

HOUSE FINANCE COMMITTEE
March 16, 2011
1:39 p.m.

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CALL TO ORDER

Co-Chair Stoltze called the House Finance Committee meeting to order at 1:39 p.m.

MEMBERS PRESENT

Representative Bill Stoltze, Co-Chair
Representative Bill Thomas Jr., Co-Chair
Representative Anna Fairclough, Vice-Chair
Representative Mia Costello
Representative Mike Doogan
Representative Bryce Edgmon
Representative Les Gara
Representative David Guttenberg
Representative Reggie Joule
Representative Tammie Wilson

MEMBERS ABSENT

Representative Mark Neuman

ALSO PRESENT

Representative Mike Chenault, Sponsor; Representative Mike Hawker; Representative Alan Austerman; Senator Cathy Giessel; James Armstrong, Staff for Representative Bill Stoltze; Sharon Kelly, Staff, Representative Mike Chenault; Daniel Seamont, Geology Commissioner, Chair, Alaska Oil and Gas Conservation Commission.

SUMMARY

HB 166 STATE AGENCY PERFORMANCE AUDITS

CS HB 166(FIN) was REPORTED out of committee with a "do pass" recommendation and with new fiscal notes from the Office of the Governor and the Legislature.

HB 110 PRODUCTION TAX ON OIL AND GAS

HB 110 was HEARD and HELD in committee for further consideration.

#hb166

HOUSE BILL NO. 166

"An Act relating to performance reviews and audits of executive branch agencies, the University of Alaska, and the Alaska Court System; and providing for an effective date."

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Vice-chair Fairclough MOVED to ADOPT workdraft CS HB 166 (FIN) (27-LS0492\X, Kirsch, 3/14/11) as a working document in front of the committee.

Hearing no objection it was so ordered.

[NOTE: The bill version used can be located on BASIS under the Documents section and is titled: "HB 166 Comparison version I to X.pdf"]

JAMES ARMSTRONG, STAFF FOR REPRESENTATIVE BILL STOLTZE, discussed that Sharon Kelly, Staff to Representative Mike Chenault had been the lead staff on the legislation. He noted that there had been a meeting on March 3, 2011 that included Representative Hawker, staff from the Office of Management and Budget, and other offices. He thanked Lisa Kirch in Legislative Legal for her hard work on the CS and all of the workdrafts that came before it. He relayed that the committee was in possession of the workdraft, the comparison, and new fiscal note. He added that the agencies had been reordered and bracketed in the legislation.

REPRESENTATIVE MIKE CHENAULT, SPONSOR, thanked the committee for hearing the bill. During the March 3rd meeting approximately 20 issues had been reviewed and the current CS was based on the consensus of the work team. He asked his staff to discuss the changes of the bill.

SHARON KELLY, STAFF, REPRESENTATIVE MIKE CHENAULT, highlighted several of the major items in the CS. She discussed that the review team would operate under the

Legislative Audit Division instead of the Budget and Audit Committee. She explained that the order of department reviews had been changed slightly to group "like" departments together. Additionally, the Budget and Audit Committee had the authority to accelerate audits and at the request of the review team the legislature and the Office of the Governor were added to the list. Lastly, the timing of the process was changed slightly to accommodate the legislative process and the review process would sunset after the first round of reviews to ensure that the legislature's desired results were accomplished.

Co-Chair Thomas asked why the legislation would have a sunset versus a continuous review. Ms. Kelly responded that Legislative Audit had requested the sunset to make certain that the process was working correctly.

Representative Doogan asked whether it was possible to speed the process up to receive reviews sooner than 10 or 11 years out. Ms. Kelly responded that it was a ten-year cycle but that the Budget and Audit Committee could choose to accelerate the process if they wished.

Representative Doogan wondered whether the entire process could be accelerated. Ms. Kelly replied in the affirmative.

Representative Doogan was concerned about the length of time it would take to complete the process given that institutional knowledge within the legislature could be lost during the ten-year period.

Co-Chair Stoltze suspected that it could be a dynamic that was in the purview. He noted that there were routine eight-year audits and that some boards, commissions, and agencies had experienced the problem.

Vice-chair Fairclough remarked that it was possible to include more money in the fiscal note in order to advance a project. She believed that the proposed CS would allow the legislature to look at the numbers in the first few years to determine what could be accomplished with the allocated funds. She noted that the legislature could revisit the fiscal note at anytime to advance things to a more rapid pace. She supported the ten-year outlook and the ability to learn from the first departments that would go through the process.

Representative Hawker relayed that the work team had discussed at length whether the ten-year review cycle was frequent enough. The solution incorporated in the bill on Page 3, Lines 15-17 included language that would specifically provide the legislature the statutory authority to conduct reviews prior to the ten-year date at the discretion of the Legislative Budget and Audit Committee.

Co-Chair Stoltze remarked that the agencies could not be eliminated through the sunset provision.

Representative Edgmon voiced his support of the legislation. He asked whether the bill would help the process regarding the scrutiny of agency budgets and provide a better understanding of division activities and court duties. Ms. Kelly responded in the affirmative. She relayed that as part of the requirements Legislative Finance and Legislative Audit would provide the review team and finance subcommittees with an in depth report of issues that had arisen during the process.

Representative Edgmon wondered how the timing of the process worked with the governor's budget that was released annually on December 15 and with the legislative session that began January. Ms. Kelly replied that beginning in 2012 Legislative Audit would receive information from departments throughout the year and that the audit would then go to the Budget and Audit Committee about the same time that the governor's budget was released every December. The departments would continue to have approximately one month to respond and the information would then be available for the finance subcommittees when their work began every January.

Representative Guttenberg referred to Page 3, Lines 14-17. He was concerned about how to handle multiagency relationships with programs, such as the Departments of Law, Public Safety, Corrections, and the Court System that were interrelated in the work that they did. He wondered whether there was a way that the integration of a justice system could work in the process. Ms. Kelly replied in the affirmative. She referred to Page 3, Lines 11-13 and explained that overlapping services between departments would be recognized as Legislative Audit developed the scope of the audit that would be approved by the Budget and Audit Committee. She stated that it could be more

appropriate for the justice system integration to occur in 2013, while issues related to other departments could be addressed at the time of the Budget and Audit Committee review.

Representative Guttenberg wondered how the logistics of the process would take place. He discussed that the new process would have significant legislative authority; however, the final product would have to come before the legislature for approval. He noted that the bill would allow Legislative Audit to rewrite missions and measures and wondered whether a new section of expertise would be required given that an understanding of exactly what programs were supposed to accomplish would be necessary. Ms. Kelly responded that the missions and measures language was the result of a request by a member of the review team. She believed that Legislative Audit would look at the missions and measures to determine whether they appropriately measured work conducted by state agencies on behalf of the Alaskan public. She added that the committee would have the ability to recommend any changes that it would see fit.

Representative Wilson wanted to make certain the reports would be available to the public. She cited language on Page 3, Lines 8-10, that read "performance review reports are confidential unless the report has been approved..." Ms. Kelly replied the reports would become public. She noted that Page 3, Section 2 referred to work that would be completed prior to its transmittal to Legislative Audit. Currently and continuing forward the information was confidential during the month-long process and the Budget and Audit Committee would release the report following the designated period. She read from the legislation that "one week before the first day of the regular session of the legislature in the year following the review [year set out in AS 44.66.020(a)], the review team shall provide to the chairs or cochairs of the [senate and house finance] committees a final report..."(Page 6, Lines 15-18).

Representative Gara wondered about the general fund budget for the University of Alaska. Ms. Kelly responded that it was approximately \$360 million.

Representative Gara was concerned that the bill included language that would allow department budget reductions of at least ten percent when inefficiencies were identified; however, he agreed with the general concept of the bill, an

external review, and the goal to identify duplicate efforts and inefficiencies. He believed the ten percent figure was arbitrary and relayed that it would be his preference to receive a report that cited inefficiencies, provided solutions, and recommended ways to save money. He opined that in some circumstances it could decimate an agency to take ten percent. He expressed that the figure would equate to \$110 million to \$120 million for the Department of Education and Early Development's (DOEED) budget and that the significant reduction would only reduce the effectiveness of the state's education system. He added that he might introduce an amendment on the House floor that would change the language for DOEED. Ms. Kelly responded that it was not mandatory that the legislature accept the ten percent reduction. She explained that the sponsor had looked at the "Texas sunset bill" and that the Texas budget committee was recommending a fifteen percent cut. Although the bill aimed at a ten percent cut to reduce inefficiencies, it did not intend agencies to cut ten percent across the board. She remarked that the legislature may decide to invest in the infrastructure to increase savings in the future.

Representative Gara reiterated concern that the bill required departments to find inefficiencies, duplications, and things not authorized by statute that equaled at least ten percent of the budget. He understood that the legislature had the ultimate appropriation authority; however, he believed that the standards outlined in the bill may not exist. He explained that some agencies may cut fifteen percent and others could be forced to cut ten percent from areas outside of the bill's standards.

Representative Chenault remarked that without the inclusion of a set percentage a department may profess that it was not able to make any cuts. He communicated that the state was fortunate that it did not have to currently require cuts of a set percentage; however, that could change in the future due to issues that were out of its control. He believed that allowing the departments to review their own programs to determine the inefficiencies and select areas that could handle budget reductions would be better than arbitrary cuts made by the legislature in the future.

Representative Gara believed that their view points on the bill were not very far apart and that the legislature would not be required to accept the budget cut recommendations.

He reiterated his concern that a reduction of \$110 million to the DOEED would do nothing but hurt the quality of education provided to Alaskans.

Representative Chenault agreed; however, he noted that in order to have the legislative "buy-in" to the budget process, it was also necessary to have a department "buy-in."

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Vice-chair Fairclough appreciated the ten percent language and would support it on the House floor. She remarked during the review of the DOEED and University of Alaska budgets those involved had worked to make the agencies aware that oil production was declining, but the increased oil price had camouflaged the decline for the general public. Two years earlier she had a conversation with the University of Alaska President Mark Hamilton who had reported that 100 new programs had been implemented and 3 had been eliminated in the last decade. She delineated that the 100 new programs did not necessarily have full classrooms, but that agencies were leaving them on the books. She opined that for transparency purposes it was important to have a prioritization of services and programs to benefit Alaskans. She explained that the legislature had worked to communicate to the university for the past six years that budget cuts may occur in the event of an oil production decline.

Representative Doogan asked whether there had been consideration to the idea of ranking the activities and programs of each agency from most important to least important. He wondered whether a ranking process in the audit would help to address the likelihood that priorities would change over time. Ms. Kelly replied that AS 37.07.050(a)(13) required departments to prioritize every agency underneath their jurisdiction (Page 7). She discussed that Representative Hawker's office had located one of the prioritization lists from 2004 and had recommended that the language be included in the legislation.

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Co-Chair Stoltze asked whether there were any comments regarding the fiscal note.

Representative Doogan MOVED a conceptual amendment to shift the sections that dealt with the legislature and the governor to the top of the list and to have reviews conducted for the two agencies every two years.

Vice-chair Fairclough OBJECTED.

Representative Doogan believed that it would be more effective to begin the review process with the legislature. He explained that he was not attached to the idea of conducting the review every two years and that every four years was another option. He thought that conducting the review every ten years would not satisfy the people of Alaska and would not help to road test what would be done with the budgets.

Co-Chair Stoltze had no objection, but wondered how the mechanics of the amendment would work.

Vice-chair Fairclough relayed that there had been prior discussions regarding the order in which the departments were listed. She was happy to have the legislature go through the review process at a much earlier year; however, she believed that until the first audit was conducted there was no way to know what resources would be required from the legislative divisions, what administrative resources would be necessary to support the departments as they went through the review process, and how much the governor's budget would be affected.

Representative Hawker was concerned about moving forward with a conceptual amendment that had not been deliberated and discussed with those who would be administering the audits. He relayed that there were specific reasons to begin with a single agency and that resources would need to be put into place and policies and procedures would need to be established. He remarked that the items could be accommodated under the amendment; however, it would be necessary to have the precise language in front of the committee in order to evaluate exactly what the impact would be. He added that even though the legislature and the governor were included in the ten-year rotation, there was a provision in the bill that would allow the legislature to accelerate the review schedule at any time.

Representative Edgmon believed that the current department order should be maintained because oil production was declining and the intent of HB 166 was to create efficiencies, prioritization, and to focus on savings. He opined that in the event of a major decline in oil revenue a self audit of the legislature and the governor's office could occur very quickly.

Representative Guttenberg was supportive of the bill but believed that the legislature should show other agencies that it was willing to go through the review process first which would help to eliminate resistance from state employees. He expressed that other agencies would be able to see that the legislature was not treated differently and that problems detected in the initial review process would be modified and improved prior to audits of other agencies.

Representative Wilson wondered about the possibility of moving only the legislature to the top of list. She wanted to make the general public aware that the legislature believed in the idea and was willing to put itself through the process first. She was very supportive of the legislation and believed that agencies, such as DOEED needed to take a close look at their programs to increase efficiencies.

Co-Chair Stoltze asked Representative Doogan to restate the conceptual amendment.

Representative Doogan replied that the proposed amendment was to move the legislature and the governor to the top of the list and to require a review for the two groups every two years.

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Representative Gara believed that the amendment maintained the bill and would add public confidence. He expounded that the Department of Health and Social Services and DOEED would be very large audits given the size of each department and that comparatively it would be easy to include the legislature, the governor's office, and the Department of Corrections (DOC) in the first year of the review given their small size.

Representative Hawker wondered about the intent to "move [the legislature and the governor's office] to the top of

the list." He asked whether the intent would be to have the two agencies share the top of the list with DOC or to appropriately adjust DOC and the remaining agencies to later years.

Representative Doogan clarified that the intent was for the legislature and the governor's office to be included in addition to DOC.

Representative Hawker advised that the committee solicit the counsel of the audit administrators in regards to the impact of moving from one to three agencies in the first year. He explained that the first year was specifically limited to one agency to account for time to hire personnel, and outside contracts.

Co-Chair Stoltze opposed the current amendment, but believed that there was potential to accomplish the goal with further deliberation on the House floor.

Representative Doogan WITHDREW the conceptual amendment. He supported the legislation, but would reintroduce a similar version of the amendment on the House floor.

Co-Chair Stoltze believed that a compromise could be reached through discussion outside of the committee.

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Vice-chair Fairclough hoped that any amendment would be discussed with the affected bodies as recommended by Representative Hawker.

Vice-chair Fairclough MOVED to report CS HB 166(FIN) out of committee with individual recommendations and the accompanying fiscal notes.

CS HB 166(FIN) was REPORTED out of committee with a "do pass" recommendation and with new fiscal notes from the Office of the Governor and the Legislature.

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AT EASE

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RECONVENED

#hb110

HOUSE BILL NO. 110

"An Act relating to the interest rate applicable to certain amounts due for fees, taxes, and payments made and property delivered to the Department of Revenue; relating to the oil and gas production tax rate; relating to monthly installment payments of estimated oil and gas production tax; relating to oil and gas production tax credits for certain expenditures, including qualified capital credits for exploration, development, and production; relating to the limitation on assessment of oil and gas production taxes; relating to the determination of oil and gas production tax values; making conforming amendments; and providing for an effective date."

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DANIEL SEAMOUNT, GEOLOGY COMMISSIONER, CHAIR, ALASKA OIL AND GAS CONSERVATION COMMISSION, (AOGCC), introduced a chart titled "Approved Permits to Drill for Each Year (1996 - 2010) Statewide: Oil, Gas and Alternative Energy Wells and Wellbores" (Page 17 of a PowerPoint presentation titled: "Alaska Oil and Gas Conservation Commission (AOGCC)"). The chart showed the number of approved permits for all oil, gas, and alternative energy wells that had been drilled in the state. The cost of oil appeared in a green line that overlaid the chart and the permit scale ranged from 0 to 400. With the exception of 1999 and 2000, there were slightly under 250 permits issued per year. He highlighted a correlation between the dip in oil prices in 1998 and 1999 and the lowest number of wells drilled in the past 20 years; however, with recent high oil prices there could have been an inverse correlation. He was not certain about the reason related to the decrease in the number of permits that were issued around 2004 and 2005, but AOGCC planned to look at the compiled total footage drilled to determine whether the oil wells were more complex and took more time.

Mr. Seamount addressed Page 18 related to wells drilled on the North Slope: "Approved Permits to Drill for Each Year (1996 - 2010) North Slope: Oil-Related Wells and Wellbores." He explained that the chart looked very similar to the one on Page 17 because the North Slope was "king" when it came to the number of oil wells drilled and very

few wells had been drilled in other locations including Cook Inlet. He discussed the actual work done by actual investors: "Alaska Oil and Gas Conservation Commission" (Page 19). He explained that the charts looked very similar to the numbers for permits to drill on Page 17 because operators tended to follow through on their plans in Alaska. He noted that this was not the case in other areas such as the Rocky Mountains where a significant number of permits issued were never used. He discussed that Mr. Davies, Petroleum Economist, AOGCC, had developed the pie chart: "Alaska 2010 Wells and Wellbores" (Page 20). The chart showed that there had been total of 183 wells drilled in 2010 and did not account for wells drilled by operators who were still in the process of submitting their completion reports. Out of 183 wells drilled the Arctic Slope accounted for 125 producer wells, 39 service wells, and 4 exploration wells. The remaining wells were located in Cook Inlet and other areas of the state.

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Mr. Seamont pointed to a chart that showed oil, gas, and alternative energy exploration wells drilled: "Exploratory Wells and Wellbores Statewide: Completed, Suspended or Abandoned (1996-2010)" (Page 21). The chart looked similar to the ones shown on Pages 17 and 18 that were related to permits to drill. There was low exploration and price in 1999 and 2000. In 2010 the number of wells drilled exceeded the number of permits (shown on the far right-hand side of the page) because many of the applications for permits to drill had been submitted in 2009. He remarked that out of the 15 exploration wells drilled in 2010 only 7 were oil or gas exploration.

Representative Gara indicated that that the numbers discussed by Mr. Seamont did not match the numbers on Page 21. Mr. Seamont clarified that there had been 15 wells drilled in 2010 by 9 operators.

Representative Gara wondered whether 2011 was the year that only one exploratory well was drilled. Mr. Seamont replied in the affirmative. He communicated that 2011 would be an abysmal year for exploration.

Mr. Seamont discussed Page 22: "Exploratory Wells and Wellbores Statewide: Completed, Suspended or Abandoned (1996-2010)," that related only to oil and gas. There was

low exploration and price in 1999 and 2000, but there was an inverse correlation between exploration and price that began in 2005. He examined development and service wells on Page 23: "Development and Service Wells/Wellbores Statewide: Completed, Suspended or Abandoned (1996-2010)." The chart did not include exploration wells and was similar to the total wells drilled because of the small number of exploration wells. ConocoPhillips (shown in red) and BP (shown in green) made up the largest percentage of the development and service wells depicted on the graph. A handful of newer producers including Pioneer, ENI, and Savant accounted for most of the remaining percentage beginning around 2008. There had been a dip in the number of wells drilled beginning in 2004 and 2005, but it had remained relatively level through 2010.

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Representative Costello asked for a breakout of the completed, suspended, or abandoned wells that were listed on Page 23. Mr. Seamount replied that he would provide the information to the committee. He added that very few of the wells shown had been abandoned and that the majority were actively producing oil or injecting fluids to keep the reservoir pressure up.

Representative Costello wondered whether Mr. Seamount supported a claim made in another committee that the legacy companies did not take into account taxes or the price of oil in their data represented on the chart. Mr. Seamount responded that he did not have enough information to answer the question and that he was not privy to that company detail.

Co-Chair Stoltze provided a baseball analogy in reference to the difficulty he had experienced in following all of the information on the production and operation wells.

Representative Guttenberg wondered whether there was a rule of thumb regarding the allowable lag time between the submittal of a development plan and the installation of a well. Mr. Seamount replied that it was highly variable depending upon how desirable a project was to a company's management team. He reflected on one prospect in Wyoming that had taken nine years to be drilled.

Representative Guttenberg remarked that the variables were incalculable, for instance a company could be highly interested in a project and then discover that there were no rigs available. Mr. Seamount replied that there were numerous variables that could delay a project, including economic, government, litigation, and more.

Representative Guttenberg had heard of circumstances in which a company had interest in drilling a well but it was unable to do so because access to a rig was not possible until the following season when an ice road could be built. Mr. Seamount agreed. He observed that the logistics in Alaska were more challenging than those in the Lower 48.

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Representative Gara wondered why Page 22 showed that there were five exploratory well developers but did not indicate the number of wells. Mr. Seamount explained that the scale shown on the left (x-axis) of the chart related to the number of wells drilled.

Representative Gara asked about the difference between Pages 21 and 22. Mr. Seamount responded that Page 21 included oil, gas, and alternative energy and Page 22 only included oil and gas.

Representative Gara wondered whether Page 14 only included information about the North Slope. Mr. Seamount replied that Page 14 related to statewide oil and gas exploratory well permits, excluding alternative energy.

Representative Gara asked whether there was a page that showed exploratory well permits for the North Slope only. Mr. Seamount responded that he would provide a chart with the data to committee members.

Representative Gara believed that the focus of the debate on ACES [Alaska's Clear and Equitable Share] centered on the North Slope and not on other areas of the state. Mr. Seamount answered that information was included later in the presentation about the wells that had been drilled on the North Slope.

Representative Gara queried whether the suspended and abandoned wells were drilled during the year they were presented on Pages 21 and 22 or whether they had been

drilled in prior years. Mr. Seamount replied that the wells were drilled in the year in which they appeared on the chart. He expounded that wells in close proximity to infrastructure were completed and those that were farther away were not.

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Representative Wilson wondered whether there was a review process to determine why wells were suspended or abandoned to ensure that the appropriate tax credits were applied. Mr. Seamount replied that there were four petroleum engineers that monitored the situation closely and that approval for a company to abandon a project was required. He elaborated that it was necessary for a company to have a good reason for abandoning one area to drill in another and that an extensive review took place.

Representative Wilson wondered whether the information on abandoned wells was public. She noted that it would be helpful for her to know why the wells were abandoned. Mr. Seamount remarked that he could provide the committee with the information. He added that there was a two-year confidentiality rule on exploration wells but the rule did not apply to development wells.

Co-Chair Thomas wondered whether there were inactive wells that might be activated once a tax system that was more desirable for oil companies was implemented in the state. Mr. Seamount was not aware of anyone using the particular strategy. He noted that there were quite a few areas in the state that were capable of production but were not currently under production due to various issues related to infrastructure or government.

Co-Chair Thomas asked whether the issue was related to state or federal permitting. Mr. Seamount responded that he was not aware of any situation in which state government was inhibiting production.

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Representative Gara observed that oil companies had also stopped production by prohibiting access to others. He cited an example in which Conoco had prevented a company from gaining access to land by denying it the ability to

cross land owned by Conoco. Mr. Seamount was not aware of the particular situation.

Representative Costello asked whether a company could slow the rate of production on an active well. Mr. Seamount replied that a company could slow the wells when gas ratios became too high and for a variety of other technical reasons.

Representative Costello wondered whether there were other reasons for slowing a well. Mr. Seamount could not think of any other economic or additional reasons.

Mr. Seamount discussed that Page 24 titled "Development and Service Wells/Wellbores Statewide: Completed, Suspended or Abandoned (1996-2010) by BP Exploration (Alaska), Inc," was similar to Page 22 and 23 but only included BP Exploration Alaska. He relayed that 99 percent of the wells were in Prudhoe Bay, Milne Point, and Point McKenzie and were all in the North Slope. Page 25 titled "Development and Service Wells/Wellbores Statewide: Completed, Suspended or Abandoned (1996-2010) by ConocoPhillips Alaska, Inc.," related only to ConocoPhillips Alaska, Inc. He reported that the majority of the company's development and service wells were located in Kuparuk and Colville River. Additionally, the company did not take much risk, but their activity had been fairly constant over the years.

Mr. Seamount directed attention to Page 26 titled: "Completed, Suspended and Abandoned Oil and Support Wells and Wellbores - North Slope Only 1996-2010." The wells were broken out by type, the oil producers were shown in green, the oil injectors were shown in blue, and waste ejector wells were indicated in black. He highlighted that the same trends that were present on the previous slides applied to Page 26 as well. He discussed a bar chart on Page 27 titled "Alaska's Active Drilling and Workover Rigs for Each Quarter (2005-2010)," that related to statewide oil, gas, and alternative energy. The light green portion of the bars represented drilling rigs and the dark green portion represented workover rigs. He delineated that there were 15 or more active drilling and workover rigs per quarter from 2005 to the fourth quarter of 2008; but there was a sharp decline in 2009 through 2010. The price of oil that was relatively high was represented as a dark green line and, with the exception of 2006 showed no correlation with the active rigs.

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Representative Gara wondered whether the dip in the price of oil in 2009 explained the lower number of active rigs one and a half years later given that plans to drill were done two years in advance. Mr. Seamount supposed that was a possibility.

Representative Gara asked whether the chart included directional drilling rigs or whether the smaller rigs in 2009 and 2010 were rigs that drilled horizontally. He had heard that the number of rigs had declined as directional drilling had increased. Mr. Seamount responded that most rigs were extended reach and that the majority were horizontal.

Representative Gara wondered how long it had been the case that most rigs were extended reach and horizontal. Mr. Seamount believed it had been since 1999 or 2000.

Mr. Seamount addressed Page 28: "Alaska's Active Drilling Rigs for Each Quarter (2005-2010)." He explained that drilling rigs were often swapped out to do workovers. He noted the correlation between the number of workover rigs and the cost of oil on Page 29: "Alaska's Active Workover Rigs for Each Quarter (2005-2010)." He reported that many of the workover rigs had been switched over from drilling rigs and that the payoff would be quicker because workover rigs were less expensive.

Representative Hawker asked for clarification that Page 28 included oil, gas, and alternative energy statewide. Mr. Seamount replied in the affirmative. He noted that 2010 was the only year on the page that included alternative energy rigs and that it would be necessary to subtract three from that year to obtain oil and gas rigs only.

Representative Hawker wondered whether alternative energy wells were drilled prior to 2010 as a result of the extraordinary number of permits that were issued to the Department of the Interior in 2008. Mr. Seamount believed that the Department of Energy had drilled nine wells in the previous two years.

Representative Hawker asked whether the chart on Page 28 included the alternative energy wells in 2008 and 2009. Mr.

Seamount responded that coalbed methane was not considered an alternative energy.

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Representative Costello asked about an earlier statement that workover rigs tended to follow the price of oil more closely because they were more cost effective for the oil companies. Mr. Seamount responded that he had interpreted the data that way.

Representative Costello wondered why there was an exception in the fourth quarter of 2009. She asked whether there was another factor at play during that time. Mr. Seamount was not aware of another factor at play.

Mr. Seamount moved on to Page 30: "Well Workover Activities for Each Year (North Slope Only) 2003-2010." Workovers had reached a significant number of over 400 per year since 2003. A high of 582 had been reached in 2008 when oil price had been at its peak. He detailed that 500 workovers out of 3000 development wells in Alaska was a significant percentage.

Representative Guttenberg wondered what constituted a workover. Mr. Seamount replied that typically a workover or drilling rig was set directly over the well and that the wellbore was drilled and modified to increase production or to fix a leak, etc.

Representative Guttenberg remarked that it took a lot to move a rig and that 500 times in one season was significant. Mr. Seamount believed that it was expensive.

Representative Gara asked about the difference between workover rigs and development rigs. Mr. Seamount explained that a development well involved drilling a new hole in the ground, whereas a workover did not.

Representative Gara asked whether rigs had been moved 558 times in 2010 to perform workovers. Mr. Seamount replied that sometimes a series of workovers was done on the same wellbore; however, a high number of moves were represented in the number.

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Representative Gara wondered where well workover activity and expense fit within the goal to maintain and enhance oil production. He asked whether the higher number of well workovers in 2010 compared to those conducted in 2007 was indicative of an attempt to enhance or stabilize oil production. He discussed that development wells and exploration wells were used to locate oil.

Co-Chair Stoltze remarked that the committee would be able to discuss some of the issues in the presentation with other presenters as well.

Mr. Seamount responded that a significant portion of well workover activity was aimed at production increase or maintenance.

Representative Doogan asked for clarification regarding the number of wells that were represented on Page 29. Mr. Seamount responded that they were average numbers for the quarter. When a rig only worked for two months out of a quarter the number was represented as a fraction.

Representative Doogan wondered whether "four and a fraction" rigs were used during the third quarter of 2010. Mr. Seamount replied that one of the rigs may not have been active for the entire quarter and was therefore represented as a fraction.

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Mr. Seamount discussed the baseline of 200,000 barrels of oil produced per day that was represented on Page 32: "Alaska's Average Daily Oil and NGL Production Rate." He did not know about the significance of the number but believed that it was very low. He explained that at 200,000 barrels per day that Alaska's production level would be below that of North Dakota; however, the probability was not high given that Alaska had shale oil as well. He detailed that Page 33: "Alaska's Average Daily Oil and NGL Production Rate," represented a six percent production decline that AOGCC estimated would take place without any new development or production. At the six percent decline rate the state would see production of 200,000 barrels per day by 2030. Page 34 represented the same information but included a scenario in which a new Alpine sized field came online in 2018(shown in yellow). With the discovery of a new field the time it took to reach the level of 200,000

barrels per day would extend to 2033. A chart on Page 35 also showed the same information but included the hypothetical discovery of another Northstar in 2018 (shown in bright blue). The chart indicated that regular production would begin in 2024 and that a drop to 200,000 barrels per day would be delayed until 2035.

Co-Chair Thomas wondered whether there was public information on the results of a drilling operation that had occurred in Yakutat years earlier. Mr. Seamount responded that the information was public, but due to the length of time that had passed the records may not be complete.

Co-Chair Thomas discussed that the first oil produced in Alaska had been in a small village named Katalla that was later designated as a wilderness site by former President Roosevelt. He surmised that it should be possible to drill diagonally offshore to gain access to the oil that still bubbled out of the ground in the village. Mr. Seamount believed that with new technology, production from shale, and with over 20 basins in Alaska, there was a very bright future for oil and gas development in the state.

Co-Chair Stoltze wondered whether ethanol was still popular in North Dakota and other areas. Mr. Seamount opined that North Dakota may have forgotten about ethanol given their current focus on shale oil.

Representative Gara wondered how much shale oil would be included in the pipeline when it was produced in the future. Mr. Seamount believed that shale oil had a lot of potential and recommended that he speak with Paul Decker and Kevin Banks at the Division of Oil and Gas [Department of Natural Resources].

Representative Gara wondered how much it would cost to build a processing facility for a field that produced 30,000 barrels per day. He had heard others recommend the idea of providing a processing facility credit to monetize smaller fields. He thought that without a processing sharing agreement that a small oil field could not currently justify building its own processing facility. Mr. Seamount did not have an estimate. He noted that he would provide the committee with the name of one of the smaller oil companies that had built its own facility for a "little" field that produced 200 million barrels per day.

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Vice-chair Fairclough wondered whether potential redundancies between state and federal regulations were reviewed. She believed that North Dakota had the advantage of drilling on private property versus federal or state land. Mr. Seamount replied that state regulations were slightly more stringent than federal and that they were fairly streamlined.

Vice-chair Fairclough wondered whether there were any suggestions related to increasing federal government drilling compliance in the state. She had received several non-flattering photos of federal drilling operations in Alaska from AOGCC Commissioner Cathy Foerster. Mr. Seamount replied that AOGCC had spoken with Senators Mark Begich and Lisa Murkowski and with John Katz [staff to Governor Parnell] at the recent Energy Council meeting in Washington D.C. The local Department of Interior office in Anchorage was not able to ask for the money and had recently been notified of the AOGCC's intent to push for federal funding to take care of the problem wells that existed. He recommended that others encourage federal Interior Secretary Ken Salazar to provide more funds to fix the wells in an orderly way. He believed that that \$200 million would be a good start.

Representative Hawker wondered whether Mr. Seamount agreed with the Department of Revenue (DOR) production estimates that indicated 90 percent of all estimated future onshore North Slope production would come from Alaska's existing legacy fields. Mr. Seamount believed the forecast was very conservative and that the discovery of another large oil field was still possible.

Representative Hawker wondered how probable it was that another onshore development existed. Mr. Seamount believed that another field existed, but it might not be discovered.

Representative Hawker asked whether Mr. Seamount believed that the DOR estimate was incorrect and that another massive development of unfound oil would occur. Mr. Seamount opined that DOR had to be conservative and that it was not possible to bank on the discovery of another Prudhoe Bay in the near future. He believed that another field did exist but did not know that it would be found.

Representative Hawker wondered about the viability of the projections by venture capital company Great Bear. The company had never drilled a well, but was making plans to create a program that would develop 200 wells per year.

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Mr. Seamont replied that similar operations were currently underway in locations such as North Dakota and although the logistics in Alaska were more difficult, there was a possibility that it would be feasible in the state.

Representative Hawker asked whether there were enough rigs available to develop 200 wells per year. Mr. Seamont answered that there were not and that the company would have to bring rigs in.

Representative Hawker asked about the validity of previous testimony provided by AOGCC commissioners that a lack in facility access on the North Slope had never resulted in the failure to produce a barrel of oil. He agreed with earlier testimony regarding the importance of the Department of Interior, Bureau of Land Management well compliance situation. Mr. Seamont believed that testimony made by other AOGCC commissioners was accurate. He clarified that twelve years earlier AOGCC had assumed that access to North Slope exploration would have been too expensive and therefore, had not asked for access.

Co-Chair Thomas wondered how to access shale oil. He had heard that large oil companies did not work with shale oil and that it would take smaller independent companies to access the large amount of shale oil that Alaska had to offer. Mr. Seamont replied that historically the smaller companies were the originators of exploration for things like coalbed methane and shale gas. He relayed that big companies tended to follow later.

Co-Chair Thomas asked for a definition of shale oil. Mr. Seamont explained that conventional oil flowed easily and had high permeability, whereas shale oil was located in very tight rock similar to cement and it was necessary to drill and break the shale into fractures to allow the oil that was trapped in the mud layers to flow out.

[3:29:48 PM](#)

Co-Chair Stoltze hoped that DOR Commissioner Butcher would help to fill in the gaps regarding the economic issues. He appreciated the depth of the presentation.

Vice-chair Fairclough noted that DOR had provided two packets dated March 15, 2011, in response to committee member questions (copy on file).

Co-Chair Stoltze thanked Mr. Seamount for his time and testimony.

HB 110 was HEARD and HELD in committee for further consideration.

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ADJOURNMENT

3:32:32 PM

The meeting was adjourned at 3:32 PM.