist and geochemist - has concluded that only four percent of the total oil generated in Cook Inlet Basin has ever been found. We don't know yet if condensing oil has escaped to the surface or it's still trapped in undiscovered oil fields or both, but there is a lot of

oil that has not been accounted for yet. As Mark Myers was saying, there are untested fault blocks within reach and under exploratory prospects that there's been identified by many petroleum explorationists over the last 50 years.

Possibly the highest potential play is the Pre-tertiary, Cretaceous and Jurassic rocks that we've been hearing about lately in the news and Mr. Myers mentioned. The Jurassic rocks is where almost all the oil is generated. To date, only 55 wells have been drilled in this section and most have been drilled only into the very top. Little is known of its productive potential. We feel the existing offshore platforms represent viable infrastructure and it makes sense to reenter their idle well bores and deepen or sidetrack to test the Pre-tertiary section of 5,000 ft. extra depth below the Tertiary. It's an arbitrary number, but it really comes close to fully evaluating the Pre-tertiary sections potential. You could also drill to see the new fault blocks and the other prospects before abandoning the platforms.

As I've alluded to, there are four tiers of potential that are within reach of the platforms. There's the unproduced oil in known reservoirs; there are new fault blocks. There are many identified exploration prospects and there's the Pre-tertiary play. These plays would most likely be uneconomic and unreachable if it were not [indisc.] to existing platforms.

Our new commissioner, Kathy Forester, pointed out to me - she's got a lot of experience on the North Slope.... She pointed out to us that the situation at Cook Inlet is analogous to that of the North Slope where ConocoPhillips and BP are already using idle well bores on existing pads to deepen or sidetrack for small accumulations of reservoirs that would be uneconomic if not for the existing infrastructure. In other words, it's possible that Cook Inlet has already been shown to be successful by the success on the North Slope.

We feel the platforms should be viewed as assets and we recommend that all stakeholders be very careful when considering abandonment and do everything they can to have all of the potential oil and gas reserves

tested before abandonment. There's a window of opportunity right now to capture additional reserves. Platform abandonment would close that window. Once the window closes, much of the state's resources and Kenai Peninsula's economic potential could be lost.

[4:10:34 PM](#)

CHAIR WAGONER added that currently there are over 300 jobs directly related to Cook Inlet platforms. "It's a very important part of the overall oil and gas economy that we have based in Cook Inlet right now."

[4:11:05 PM](#)

MIKE MONGER, Executive Director, Cook Inlet Regional Citizens Advisory Council (CIRCAC), said the council has similar interests in the Cook Inlet platform removal. Their research has revealed that DNR has no specific regulations or statutes governing lessee's obligations and determines their obligations on a case-by-case basis. He said the council's research paper will be released in May and he would be happy to share it with them.

[4:13:28 PM](#)

CHAIR WAGONER closed the public hearing.

[4:13:33 PM](#)

SENATOR GRETCHEN GUESS moved Amendment 1.

24-Ls0775\A.1
Chenoweth
4/12/05

AMENDMENT 1

OFFERED IN THE SENATE

BY SENATOR WAGONER

TO: SCR 6

- 1 Page 2, line 6:
- 2 Delete "smaller"
- 3 Insert "growing, independent"

SENATOR ELTON objected to ask if using the word "growing" limits the intent.

MS. JACKSON explained that this paragraph references XTO Energy that is no longer in a smaller bracket. "They are a growing independent company."

CHAIR WAGONER said it is growing worldwide since taking over the Shell platforms.

SENATOR ELTON removed his objection.

[4:15:32 PM](#)

SENATOR SEEKINS moved CSSCR 6(RES) from committee with individual recommendations. There were no objections and it was so ordered.

SCR 7-OIL AND GAS REG REVISIONS

CHAIR THOMAS WAGONER announced SCR 7 to be up for consideration.

MARY JACKSON, staff to Senator Wagoner, said this resolution came from the Kenai meeting also. Practically speaking, a gentleman named James Udelhoven who began work in Cook Inlet in the late 1960's cautioned, "Don't make the first hurdle so big that the new kid won't try to take the hurdle."

She said this resolution was created to applaud the efforts that have been made to streamline permitting and to insure that those efforts are continued.

MARK MYERS, Director, Division of Oil and Gas and State Geological Survey, supported SCR 7 saying it would eliminate overhead and duplication.

[4:19:01 PM](#)

CHAIR WAGONER said the Regulatory Commission of Alaska (RCA) could work at a faster rate and has already demonstrated that recently.

SENATOR RALPH SEEKINS asked for examples of enhanced attractiveness of exploration and development.

MR. MYERS replied that some outstanding examples are in the Beaufort Sea where Teck Cominco and Armstrong Resources bought leases and within four months had their permits to drill in the Beaufort Sea, which is usually one of the hardest places to permit because of the environmental issues, remoteness of location and concerns over subsistence resources. They have developed good working relationships with the North Slope Borough, which is necessary. Kerr McGee did the same with two separate rigs this winter and last. These companies are brand new to Alaska. He explained that the hearing process within the

communities has to happen up front and that while it is labor-intensive, it streamlines the process later on.

[4:22:51 PM](#)

SENATOR SEEKINS asked if the streamlining had been accomplished through efforts of the legislature or just through incentives initiated by the administration.

MR. MYERS replied that the legislature has enhanced the process by funding some positions and moving program offices like Coastal Zone Management into the Department of Natural Resources. It has provided funding on a case-by-case basis for project coordinators and supported budget increases at times for agencies like DEC in critical areas. Having extra folks on staff has been critically important.

[4:24:45 PM](#)

CHAIR WAGONER related that other companies are going to drill in the Beaufort Sea.

MR. MYERS replied that ConocoPhillips has a well, Kerr McGee has multiple wells and Pioneer is looking at development. Another well will potentially be shallow-drilled off the Point McIntyre area.

CHAIR WAGONER asked if Pioneer was in the process of having a platform built for them.

MR. MYERS replied yes, it is lighter weight and more mobile. He said Pioneer is not actively drilling this year, but they are assessing sanctioning a development project from the earlier successful drilling out there about two years ago.

[4:26:19 PM](#)

SENATOR SEEKINS moved to pass SCR 7 from committee with individual recommendations and zero fiscal note. There were no objections and it was so ordered.

CHAIR WAGONER adjourned the meeting at [4:26:58 PM](#).