

**ALASKA STATE LEGISLATURE
HOUSE JUDICIARY STANDING COMMITTEE**

February 16, 2018

1:03 p.m.

MEMBERS PRESENT

Representative Matt Claman, Chair
Representative Jonathan Kreiss-Tomkins
Representative Chuck Kopp
Representative Charisse Millett (alternate)
Representative Louise Stutes (alternate)

MEMBERS ABSENT

Representative Zach Fansler, Vice Chair
Representative Gabrielle LeDoux
Representative David Eastman
Representative Lora Reinbold

COMMITTEE CALENDAR

HOUSE BILL NO. 330

"An Act authorizing the commissioner of natural resources to disclose confidential information in an investigation or proceeding, including a lease royalty audit, appeal, or request for reconsideration and issue a protective order limiting the persons who have access to the confidential information."

- HEARD AND HELD

PREVIOUS COMMITTEE ACTION

BILL: HB 330

SHORT TITLE: DNR: DISCLOSURE OF CONFIDENTIAL INFO

SPONSOR(s): RULES BY REQUEST OF THE GOVERNOR

02/05/18	(H)	READ THE FIRST TIME - REFERRALS
02/05/18	(H)	JUD, RES
02/16/18	(H)	JUD AT 1:00 PM GRUENBERG 120

WITNESS REGISTER

ED KING, Legislative Liaison
Commissioner's Office
Department of Natural Resources
Anchorage, Alaska

POSITION STATEMENT: During the hearing of HB 330, offered a PowerPoint presentation titled, "Protective Orders, HB 330" and presented a sectional analysis.

PETER CALTAGIRONE
Assistant Attorney General
Natural Resources Section
Anchorage, Alaska

POSITION STATEMENT: During the hearing of HB 330, answered questions.

ACTION NARRATIVE

[1:03:36 PM](#)

CHAIR MATT CLAMAN called the House Judiciary Standing Committee meeting to order at 1:03 p.m. Representatives Claman, Kopp, Stutes (alternate for Representative Fansler), and Millett (alternate for Representative Reinbold) were present at the call to order. Representative Kreiss-Tomkins arrived as the meeting was in progress.

HB 330-DNR: DISCLOSURE OF CONFIDENTIAL INFO

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CHAIR CLAMAN announced that the only order of business would be HOUSE BILL NO. 330, "An Act authorizing the commissioner of natural resources to disclose confidential information in an investigation or proceeding, including a lease royalty audit, appeal, or request for reconsideration and issue a protective order limiting the persons who have access to the confidential information."

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ED KING, Legislative Liaison, Commissioner's Office, Department of Natural Resources, advised that HB 330 is viewed as the "Protective Orders Bill." The title of this bill is "DNR disclosure of confidential data," which may raise alarm bells for some people. Mr. King turned to the PowerPoint presentation titled, "Protective Orders, HB 330" slides 1-3, and advised that the intent of HB 330 is not to publish confidential data for the general public to consume. This protective order bill directs that the confidential information would be disclosed only to appellants or participants in an audit in order to provide the

complete administrative record in the adjudication of an appeal, he explained.

MR. KING advised that the Department of Natural Resources (DNR) is the land manager of the lands of the state, the Division of Oil & Gas is housed under DNR and it is responsible for the management and administration of the oil & gas leases in the state. Within the Division of Oil & Gas, a section performs audits to make certain the state receives its due share under its lease agreements. He pointed out that the lease agreements contain terms requiring payments to the state, and every month the leaseholder provides a report to the state calculating the amount of the royalty or net profit share payments due to the state. The audit section ascertains whether those payments were correctly calculated and the state received its appropriate amount of funds, he said.

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MR. KING noted that prior to 2003, the royalty audit section was housed under the Department of Revenue (DOR), and under House Bill 246 [passed in the Twenty-Third Alaska State Legislature], those functions were moved to DNR to perform its own audits. Subsequent to the 2003 move, 91 audits have been conducted and have generated additional payments to the state in the amount of approximately \$270 million. Those payments, he explained, are usually the result of an error on one of the reports, usually on something associated with either transportation deductions or the price used in the calculation of the royalty payments. There are four methods within the state's lease contracts to calculate the appropriate payments to the state, and the highest of those four calculations is the amount due to the state. The first method, he offered, is simply the price the company received for the oil it sold from the lease; the second is the volume weighted average of the three highest (indisc.) prices; and the other two calculations are based on "posted prices," which are not actually applicable to Alaska. Generally, he remarked, the first two computation methods are used and the highest of those two computations generate the appropriate payments to the state under its lease terms.

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MR. KING turned to slide 4, titled "Why HB 330?" and advised that this legislation is important to DNR because the companies provide royalty reports to DNR, and it calculates the average of those highest three payments to determine the appropriate

payment. He explained that when a company provides its royalty reports to the state, the company bases those payments on what it received, and that is not necessarily what the lease terms will dictate. However, he explained, because those contracts between the leaseholder and its purchasers are confidential under current law, DNR cannot provide those confidential contracts to the company being audited wherein DNR is evaluating these additional royalty assessments. Currently, seven royalty audits are pending in the commissioner's office and are worth approximately \$39 million, if all are adjudicated in the state's favor. In recent years, some of these leaseholders have objected to the state disclosing that confidential data to other leaseholders, he advised. Therefore, the Department of Natural Resources (DNR) has experienced situations where even though it believes it has the authority to prosecute the lease terms, if there was a court ruling against DNR's ability to do so, it would carry criminal charges for the person disclosing that confidential data. Out of an abundance of caution, he advised, DNR is asking for explicit authority to disclose that information to certain parties during an appeal because that information is necessary to fully adjudicate that appeal.

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MR. KING explained that the major issue relates to those seven currently pending and future audits, and this bill allows DNR to more quickly adjudicate those additional revenues for the state. He offered that DNR realized that, occasionally, an appeal was before the commissioner and due to the confidential data contained within the record, the appeal could not be fully adjudicated. He described that it is a "very rare circumstance," and opined that it has only taken place twice in the last 10-years. These situations, he explained, are when a third party, outside of a unit agreement, brings an appeal to the commissioner's attention because it had a financial interest in the decision. Thereby, causing DNR to go to court to obtain a protective order allowing that information to be disclosed. The manner in which HB 330 is written, allows DNR to issue that protective order in those rare circumstances, as well.

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MR. KING turned to slide 5, titled "What are Protective Orders" noting that the slide discusses a confidentiality agreement the commissioner can issue, and companies are compelled to enter into that agreement. He acknowledged that this might sound as though it is "a very forceful tool," but it is actually a tool

many agencies utilize within the state, such as the Department of Fish & Game (ADF&G), and the Department of Administration (DOA). He reiterated that both of these departments have the ability to issue these protective orders, and the Department of Revenue (DOR) has the ability to disclose confidential data in the same manner discussed here when adjudicating appeals on tax issues. Of course, he said, courts issue protective orders when situations arise where the lack of the confidential data would prevent the case from being completed. It is a common tool, he described, used by courts, arbitrators, and many other agencies, and DNR is not asking for anything "that is too much beyond that." It would give DNR the ability to provide confidential information contained in the record solely to those parties directly interested as an appellant and, he stated, only under the protective order limiting the ability to utilize that information. He reiterated that DNR will not disclose the confidential information to the general public because DNR is under a strict and limiting condition. Under the current bill language, it is discretionary and the commissioner can issue those protective orders only when deemed necessary to complete the appeal process, he related.

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MR. KING turned to slide 6, titled, "HB 330" sectional analysis, and explained that Section 1 is the meat of the bill wherein it grants an additional duty and power to the commissioner. He referred to HB 330, [AS 38.05.020(b)(15), page 3, lines 25-30 and page 4, lines 1-4] and advised that DNR adds an additional paragraph authorizing the commissioner to issue these protective orders if deemed necessary. The paragraph also provides that the company's confidential data to be released to these other parties must have an opportunity to be heard, which is identical language to DOR under AS 43.55.040. He said that AS 38.05.020(b) allows the commissioner to issue that protective order limiting the person who may have access to the information, and the purposes for which that information can be used.

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MR. KING advised that Sections 2-3 are conforming language to include that additional provision within the existing statutes.

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REPRESENTATIVE MILLETT surmised that when it comes to what DNR would be using the protective order for, it would be a lease audit, an appeal on royalty rights. She said she was unsure about the requests for reconsideration, noting there were two in the last 10-years.

MR. KING responded that there have been two rare situations where a non-royalty issue was brought forward requiring the disclosure of confidential data. Both of those situations took place in the Ninilchik unit, they went to court and one case is currently pending litigation, he offered. The royalty audit issue is the real issue DNR is attempting to address here so DNR does not have to continue to report when situation do arise or come back before the legislature for this additional authorization at a later date.

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REPRESENTATIVE MILLETT surmised that the royalty audit would be when the state is in dispute with a company regarding what the company owed the state. In the event a unit had two or three different producers, which is common in Alaska, that information would have to be compared in that unit to other royalty. She asked whether there is any concern through this bill about disclosure and what each producer is paying for competitive reasons.

MR. KING answered that, from DNR's perspective, it does not believe there are any concerns. The Department of Natural Resources (DNR) does not view this idea as violating anti-trust laws, allowing collusion, or something along those lines, as being a relevant point here. These are audits of issues that happened in the past and are contracts from the past wherein DNR discloses one contract to another party for the purposes of determining how much royalty was due three-to-six years ago. Therefore, he pointed out, the release of that confidential data is different than getting two people in a room to collude and try to drive prices toward a certain market level. This legislation is different than what an anti-trust type argument would require, and DNR does not believe there are any reasons why, for competitive reasons, the ability to disclose would somehow injure one of the parties. In the event there are issues, he advised that the party has the opportunity to bring those issues to the attention of the commissioner prior to that protective order being issued and the confidential data disclosed. He pointed out that if DNR did have to go to court, this protective order idea is how the court would resolve the

issue, and when the court issues a protective order, no colluding or anti-trust issues are brought forward in those cases.

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REPRESENTATIVE MILLETT related that she understands how a court would deem a protective order, except the discussion here is about a commissioner who could change every four-years or more often. She surmised that DNR's problem is that it just does not want to go to court every time it wants a protective order to disclose data. She asked whether DNR is anticipating higher audit disputes in the future, and what is the genesis of the bill.

MR. KING replied that DNR currently has seven audits pending that are related to this issue, and that DNR does believe it has the authority to disclose the confidential data that is the part of the audits. However, he said, due to a statute maintaining that the disclosure of confidential data carries a criminal penalty, DNR is hesitant to enforce that clause in the lease simply because it may provide some type of criminal charge for DNR's employees. One way to resolve this issue would be for explicit authority from the legislature to release confidential data, another option is to prosecute the lease terms and "do it" without the explicit authority, or DNR could continue going to the court requesting a protective order, he explained. It is DNR's belief that HB 330 is the most expeditious manner in which to resolve the immediate issues, and in the future, he said.

[1:20:03 PM](#)

REPRESENTATIVE KOPP asked whether this legislation solely discusses producers.

MR. KING responded that the confidential data would almost exclusively come from a leaseholder, it would be a producer of oil and gas, and the language is general enough that it could include other leases DNR holds. This could cover some circumstance in the future, for example, a mining lease with confidential data, and an appeal from a third party. He related that that type of situation does not exist currently, but it could theoretically, and that he guesses he would say yes, that it is the producers' data, generally speaking.

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REPRESENTATIVE KOPP surmised that each producer is currently obligated to share their price information with the Division of Oil & Gas via the lease provisions.

MR. KING answered in the affirmative.

[1:21:15 PM](#)

REPRESENTATIVE KOPP surmised that the discussion here is what value is used to compute the royalty due under the lease. He further surmised that the reason DNR needs to share confidential information with the producer who "disagreed with the audit," is because that determination is made on the average price of other producers and those other producers may not want that information disclosed due to the competitive advantage of the information. He asked whether that is the only way, set out in the law, for DNR to establish what the value is that is owed under the audit.

MR. KING answered that Representative Kopp was correct.

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CHAIR CLAMAN clarified that it is DNR's routine practice to audit "pretty much every royalty payment." In order to audit a company effectively, DNR must have access to information from the producer being audited and may also need information from another producer not being audited. Information from that producer's data is partially how DNR determines whether the royalty payments were correct for the producer being audited, he commented.

MR. KING clarified that the division already has the confidential data from all of the leaseholders and it is not compelling a company to provide additional data.

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CHAIR CLAMAN offered a scenario in which Company A is being audited and Company B's information is important to performing the audit correctly. Company A needs Company B's information, which it otherwise would not have, to complete the audit process correctly, he asked.

MR. KING answered that Chair Claman was correct.

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CHAIR CLAMAN noted that before a protective order would be entered, he surmised that these are protective orders that must be agreed to by the producers, and it not where DNR can unilaterally impose the protective order.

MR. KING explained that under current law and processes, DNR does go to the producers requesting a confidentiality agreement in order to share the data. The issue is when the producers refuse to sign the confidentiality agreement that the problem arises, and this bill would allow DNR to enter into that protective order and disclose that information without the permission of the producer.

CHAIR CLAMAN asked whether it is the producer that is not a party to the audit.

MR. KING replied that it is the owner of the confidential data.

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CHAIR CLAMAN surmised that this is confidential data of the party that is not being audited. Under this law, he commented, the company not being audited would be able to register its objections with DNR and the department would decide as it deemed fit.

MR. KING said that Chair Claman was correct.

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CHAIR CLAMAN added that this legislation would give DNR authority to [release the confidential data], and he asked whether, before the protective order took effect, the company not being audited would have the option of appealing that decision to the court.

MR. KING deferred to Peter Caltagirone, Department of Law (DOL).

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PETER CALTAGIRONE, Assistant Attorney General, Natural Resources Section, explained that when the information being discussed here is to be disclosed, the unaudited producer receives notice that its information will be disclosed pursuant to the terms of a protective order. He explained that there is a period of time between when it received notice and the information was

disclosed, and within which time it could register its objections to the division.

CHAIR CLAMAN asked that after the company registered its objection with the division, and the division decided to proceed with the protective order allowing the use of the unaudited company's confidential information, whether the company had the option of appealing that decision.

MR. CALTAGIRONE responded that the unaudited company would have to petition the court.

CHAIR CLAMAN agreed, and he asked whether the company would have the option, if unhappy with the division's decision, to petition the court for a review of that administrative decision by DNR.

MR. CALTAGIRONE said that Chair Claman was correct.

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REPRESENTATIVE MILLETT said, "That's what they do now," and noted confusion because that is the current process.

CHAIR CLAMAN said that he thought DNR was not issuing protective orders currently and it had to go to the court each time, and this bill gives it the authority to issue a protective order.

MR. KING opined that Representative Millett was referring to the fact that if DNR followed the chain of events "that were just laid out, then we might not be any better off than we are today." He then deferred to Mr. Caltagirone.

MR. CALTAGIRONE asked Chair Claman to repeat the question.

CHAIR CLAMAN asked what happens today when an unaudited company refuses to agree to allow confidential information shared with the company being audited.

MR. CALTAGIRONE responded that today, the unaudited company receives a notice letter that its information will be disclosed. In the event the unaudited company so chose, it could contact the Division of Oil & Gas, state its objections, and if those objections could not be resolved, the unaudited company would seek an injunction from the court preventing its information from being disclosed.

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CHAIR CLAMAN surmised that the department does not have to go to the court to obtain the protective order, and that the department is essentially going forward. It is simply a question as to whether the company wants to file suit to stop the department from going forward, he commented.

MR. CALTAGIRONE clarified that the Division of Oil & Gas is not simply going forward, the division issues a letter to the audited company advising that the information at issue from the other producers will be disclosed, but only if the audited company executes a confidentiality agreement. Essentially, he explained, the confidentiality agreement lays out the same terms and protections as a protective order. The division advises the unaudited company that its information will only be disclosed "if they sign a confidentiality agreement." In short, he said, the confidentiality agreement limits who can see the information, the purpose the information can be used for, and it limits the state's liability if the audited company somehow missuses the information that is disclosed.

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REPRESENTATIVE STUTES asked for clarification because she thought Mr. King had said that the contracts with the producers currently have that clause in it, but there is a statute that precludes that clause, and the concern was the effect of the statute even though the division has the ability, based on the contracts, to disclose. She said she was under the impression that HB 330 would address the concern with the clause in the statute, even though, currently the contracts the division enters into allow it to disclose information.

MR. KING said he believes Representative Stutes is correct, the contracts do have the clause and enforcing the contract requires that this disclosure be allowed. He explained that when a company paid the division a royalty payment based on a \$50 barrel of oil, and another leaseholder paid the division a royalty payment based on a \$60 barrel of oil, the division would then send a bill for the difference to the company that received \$50 per barrel. He offered a scenario of the \$50 a barrel company going to the division and asking how it would know that what the division billed it was accurate, the division would respond that the bill is based on the contract from this other company, and the billed company would ask to see that contract, but the division cannot show it to them because it is confidential data. It is the division's belief that it has

authority, under enforcement of that contract, to disclose. Except, he reiterated, a confidentiality clause in statute carries a criminal penalty and if for some reason a court decided against the division, then the division's employees may be subjected to a criminal penalty. He offered that the Department of Revenue (DPR) has a statute that read, "for these circumstances you have explicit authority from the legislature" to get around that statute. The Department of Natural Resources (DNR) does not have that provision in its statutes, and that is what it is trying to clean up today.

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CHAIR CLAMAN opened public testimony on HB 330. After ascertaining no one wished to testify, closed public testimony on HB 330.

[1:34:36 PM](#)

REPRESENTATIVE KOPP commented that he would have preferred to have heard from someone in the industry and the producers, but "apparently, they did not feel that was necessary." He related that he is glad to see that the [Division of Oil & Gas] has this fiduciary duty to make certain the appropriate revenue is collected in every lease agreement. He pointed to the sensitivity in this issue, commenting that if the only vehicle available to come to an appropriate evaluation of the state royalty owed requires a competitive disclosure, and if the company's competitor knows the price point, the competitor can pretty much build the first company's whole portfolio. Frankly, he said, "we all benefit" from a competitive environment and he understands why this is a sensitive issue. When the court is involved, he pointed out, it is a neutral decider of facts whereas perhaps the individual could be considered favorable one time and unfavorable another time. He said he guessed there is some weighing of the balance in how to de-politicize these orders, and also how to protect the private market information of these companies so they are not compromised.

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CHAIR CLAMAN noted that there is an oil company representative in the audience who, obviously, prefers not to testify. He commented that the perspective of the industry on this legislation is important and his office will contact representatives as to whether they have an objection to the bill and address the confidential information issue. Previously, he

said, he had conversation with folks, including industry folks, who commented that the price information, although confidential, is not especially sensitive because it is pretty well known. Although, when getting into things such as geologic data and proprietary information, it starts becoming more important as to what is known and not known, he said.

[1:38:10 PM](#)

REPRESENTATIVE MILLETT suggested asking someone from DOR Tax Division to speak to the committee about how it adjudicates decisions on appeal.

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CHAIR CLAMAN related that DOR would be asked to attend the next hearing. He said that one of the points of this bill is for DNR to be on the same footing as other departments when pursuing these types of audits. The Department of Natural Resources (DNR) is not attempting to be put in a position that is more advantageous than other departments in the state, he pointed out.

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REPRESENTATIVE KREISS-TOMKINS said he would appreciate hearing the industry's perspective on this bill and echoed Representative Millett's comments. Particularly, he said, if DNR is trying to create a parallel in the statutes between DNR and DOR, it would be helpful to learn how this works at DOR and to possibly extrapolate any potential pitfalls.

[HB 330 was held over.]

[1:39:47 PM](#)

ADJOURNMENT

There being no further business before the committee, the House Judiciary Standing Committee meeting was adjourned at 1:39 p.m.