

SENATE FINANCE COMMITTEE
March 26, 2012
9:11 a.m.

[9:11:23 AM](#)

CALL TO ORDER

Co-Chair Stedman called the Senate Finance Committee meeting to order at 9:11 a.m.

MEMBERS PRESENT

Senator Lyman Hoffman, Co-Chair
Senator Bert Stedman, Co-Chair
Senator Dennis Egan
Senator Donny Olson
Senator Joe Thomas

MEMBERS ABSENT

Senator Lesil McGuire, Vice-Chair
Senator Johnny Ellis

ALSO PRESENT

Bryan Butcher, Commissioner, Department Of Revenue; Donna Keppers, Audit Master, Tax Division, Department of Revenue; William C. Barron, Director, Division of Oil and Gas, Department of Natural Resources;

PRESENT VIA TELECONFERENCE

Merlin Wibbenmeyer, Independent Contractor, Department of Revenue; John Larsen, Tax Division, Department of Revenue;

SUMMARY

SB 192 OIL AND GAS PRODUCTION TAX RATES

#sb192

SENATE BILL NO. 192

"An Act relating to the oil and gas production tax; and providing for an effective date."

9:13:14 AM

BRYAN BUTCHER, COMMISSIONER, DEPARTMENT OF REVENUE, testified that the change from a gross tax to a net tax in 2006, as well as changes made to Alaska's Clear and Equitable Share (ACES) in 2007, slowed the collection of in-depth information and evaluation of current oil activities on the North Slope. He shared that the information had finally been compiled and divided into two branches. One was a five-year review of activities on the North Slope; the department had encountered difficulty in acquiring the information because companies recorded the data in categories and sub-categories that were difficult to separate into necessary detail. The second branch involved categorizing the information in an easily understandable format. He relayed that the department had entertained meetings and workshops with the involved companies in an attempt to move forward as seamlessly as possible. He believed that 2012 would be the first year going forward that the detailed information would be available, which would result in the availability of actual necessary information by March 2013. He continued that the attempt to fill the data gaps had strengthened the Department of Revenue's (DOR) relationship with the Department of Natural Resources (DNR) and the Alaska Oil and Gas Conservation Commission (AOGCC). He explained that DOR had compiled the information while implementing a new tax revenue management system. The system would allow DOR to integrate the more detailed categories immediately.

9:17:09 AM

DONNA KEPPERS, AUDIT MASTER, TAX DIVISION, DEPARTMENT OF REVENUE, presented the PowerPoint Presentation: "Data Assessment Project Access to Information." She pointed out to the committee the Index on Slide 2:

- Project purpose and goals
- Accomplishments to Date
- Project Approach
- Five Focus Areas
- Cost Information Gathering Process
- Data Assessment - Over the Past Year
- Capital Expenditure Categories

- 5 Year Look Back Overview
- Data Assessment - Next 15 Months
- Data Assessment - Future 2014 Forward
- Benefits of the Project
- Next Steps
- Handout List
- Industry Information Catalogue
- SB 192, Amendment 26 Comparison to Currently Collected Data by Agency

[9:18:10 AM](#)

Ms. Keppers looked at slide 3," Data Assessment Project Purpose and Objective":

Purpose: to establish the foundation of data types required by the department for establishing a centralized, reliable, secure, and automated database of oil and gas production and tax information for DOR to evaluate tax obligations, have efficient reporting, have full compliance form producers/explorers, and for data integration into more advanced information and revenue management systems.

Objective: to assist in the design, development, and implementation of standardized reporting forms from industry leading to the development and implementation of a standardized and automated collection of oil and gas production volume, value, expense, credits, cost forecasts and revenue information to address tax related oil and gas economic, financial, and policy issues and questions for the legislature, the Governor and department.

Ms. Keppers testified that the project had been a valuable exercise and that significant work had been completed over the last year. She stated that DOR recognized that there were levels of information that were necessary for informed decision making; the department had captured the necessary information in a standardized format. She relayed that standardizing the information in order to collect it, report it back, and analyses it was the first step in setting up a new revenue management system.

[9:18:21 AM](#)

Ms. Keppers discussed slide 4, "Accomplishments Spring 2011 to Spring 2012." She stated that the accomplishments were as follows:

- Gathered data, identified information needs and sources.
- Completed Industry Information Catalogue - Handout 1.
- Focused on 5 Areas of oil and gas tax information needs.
- Hosted 4 industry workshops to communicate goals.
- Requested and compiled 5-year look back (2006-2010) of capital expenditures (CAPEX) by high level category.
- Integrated, streamlined, and automated forms.
- Proposed work plan to obtain/report detail data for FY12.
- Proposed work plan to integrate (sub ledger) oil and gas accounting data into other information systems.

Ms. Keppers stressed the DOR's responsibility to correct and clean-up any duplicate information in order to streamline the flow of data.

[9:21:51 AM](#)

Ms. Keppers discussed slide 5, "Project Approach." The slide listed the following approach:

DOR used and "integrated collaborative" approach among DOR, DNR, AOGCC, industry, and other agencies to gather current information.

- Identified current information received by DOR, DNR, AOGCC and other oil and gas industry associated agencies - "Industry Information Catalogue" - *Handout 1*.
- Identified and cross referenced statute and regulation requirements of data received and NOT received.
- Reviewed past and current DOR information requests.
- Reviewed compliance level of responses.

- Identified type and format of information submitted by companies (PDF's, Excel Spreadsheets, etc) for documents, graphs, charts, displays, narratives, spreadsheet data files.

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Ms. Keppers continued to slide 6, "Focus on Current Areas." She stated that the areas that were the key sources of oil and gas tax related information and reporting activities were:

- Production Forecast Reporting
- Cost Forecast Reporting
- Monthly Information Reporting
- Credit Application Filing
- Annual Production Tax Return

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Co-Chair Stedman noted that there was a section of SB 192 that dealt at length with the collection of information. He hoped DOR could work with the committee to draft agreeable language into the legislation.

[9:23:11 AM](#)

Co-Chair Hoffman felt that audit analysis and time-frame for receiving information should be included in the key areas. Ms. Keppers replied that the issue could be addressed.

[9:23:37 AM](#)

Ms. Keppers discussed slide 7, "Cost Information Gathering Process." She discussed the following work plan:

- Conducted in house discussion and review.
- Developed CAPEX & OPEX Expense Category Lists.
- Conducted 4 workshops with industry.
- Industry responsive in both active participation and written comments.
- Developed CAPEX 5 year look-back of high level cost categories.

- Proposed forward-looking more detailed CAPEX and OPEX cost categories - *Handout 2*.

[9:26:10 AM](#)

Ms. Keppers looked at slide 8, "Data Assessment to Date":

- Data Assessment Project accomplishments, forms & processes.
- 5 Year Look Back effort - compiled baseline data.
- Annual Cost Supplemental Information Report, rev 1.
 - Effective for CY 2011 tax reporting due March 31, 2012
 - Uses high level look back CAPEX categories
 - Filed by producers and explorers
- Near completion of Annual Production Tax Return

Ms. Keppers spoke to the issue of audits. She stated that DOR had a 6 year statute of limitation to complete audits. She explained that the process was large and complex; considering the 6 year time period for completion, the tax division should not be accused of being behind on the audits. She reiterated that automatizing and standardizing the information, collecting it in a timely manner and putting it into an easy to read format would expedite the auditing process. She relayed that the department had made some accomplishments concerning form and processes and had prescribed what was necessary according to statute. She said that DOR had worked with industry to standardize data. She furthered that some changes that had been made would be effective in the current tax reporting year; the annual cost supplemental information would be categorized in the 5 high level areas listed on Slide 9 and then added to the look back effort.

[9:31:40 AM](#)

Ms. Keppers discussed slide 9, "Capital Expenditure Categories":

- Look Back Categories for 2006-2010:
 - Geological & Geophysical Work (G&G)
 - Exploration Drilling
 - Development Drilling
 - Facilities
 - Other Capital

- High level categories were used as a result of workshop discussions with industry to balance the department's information needs and the industry's ability to respond in a short time frame for 5 years of historical data.
- Categorized capital expenditure data provided represents 90% of company reported capital expenditures relating to credits.

[9:32:07 AM](#)

Ms. Keppers addressed slide 10, "5 Year Look Back (2006-2012) Qualified Capital Expenditures":

- Another aspect of the Data Assessment Project included the 5 year look back of qualified capital expenditures into pre-defined industry compatible categories.
- The pre-defined categories for the look back were high level common categories used across the industry to serve as a historical baseline for analysis.
- For CY 2012 and forward tax reporting the department has proposed expanded pre-defined more detailed CAPEX and OPEX cost categories to the industry.

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Ms. Keppers discussed slide 11, "Data Assessment Next 15 Months":

- Host prospective Cost Information Workshops on CAPEX\OPEX.
- Update Annual Cost Supplemental Information Report, rev 2.
 - o Effective for CY 2012 reporting due March 31, 2013
 - o Uses more detailed categories following additional workshops - April 2012
 - o Filed by producers and explorers
- Finalization of Annual Production Tax Return for 2012 reporting.

- Consolidating standardized forms to eliminate duplicate reporting.
 - Finalize oil and gas reporting processes, definitions
 - Compile 5 YLB historical cost data with 2012 cost data for analysis
- Complete the foundation and basis for data integration with a Tax Revenue Management System ("TRMS").
- Refine proposed work plan to initiate development and integration of standardized oil and gas accounting information into a secured database once the Tax Revenue Management System ("TRMS ") project plans decisions advance.

Ms. Keppers stressed that there was a great amount of baseline information necessary before the new system could be implemented.

[9:36:14 AM](#)

Ms. Keppers looked at slide 12, "Data Assessment Future July 2014 Forward."

- The project has defined what we need to do to organize the oil and gas accounting information.
- TRMS project needs to establish the project implementation plan in order for our project to integrate into that system.
- After TRMS project implementation plan is defined, the next step is to define how the oil and gas accounting information will be incorporated into TRMS and when it can begin.

[9:37:06 AM](#)

Ms. Keppers discussed slide 13, "Benefits of Data Assessment Project":

- Proposed reporting definitions and automation standards.
- Established reporting categories for qualified capital expenditures categories.

- Obtained historical capital expenditure information.
- Developed requirements to report cost categories going forward in 2012.
- Identified potential for electronic data sharing among associated agencies.

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Ms. Keppers continued to Slide 14, "Next Steps":

- Continued interaction with stakeholders to complete identifying and defining more detailed cost categories for both CAPEX and OPEX for 2012 tax reporting
- Complete standardization of forms, format and content
- Automation of the standardizes forms

Ms. Keppers recognized the committee maintained the expectation that more useful information would be made available within the next year.

[9:38:06 AM](#)

Ms. Keppers referred to Slide 15, which listed the handouts. She stated that the Industry Information Catalogue was a compilation of information that DOR, DNR, and AOGCC had received. She discussed the spreadsheet, "Oil and Gas Information Disclosure in Alaska". The column headers on the document signaled the following information:

- Type of Data
- Agency Receiving Data
- Statue/Regulation Authority
- Agencies with which Data May be Shared
- Reason for Data Submission
- Disclosure Timeframe
- Publication and Public Access
- Form of Reported Info.
- Data Provided By Source Agency
- Additional Data Needs of DOR

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Ms. Keppers relayed that while crafting the spreadsheet workshops were held with industry. Research into DOR's tax accounting system had revealed that the department had been receiving the requested general information. She revealed that DOR would need to request more specific information in regard to lease expenditures and the form in which the department received the information would need to be standardized. She shared that companies often believed that DOR was requesting redundant information. She conceded that volumes of information had been given to DOR by industry; however, the information could not be categorized because it was not in a standard form. She said that it should not be the role of the department to decide where the costs should be categorized. She trusted that once the department defined the categories industry could make the decision.

[9:41:36 AM](#)

Ms. Keppers stated that DOR had created a large matrix of every piece of industry information that the tax division had received. She stated that more specific information concerning lease expenditures would be gathered through the capital and operating expenditures (CAPEX & OPEX) exercises.

[9:42:34 AM](#)

Ms. Keppers discusses the handout, "Proposed Master Expenditures Categories List" (copy on file). She explained that when DOR resumed workshops with industry in April 2012 the list would be reviewed in detail. Page 1 of the list gave the CAPEX expenditure categories and accompanying definitions. Working through the list with corporations would define what information needed to be shared between DOR and industry. Pages 2 through 4 listed OPEX expenditures.

[9:44:09 AM](#)

Ms. Keppers addressed the handout, "SB 192, Amendment 26, PIMS Data Requirements Comparison to Currently Collected Data by Agency" (copy on file). She explained the handout detailed the comparison of what was listed in the amendment and what was currently collected by agency. The first column listed individual items that may have been listed as a single line item in the amendment. The second column listed the information that could be found in the industry

catalogue; the third column listed the agency collecting the information.

[9:45:11 AM](#)

Co-Chair Stedman wondered which items on the handout were proprietary. He spoke to concerns that the requests in the CS involved issues that were more complicated than they appeared in the surface.

Commissioner Butcher replied that DOR had the responsibility be very careful with proprietary information. He said that the majority of information requested in the CS was currently being collected. He added that the determination of what information could be released to the public would be determined on a case-by-case basis.

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Ms. Keppers referred to the center column on the handout. She stated that it had been discovered that four items listed in the amendment had not been collected. She said that the information could be collected with more coordination with DOL&WD.

[9:47:20 AM](#)

Ms. Keppers stated that there was data collected among the three agencies that was not identified in the amendment.

[9:47:35 AM](#)

Commissioner Butcher interjected that slide 17 touched on the fact that 90 percent of the data requirements in the CS were already being collected by the 3 agencies. Only 4 of the 35 data items were not currently being collected, which could be fixed through further coordination with DOL&WD. He expressed concern that redundant information collection would be financially inefficient. He said that over the last year DOR had been the agency compiling all of the information and would expand the search to the handful of data items not currently being collected.

[9:48:33 AM](#)

Co-Chair Stedman pointed out that the handout listed 5 data items that had not been collected.

[9:48:41 AM](#)

Co-Chair Hoffman referred to page 2 of the handout. He queried why DOR had not collected information about Production Work Programs and Production Work Program Budgets.

[9:49:08 AM](#)

Co-Chair Stedman added that no information had been gathered concerning Exploration Work Program Budgets.

Ms. Keppers understood that further collaboration with DOL&WD would be necessary in order to collect information at the level DOR needed.

[9:50:05 AM](#)

Co-Chair Hoffman noted that the missing information had been previously requested by the committee. He expressed disappointment that the data had not been made available to the state.

Commissioner Butcher agreed to provide the information following future conversations with DOL&WD. He explained that the DOR had worked to identify all of the information necessary in order to evaluate revenue issues. He admitted that the department had failed to consider collecting the information prior to the last year.

Co-Chair Hoffman wondered if DOR felt that gathering the missing information was a worthwhile pursuit. Commissioner Butcher replied that the information would have value to the state.

[9:51:40 AM](#)

Co-Chair Stedman asked if DOR had been communicating with DOL&WD the importance that the requested information reached the committee expeditiously. He suggested that a letter from the committee might expedite the process. Ms. Keppers testified that DOR would work with the DOL&WD. She said that to date the department had collaborated with DNR and AOGCC on the commonality of information.

[9:52:30 AM](#)

Senator Egan referred to page 3 document. He understood that DOL was receiving monthly reports concerning Oil and Gas Employment Information and Training. He wondered why DOR did not have access to the information.

Ms. Keppers stated that the area was one in which a gap had been recognized. She assured the committee that the department recognized that more work needed to be done with DOL&WD in the area of information sharing.

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Co-Chair Stedman noted that the section of the bill that spoke to the issue could be altered to reflect the recommendations of the department. He thought the priority moving forward should be to focus on the delivery of information to the committee. Commissioner Butcher replied that the department would provide specific recommendations.

Co-Chair Stedman added that the committee was not interested in redundant information. He highlighted that the concern centered on the flow of information to the committee.

[9:54:37 AM](#)

Senator Olson expressed concern regarding abandoned wells; wells that had been abandoned or that could no longer be located. He understood that most of the wells were on federal ground, but wondered why page 3, item (6)(A), reflected that there was missing information concerning the wells.

[9:56:13 AM](#)

MERLIN WIBBENMEYER, INDEPENDENT CONTRACTOR, DEPARTMENT OF REVENUE (via teleconference), responded that the item specifically referred to the budget information pertaining to abandonment wells, leases, production, and transportation. He stated that industry did not normally provide the level of detailed information requested by the department.

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Co-Chair Stedman understood that DOR requested expected expenditure estimations from industry twice per year. He said that the most current figures had been released to the Senate Resources Committee in Summer of 2011. He queried when the information would be introduced to the committee for use in future discussions. He understood that industry could have confidentiality issues when presenting information to the legislature, but that the numbers the committee received were in the aggregate, which made the data difficult to parse. He assumed that the data would vary, but thought it would be beneficial to the committee to have a more fluid flow of information from industry in order to craft sound policy. He stressed that the substantial number of credits that affected the treasury each year necessitated open-ended appropriations in order to pay the credits as they were submitted.

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Commissioner Butcher replied that the department would provide more frequent updates to the committee.

[9:59:43 AM](#)

Co-Chair Stedman clarified that receiving the information in January was sufficient. He expressed concern that the facts of the data had varied from one committee to the next. He wondered how the problem could be alleviated.

[10:00:20 AM](#)

Commissioner Butcher replied that the department had been examining the issue of inconsistent information. He stated that for decades, the department had been too optimistic with production forecasts. He felt that the issue had been driven by overly optimistic industry projections. He pointed out that there was a similar concern regarding the capital expenditure forecasts. He explained that the industry's capital expenditure forecasts had also been too optimistic. He assured the committee that DOR was researching the issue.

[10:02:01 AM](#)

Co-Chair Stedman wondered if the situation could work in the opposite; could industry spend more than anticipated on a year-by-year basis.

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Commissioner Butcher replied in the affirmative.

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Co-Chair Stedman asserted that the issue should be frequently discussed in order to track potential capital expenditures in the future.

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Ms. Keppers replied that the forecast information was gathered twice per year by DOR's economic research group. The first forecast arrived in October and was published in the Revenue Source Book the first week of December. The spring forecast was updated in January or February of the following year.

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Co-Chair Stedman emphasized that there was always an interest in the projected forecast and the actual numbers. He shared that the change in the forecast was of interest to the committee.

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Ms. Keppers agreed that the forecast to forecast analysis was significant. She said that the department currently received the information, but not at the level of detail requested by the committee.

10:05:40 AM

Co-Chair Hoffman noted that the job of the committee was to set tax policy during the legislative session. He opined that there still seemed to be missing information. He queried the current audit results for Alaska's Clear and Equitable Share (ACES), and added that the audits were unavailable as far back as 2007. He argued that informed decisions on tax policy for the State of Alaska could not be made without all of the pertinent information. He wondered why the administration would ask the committee to make changes in the tax structure without any of the audit information. He added that the issue of abandoned wells should not be ignored by DOR. He stressed that the

information collected by DOR should be shared with the Department of Environmental Conservation (DEC), and the situation should be under better control. He declared that the state should be more aggressive in seeking the information necessary to craft sound public policy.

[10:07:55 AM](#)

Commissioner Butcher stated that he agreed that the state needed more information. He noted that 2006 was the most difficult year to audit. The state had switched from a gross tax to a net tax, while implementing dozens of new regulations. He stated that DOR was working on 2007 and was well within statutory guidelines. He said that providing the information expeditiously was a priority for the department. He shared that when the department received the returns from the companies, a desk audit was performed to assure the numbers looked accurate. He stated that a more detailed audit was later performed in order to establish the accuracy of the numbers to a higher degree. He said that the department had not noticed any large errors in the desk audits. He reiterated that the department had more audits that needed to be done, but was not behind statutorily.

[10:10:50 AM](#)

Co-Chair Hoffman accepted that the department was within the timeframe provided under statute. He asserted that the question still remained as to whether the credits were working for the state or not. He reminded the committee that consultants had testified that the state had provided too much in tax credits; the committee did not have the information to fix the problem, and the department had provided no recommendations.

[10:11:21 AM](#)

Commissioner Butcher said that half of the tax credits that were paid out were to companies that were already exploring, and that the department would not know for a decade whether production had increased as a result. He relayed that the companies themselves could give the legislature better insight as to what the credits accomplished than could DOR.

[10:12:08 AM](#)

Co-Chair Hoffman stressed that billions of dollars for the state were at risk. He asserted that an understanding of whether the credits were working or not should be a high priority for the department.

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Commissioner Butcher agreed that it was the responsibility of the department to provide sufficient information concerning the issue to the committee. He qualified that DOR was limited by an inability to foretell the future.

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Co-Chair Hoffman probed the various ways in which the legislature could assist the department in gathering the information.

[10:13:09 AM](#)

Commissioner Butcher reiterated that in 2006 the department had been overworked by the implementation of regulations for ACES and the Petroleum Production Tax (PPT). He felt that the presentation reflected the level of detail the department could provide concerning audits. He assured the committee the department would provide more detailed information in the future.

[10:13:42 AM](#)

Co-Chair Stedman expressed concern that the administration would support an increase in oil tax credits without considering consultants testimony that the credits currently extended to industry were too large and had caused a negative production tax at high oil prices. He felt that DOR had not provided a reasonable analysis or explanation for the credit increase. He noted that when PPT was crafted, the 20 percent capital credit had been targeted for increased production, but had instead gone into maintenance.

[10:16:07 AM](#)

Commissioner Butcher solicited additional questions concerning the presentation.

[10:16:16 AM](#)

Co-Chair Stedman concluded that there would be continued work between DOR and DOL&WD on providing more detailed information to the committee and the legislature.

Commissioner Butcher agreed.

[10:16:59 AM](#)

Commissioner Butcher stated that switching from a gross-system to a net-system had allowed DOR to collect a higher degree of data. He stressed that many agencies worked together to gather the important information. He shared that DOR was learning to work with each company's database program.

[10:18:07 AM](#)

Co-Chair Stedman looked to page 1 of the Industry Information Catalogue. He asked why the Joint Operating Agreements were listed as "not public information." He remarked that the chairman of the Senate Judiciary Committee had cited the joint operating agreements during public committee meetings.

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Commissioner Butcher deferred the question to the department's tax division.

[10:19:49 AM](#)

JOHN LARSEN, TAX DIVISION, DEPARTMENT OF REVENUE (via teleconference), stated that the joint operating agreements were a confidential contract between working interest owners. He explained that there were several types of agreements: joint operating agreements and unit operating agreements. He deferred further explanation to DNR.

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Co-Chair Stedman believed that DNR could clarify the difference between the two agreements. He noted that questions had risen during past meetings concerning the operating agreements. He referred to the agreements as a sort of "black box" which provided no answers.

[10:22:00 AM](#)

Senator Thomas wondered if the process of gathering data was becoming more streamlined or more burdensome for the department.

[10:23:16 AM](#)

Commissioner Butcher responded that the implementation of the new tax management system would require increased labor. He relayed that collecting the information would not be labor-saving, but would provide more detailed information.

Senator Thomas thought that the coordination between departments and reformatting of information would alleviate some of the redundant data.

Commissioner Butcher replied in the affirmative. He shared that Legislative Audit had highlighted that the archaic database programs used by the department had resulted in auditors spending time manually entering information. He believed the new system would benefit the department greatly.

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Co-Chair Hoffman requested the time-frame for completing the audits.

Commissioner Butcher replied that a time-frame could not be provided.

[10:25:14 AM](#)

Co-Chair Hoffman wondered when the department would be able to provide a time-frame in which the audits would be complete. He contended that the information was critical in discussion about revisions to the tax structure.

Commissioner Butcher responded that a snap-shot of where DOR was in the process, and how fast the department was getting caught-up, could be provided. However, the department was hamstrung by the implementation of the new database.

[10:27:32 AM](#)

Co-Chair Hoffman asserted that the committee would be negligent to not make the audits a priority. He felt that the committee had a fiduciary responsibility to the citizens of the state to push the issue of the audits. He implored DOR to establish a time-frame and report back to the committee.

Commissioner Butcher understood; however, he could not give an accurate time-frame.

[10:28:58 AM](#)

Senator Olson expressed discomfort discussing additional tax credits for the industry without having seen the audits in question.

Commissioner Butcher replied that more information was always better. He noted that DOR and the legislature had much more information now than when ACES and PPT were voted on.

[10:30:05 AM](#)

Co-Chair Stedman interjected that much of the currently available information was conflicting. He said that the report from DOR when HB 110 was introduced had raised numerous concerns on many levels, particularly the department's direct involvement in a particular piece of legislation.

[10:30:50 AM](#)

Co-Chair Hoffman referred back to the proposal in 2007 of ACES by the administration. He stated that he had not felt at that time that sufficient information had been provided, which resulted in his vote against ACES. He reiterated that a sound decision could not be made without the proper information.

Commissioner Butcher replied that the detailed audits through 2012 would have a minimal effect on the information policy makers would need to make tax decisions. He said that the department was basically going through and "dotting I's and crossing T's." He argued that the detailed audits would not provide information concerning necessary changes in the tax structure.

Co-Chair Hoffman maintained that he did not have enough information. Commissioner Butcher replied that DOR would work to provide all of the requested information.

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AT EASE

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RECONVENED

[10:44:51 AM](#)

WILLIAM C. BARRON, DIRECTOR, DIVISION OF OIL AND GAS, DEPARTMENT OF NATURAL RESOURCES, addressed a question regarding joint and operating unit agreements. He stated that he did not have the information, but would address the issue at a later date in a letter to the committee.

[10:45:35 AM](#)

Mr. Barron presented a PowerPoint Presentation, "Senate Finance Committee, 26 March 2012" (copy on file).

[10:45:47 AM](#)

Mr. Barron discussed slide 2, "Outline of Presentation":

- Land Disposition
- Land Management
- Facility Capacity Access

[10:45:52 AM](#)

Mr. Barron continued to slide 3, "Land Management: Life of Lease," which illustrated the current state process for land disposition and management. Parties could acquire access to state land in two ways: through an exploration license, or through an area-wide lease sale. Once the lease was issued there was a primary term for exploration and during that time-frame parties were expected to explore the land to prove moveable hydrocarbons. If no moveable hydrocarbons were found within the time-frame, the acreage would be made available for the next lease sale. In the event that moveable hydrocarbons were found, a unit would be formed under careful state direction concerning work programs and expectations for the first five years of development. He stated that if no significant production

occurred after five years, the unit would terminate, and the land would be returned to the state for resale. If the unit proved successful it would be deemed a Participating Area (PA). He noted that he leased under discussion before the committee were in the PA stage.

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Co-Chair Hoffman wondered why there was no time frame addressed for exploration during the primary term. Mr. Barron replied that the question would be addressed further into the presentation.

[10:48:33 AM](#)

Mr. Barron addressed slide 4, "Alaskan Area-wide Leasing System.": He stated that the area-wide lease sale was primarily the largest function of land disposition used by the state, and covered areas where:

- limited or no data exists regarding actual resource potential
- some basins have shown production or promise

Mr. Barron cited the North Slope Foothills as a primary area of interest in an active basin. He continued that new rental rates would provide a mechanism that would encourage timely exploration and development without the additional administrative burden to State. He said that during the new ten-year time-frame, the leaseholder would retain exclusive rights to explore the land. He shared that the leasing system was a product of U.S. Oil and Gas law; it relied on the highest bidder and was non-discriminatory. He explained that the state could impose work committees and special terms in lease sales (AS 38.05.035(h)) which typically occurred when the state was aware of a higher probability of known hydrocarbons in an area.

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Co-Chair Hoffman requested the imposed work commitments for the prior 5 years. Mr. Barron agreed to provide the information.

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Mr. Barron added that the state did not typically impose work commitments. Current statute required the state to provide expectations to companies concerning the lease, not vice-versa. Mr. Barron continued to slide 5, "Current Lease Terms." He relayed that in primary producing areas, i.e.; Cook Inlet and the North Slope, were currently bidding out at a minimum of \$25.00 per acre. The rental for the first seven years was \$10.00 per acre and jumped to \$250.00 per acre in years 8, 9, and 10.

[10:52:11 AM](#)

Co-Chair Hoffman questioned if the rates had been established under statute, and queried the date of their last review. Mr. Barron replied that the rates had not been established under statute, rather by the Division of Oil and Gas. The division reviewed the rates on an annual basis. He clarified that the terms in the presentation were first used in 2011 for the North Slope lease sale. He said that between the years 2002 and 2005, the lease term was for seven years, between 2006 and 2009 the term varied between five years and seven years; depending on the area, and between 2009 and 2011 it varied between seven years and ten years. The division had recognized over time that five years did not seem to be enough time because of the short drilling and exploration season. The division had established that 10 years was a reasonable maximum amount of time. He said that the jump to \$250.00 per acre at the eight year mark gave companies the choice to make a business decision after seven years at a significantly lower rate. He cited the example on slide 5:

Lease term expenditures

(20 tracts/5,760 acres each)

- Minimum bonus bid for land is \$25/acre
- 20 tracts at 5760 acres multiplied by \$25 equals \$2.88 million
- Rentals: \$10/acre equals \$1.15 million each year in annual rentals years 1 through 7
- Rentals: \$250/acre equals \$28.8 million each year in annual rentals years 8 through 10

[10:56:05 AM](#)

Mr. Barron shared that the idea was to get companies to do the work within the first seven years or pay the elevated rate for years 8, 9, and 10.

Senator Olson asked how the state's lease terms compared to terms on federal land. Mr. Barron replied that leases on federal lands were much lower.

[10:56:36 AM](#)

Co-Chair Stedman concluded the meeting with housekeeping information.

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ADJOURNMENT

[10:57:03 AM](#)

The meeting was adjourned at 10:57 AM.