

**ALASKA STATE LEGISLATURE  
SENATE RESOURCES STANDING COMMITTEE**

January 28, 2011

3:31 p.m.

**MEMBERS PRESENT**

Senator Joe Paskvan, Co-Chair  
Senator Thomas Wagoner, Co-Chair  
Senator Bill Wielechowski, Vice Chair - via teleconference  
Senator Lesil McGuire  
Senator Hollis French  
Senator Gary Stevens

**MEMBERS ABSENT**

Senator Bert Stedman

**OTHER LEGISLATORS PRESENT**

Senator Fred Dyson  
Senator Cathy Giessel  
Senator Joe Thomas

**COMMITTEE CALENDAR**

Presentation: Kevin Banks, Director, Division of Oil And Gas,  
Department Of Natural Resources (DNR)

- HEARD

**PREVIOUS COMMITTEE ACTION**

No previous action to record

**WITNESS REGISTER**

KEVIN BANKS, Director  
Division of Oil and Gas  
Department of Natural Resources (DNR)  
Anchorage, AK

**POSITION STATEMENT:** Presented an overview of his division.

SENATOR FRED DYSON  
Alaska State Legislature  
Juneau, AK

**POSITION STATEMENT:** Asked oil and gas questions relative to Mr. Banks' presentation.

**ACTION NARRATIVE**

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**CO-CHAIR WAGONER** called the Senate Resources Standing Committee meeting to order at 3:31 p.m. Present at the call to order were Senators French, McGuire, Co-Chair Paskvan and Co-Chair Wagoner.

**Presentation: Kevin Banks, Director, Division of Oil and Gas,  
Department of Natural Resources (DNR)**

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KEVIN BANKS, Director, Division of Oil and Gas, Department of Natural Resources (DNR), presented an overview of his division. He stated that in 2010, the Division started to develop a strategic plan. They have ninety staff, and they need to act consciously and make sure appropriate people have vetted important decisions and reached a consensus. At the same time, he noted, they must be conscious of the impact of their decisions on revenue and development.

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SENATOR GIESSEL arrived at the meeting.

MR. BANKS pointed out that the division is told what it needs to do by statute, and makes decisions that affect the whole state. He said they want to maximize development of resources for the greatest benefit of all Alaskans, and the economically efficient recovery of resources; the Conservation Division, on the other hand, seeks to develop resources with the least surface disruption.

CO-CHAIR PASKVAN asked about interplay of the two.

MR. BANKS answered that normally units are formed to assure maximum recovery of the resource. He stated he must assure facilities are used efficiently, and must also look at plans of operation. He noted that if you thought of the state as a producer, it would be number four as a royalty producer.

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MR. BANKS said the Petroleum Systems Integrity Office (PSIO) was added to the division and relies on it for internet technology and administrative support, but has its own budget. He said that it may be considered an added layer of regulatory impact, but it

tells oil companies what they are capable of - and responsible for - developing resources safely.

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SENATOR STEVENS joined the committee.

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SENATOR WIELECHOWSKI joined the meeting via teleconference.

MR. BANKS explained the division's workflow design.

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CO-CHAIR PASKVAN asked when he anticipated the final strategic plan would be released.

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MR. BANKS responded that when the new commissioner completes his transition, a document should be available. He explained that resource evaluation completed a Cook Inlet gas supply study last December, which only covers existing fields. The study examines the potential for additional gas from the existing fields, and will reveal how much it would cost to develop those fields.

MR. BANKS explained that once resources have been identified, the leasing staff begins the process of making those lands available in a bonus bid auction as required by law. The process includes development of a best interest finding, a complicated document. He noted the division holds leases sales two times a year.

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SENATOR DYSON asked if the state's jurisdiction starts at the offshore islands in the Beaufort Sea or from the existing changing coastline.

MR. BANKS answered the islands count, and sometimes the coast does, depending on whether the islands are submerged or not.

SENATOR DYSON asked if we have a contest with the federal government over that.

MR. BANKS replied there's always potential for disagreement, but he wouldn't anticipate it becoming a serious problem. Part of the North Star unit is in federal land, and the division is in intense discussion with the developer and the federal government about that.

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MR. BANKS said that the royalty accounting staff has created an electronic filing process, and most lessees pay online. The division is able to validate those revenues in an audited form.

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CO-CHAIR PASKVAN asked about the recent Department of Revenue (DOR) report concerning the need for a central data base to analyze capital expenditure monies. He asked if the division's system is different.

MR. BANKS replied their system is different because the Department of Revenue has to track costs and the DNR does not; instead, the DNR is interested in leases and calculation of royalty. They manage for ownership issues and assign ownership.

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He stated the division's staff audits state and federal royalty by arrangement, and that audit claims in the amount of \$33 million are currently outstanding.

CO-CHAIR PASKVAN asked, in trying to understand the distinction between DOR and DNR and ACES audits, how current is DNR?

MR. BANKS replied that the division's audits aren't going as fast as he would like them to. They have been in the state of catch up for quite a while; there is some potential for shared information between DNR and DOR, particularly measuring production data. As the automation of those systems improves, they will automatically share that information.

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CO-CHAIR PASKVAN asked what audits typically show.

MR. BANKS answered that in most cases they are auditing for increased value in royalty, although sometimes they identify problems with the way 20-year old agreements are working.

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He then explained that the Gap analysis is designed to find where the state has overlap in upstream issues. It is largely complete, and there is a list of corrective actions that has been submitted to the Natural Resources, Department of Law Subcabinet. The subcabinet is preparing recommendations for the governor.

CO-CHAIR PASKVAN asked what is meant by "integrity events."

MR. BANKS answered that integrity events typically occur because some corrosion inspection is missing in the management plans of companies operating the equipment. The division is seeking the root causes of integrity events; they get phone calls from employees working for the companies, raising concerns. The department looks at the concerns.

CO-CHAIR PASKVAN asked what has been the success of an employee calling in.

MR. BANKS answered they haven't had a lot of valid calls, but enough to raise issues. It is usually enough to discuss with the operator. Often an employee will see something; for instance, people were concerned that Exxon was taking equipment away from Point Thomson. But they discovered that was not the case.

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CO-CHAIR PASKVAN asked how aware employees are of a number to contact.

MR. BANKS said the division has it on their website, but probably it's not widely known.

[4:02:23 PM](#)

SENATOR DYSON asked about drilling for hydrates and new technology.

MR. BANKS explained that hydrates are highly experimental. No one has effectively figured out how to produce them. A test conducted in Canada lasted six days; hydrates form in an ice crystal cage (methane molecule) at a specific range of pressure and temperature. On the North Slope, those pressures and temperatures form at a very shallow level, below the existing infrastructure. The USGS has estimated 85 trillion cubic feet of technically recoverable gas from hydrates in the area around the existing infrastructure. They have known that hydrates are a drilling hazard, which also could provide a method of recovering hydrates; as wells are drilled through the hydrates, the methane is released and could cause hydrate gas to be kicked into the well. This occurs when the drilling muds are too warm and heat up the area around the well, or when pressure is relieved from the well. A third technique being studied is to inject co2 into a well to displace the methane molecules.

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MR. BANKS further stated the USGS is proposing drilling a well at Prudhoe Bay to try some new techniques.

SENATOR DYSON asked how deep those wells would be.

MR. BANKS said he wanted to get a better answer, but he thought about five thousand feet.

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SENATOR FRENCH asked what is happening with heavy oil production on the North Slope.

MR. BANKS answered that heavy oil has been produced for some time, mostly at Milne Point, using pumps at the bottom of the wells. The issue has been how to get production without a lot of sand. They have been producing oil from Schrader Bluff for the last ten years, and West Sak is another source of heavy oil from the same structure.

He also noted that BP is experimenting with a CHOPs heavy oil producing system where they will produce the sand and remove it at the surface. It's very expensive, but is a tremendously prolific resource.

SENATOR FRENCH asked how far along it is. Is it permitted?

MR. BANKS answered yes.

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SENATOR WIELECHOWSKI asked about the Cook Inlet time table for production.

MR. BANKS said he didn't have an estimate off-hand for oil production, but the division has an estimate of gas potential in Cook Inlet; numbers are not in the trillions. The USGS is about to complete a resource assessment of Cook Inlet that will go after a more sophisticated estimate for undiscovered technically recoverable resource. He believes there are reserves of 1 trillion to 3 trillion cubic feet of gas in undiscovered resources.

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SENATOR WIELECHOWSKI asked how many acres are leased by the North Slope in Cook Inlet that are not currently being developed, and do we have tools to estimate rates of return on those fields under a different tax structure.

MR. BANKS said that is a difficult question, and he would respond to it later.

SENATOR WIELECHOWSKI said he heard from various producers and explorers that they would develop more fields with a change in tax structure.

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SENATOR MCGUIRE asked Mr. Banks to comment on North Slope shale.

MR. BANKS replied that it is definitely worth paying attention to.

CO-CHAIR PASKVAN said they are hoping to have a presentation on shale oil in 3-4 weeks.

SENATOR FRENCH asked for an update on ConocoPhillips getting the permit for crossing the Coleville River.

MR. BANKS answered that higher-ups in the Corps have remanded the decision to revisit their previous decision. There was concern about burying a pipe rather than letting it cross over the river, and ConocoPhillips is still waiting for a decision.

SENATOR FRENCH asked if the long-time future development of NPRA demands a bridge at some point.

MR. BANKS answered he couldn't agree more; three quarters of gas is in the Arctic and a crossing is essential.

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SENATOR FRENCH noted that sometimes the public has misconceptions on how ACES applies to different sections of land.

MR. BANKS responded that the tax system applies to on-shore federal land, including NPRA. Alaska shares in royalties from the NPRA, but those revenues are dedicated by the federal government to local impact funding. The current status of ANWR is that the state would receive ninety percent of the royalties from development of ANWR. In attempts to gain approval to open ANWR, our delegation has been willing to accept fifty percent, but that hasn't happened. The OCS provides a minimal share of royalty sharing.

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SENATOR DYSON noted that onshore states in the Gulf of Mexico have negotiated with the federal government to get more revenues because of onshore impacts. Would those negotiations include us?

MR. BANKS said they would not.

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CO-CHAIR PASKVAN asked if Mr. Banks could review commercial achievements in 2010, such as completion of a study on the impact of shale gas on gas pricing in the lower 48, and other items.

MR. BANKS stated that preliminary economic studies for a bullet line are being conducted with a fresh look at costs from the Alaskan Development Corporation. Shale gas prices and impacts work was conducted by Black and Veatch, and that study is available on the DNR website. Completion of regulations governing calculation of royalty value, and implementing the aspects of AGIA that called for calculating how royalty in kind and royalty in value would be calculated, is not complete.

CO-CHAIR PASKVAN asked if those were the regulations that assume a coupled tax structure for oil and gas.

MR. BANKS said it simplified the calculation.

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CO-CHAIR PASKVAN said when it comes to audits, the proposed tax bill shortens the statute of limitations and asked what the oldest data is that has not yet been audited.

MR. BANKS replied that the state is losing royalty revenue as they speak - every month, as it slips off the six-year statute of limitations. Several audits should have been done, but were not.

SENATOR DYSON asked how close the Anchorage area got several weeks ago to not having enough gas pressure to run their power plants.

MR. BANKS responded that MLP was the one company that had trouble, and they fired up their diesel plant; the other utilities could be supplied from other sources.

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SENATOR DYSON asked if it was lack of gas or a problem with the distribution system.

MR. BANKS replied that it was a question of who owned the gas supply and who was obligated to deliver it. He noted that the players play well together - getting gas to where it needs to be, and then working the details out later.

SENATOR DYSON asked if there was enough gas to supply the region physically.

MR. BANKS answered that there was enough gas, but it was an ownership issue.

CO-CHAIR WAGONER thanked Mr. Banks and finding no further business to come before the committee, adjourned the meeting at 4:35 p.m.