Introduced: 2/17/78
Referred: Resources and Finance

IN THE HOUSE

BY THE RULES COMMITTEE BY REQUEST OF THE GOVERNOR

CCS CS HOUSE BILL NO. 854 (Finance)(Rules)2d

IN THE LEGISLATURE OF THE STATE OF ALASKA

TENTH LEGISLATURE - SECOND SESSION

A BILL

For an Act entitled: "An Act relating to the leasing and exploration of state land for oil and gas development."

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

Section 1. AS 38.05.180 is repealed and re-enacted to read:

Sec. 38.05.180. OIL AND GAS LEASING. (a) The legislature finds that

(1) the people of Alaska have an interest in the development of the state's oil and gas resources to

(A) maximize the economic recovery of the resources;

(B) minimize the exploitation of these natural resources in protection of the public interest;

(C) maximize competition among parties seeking to explore and develop the resources;

(D) maximize use of Alaska's human resources in the development of the resources;

(2) it is in the best interests of the state to encourage an assessment of its oil and gas resources and to allow the maximum flexibility in the methods of issuing leases to

(A) recognize the many varied geographical regions of the state and the different costs of exploring for oil and gas in these regions;

(B) recognize the need for stimulating development in particular regions of the state;

(C) minimize the adverse impact of exploration, development, production, and transportation activity on the environment of the state;

(D) maximize state revenue from profitable oil and gas production, while minimizing revenue from unsuccessful exploration and from marginal economic oil and gas production.

(b) The commissioner shall prepare, review, revise, and maintain an oil and gas leasing program as follows:

(1) The leasing program shall be submitted to the legislature for its information within 10 days after the convening of each regular session of the legislature. The leasing program must indicate as precisely as practicable the size, timing, and location of leasing activity which the commissioner determines will best meet state needs for the following five-year period. The commissioner shall establish the timing and location of leasing, to the maximum extent practicable, so as to obtain a balance between the potential for environmental damage, the potential for the discovery of oil and gas and the potential for adverse impact on the local communities in the state.

(2) After the leasing program has been prepared by the commissioner, a lease shall be issued if it is for an area included in the leasing program; however, leasing may continue until January 1, 1980 or until a program is prepared, whichever is sooner, and leasing under (t) of this section may be excepted from the leasing program if the commissioner finds it to be in the best interests of the state.

(3) The commissioner shall review the leasing program at least once each year, at which time he may revise and reapprove the program.

(4) The commissioner shall, by regulation, establish procedures for

(A) receipt and consideration of nominations for any area to be offered for lease or to be excluded from leasing;

(B) public notice of and participation in development of the leasing program;

(C) review by federal and local government agencies which may be affected by the proposed leasing;

(D) consultation with local governments, oil and gas lessees and permittees, and others engaged in activity on state land;

(E) coordination of the program with the management program developed under the Coastal Zone Management Act of 1972; and

(F) the use of the capabilities and resources of all state agencies in preparation of the leasing program, and for the provision by agencies to the commissioner of any nonproprietary information he requests.

(5) At the time the commissioner submits the leasing program to the legislature, as required by (1) of this subsection, he shall also submit to the legislature for its information, a report concerning the use of the various leasing methods provided for in (c) of this section. The report must include:

(A) the schedule of all lease sales held during the preceding calendar year and the bidding method or methods utilized;

(B) the schedule of all lease sales to be held the following year and the bidding method or methods to be used;

(C) the benefits and costs associated with conducting lease sales using the various bidding methods;

(D) the reasons why a particular bidding method was selected; and

(E) if applicable, the reason why more than 50 per cent of the area leased in the upcoming year was or is to be leased under one particular bidding method.

(c) The commissioner may issue oil and gas leases on state land to the highest responsible qualified bidder determined by competitive bidding under regulations adopted by the commissioner. Bidding may be by sealed bid or according to any other bidding procedure the commissioner determines is in the best interests of the state. Whenever, under any of the leasing methods listed in this subsection, a royalty share is reserved to the state, it is free of all lease or unit expenses, including but not limited to separation, cleaning, dehydration, gathering, salt water disposal, and preparation for transportation off the lease or unit area. Following a pre-sale analysis, the commissioner may choose at least one of the following leasing methods:

(1) bonus bidding

(A) a cash bonus bid with a fixed royalty share reserved to the state of not less than 12 1/2 per cent in amount or value of the production removed or sold from the lease or unit area encompassing the lease;

(B) a cash bonus bid with a fixed royalty share reserved to the state based on a sliding scale according to volume of production but in no event less than 12 1/2 per cent in amount or value of the production removed or sold from the lease or unit area encompassing the lease;

(2) royalty bidding

(A) a fixed cash bonus with a royalty share reserved to the state as the bid variable but not less than 12 1/2 per cent in amount or value of the production removed or sold from the lease or unit area encompassing the lease;

(B) a fixed cash bonus with a royalty share reserved to the state based on a sliding scale according to the volume of production as the bid variable but not less than 12 1/2 per cent in amount or value of the production removed or sold from the lease or unit area encompassing the lease;

(3) net profit bidding

(A) a cash bonus bid with a fixed royalty share reserved to the state of not less than 12 1/2 per cent in amount or value of the production removed or sold from the lease or unit area encompassing the lease and a fixed share of the net profit derived from the lease of not less than 30 per cent reserved to the state;

(B) a fixed cash bonus with the share of the net profit derived from the lease reserved to the state as the bid variable;

(C) a fixed cash bonus with a fixed royalty share reserved to the state of not less than 12 1/2 per cent in amount or value of the production removed or sold from the lease or unit area encompassing the lease with the share of the net profit derived from the lease reserved to the state as the bid variable;

(D) the share of the net profit derived from a lease reserved to the state under this subsection is royalty sale proceeds for the purpose of the Alaska Permanent Fund under AS 37.10.065;

(4) a work commitment bid with a fixed cash bonus, or a fixed royalty or a fixed sliding scale royalty or a fixed net profits share reserved to the state, or any combination of these methods, at the discretion of the commissioner, with a work commitment stated in a dollar amount as the bid variable; however, in no event may a royalty

share reserved to the state be less than 12 1/2 per cent in amount or value of the production removed or sold from the lease or unit area encompassing the lease.

(d) To prolong the economical life of an oil and gas field, the commissioner shall adopt regulations for all bidding methods to allow reduction of royalty to compensate for increasing costs in the later stages of production decline. The commissioner may grant such a reduction of royalty so long as the reduced royalty begins no sooner than two years after initial production from the lease.

(e) The commissioner may, in his discretion, defer any part of the payment of a cash bonus, under (c) of this section, according to a schedule announced at the time of the announcement of the lease sale, but such payment shall be made in total no later than five years from the date of the lease sale.

(f) The commissioner may withhold acreage from leasing in a particular lease sale.

(g) The commissioner shall adopt regulations governing the calculation of net profits for lease sales under (c)(3) of this section. In the event of any dispute between the state and a lessee concerning the calculation of the net profits under the regulation adopted under this subsection, the burden of proof is on the lessee.

(h) The commissioner shall adopt regulations governing the exploration work commitment leasing method under (c)(4) of this section. The commissioner shall require either (i) a cash deposit for 20 per cent of the work commitment or, (ii) a performance bond, in form and substance and with a surety satisfactory to the commissioner, in the principal amount of 20 per cent of the exploration work commitment assuring the commissioner that the commitment will be faithfully discharged in accordance with this section, the regulations, and the lease.

A lessee who fails to discharge a work commitment in its entirety is liable to the state for the undischarged portion of the commitment. At his discretion, the commissioner may terminate the work commitment if he finds that the work would be unnecessary or cumulative.

(i) At his discretion, the commissioner may enter into an agreement whereby, with the consent of the lessee, the state's royalty share of oil and gas production may be stored or retained in storage by the lessee, or the commissioner may enter into an agreement with one or more of the affected field lease holders to trade current royalty production from a field for a like amount, kind, and quality of future production, on the condition that the state receives back its stored or traded royalty share during the first half of the estimated field life or no later than 15 years after start of production, whichever is sooner.

(j) An oil and gas lease must cover a reasonably compact area not exceeding 5,760 acres, and must be for a period of five years. The commissioner may grant a lease for a term greater than five years but not to exceed 10 years, where he finds that the longer period is necessary to encourage exploration and development in areas where environmental conditions severely restrict operations. An oil and gas lease shall be automatically renewed if and for so long thereafter as oil or gas is produced in paying quantities from the lease or, if the lease is committed to a unit approved by the commissioner. A lease issued under this section covering land on which there is a well capable of producing oil or gas in paying quantities does not expire because the lessee fails to produce oil or gas unless the lessee is allowed reasonable time to place the well on a producing status. Upon renewal, the commissioner may increase lease rentals so long as the increased rental rate does not exceed 150 per cent of the rate for the preceding year. The commissioner may provide by regulation and in the lease that the lessee may earn production rights only to the depth drilled at the beginning of production from the lease. If drilling has commenced on the expiration date of the primary term of the lease and is continued with reasonable diligence, including such operations as redrilling, sidetracking, or other means necessary to reach the originally proposed bottom hole location, the lease continues in effect until 90 days after drilling has ceased and for so long thereafter as oil or gas is produced in paying quantities.

(k) The commissioner may establish by regulation that after a well has been plugged and abandoned, the rental rate which was in effect during the year of abandonment is maintained for the remainder of the term. Rental is payable in advance and continues until income to the state from royalty, net profit, or exploration work commitment exceeds rental income to the state for that year; after the rental income schedule has been exceeded for three consecutive years, the rental terminates. Oil and gas leases shall provide for payment to the state of rental on the following basis:

(1) for the first year, $1.00 per acre;

(2) for the second year, $1.50 per acre;

(3) for the third year, $2.00 per acre;

(4) for the fourth year, $2.50 per acre;

(5) for the fifth year, $3.00 per acre.

(l) Upon timely application as provided by regulation, the state may issue to the holder of a federal or private lease, a state shorelands lease covering land within the exterior boundaries of the federal or private lease which has been excluded on the basis of navigability or which is later administratively or judicially determined to be shoreland. The term of such a state shoreland lease shall be the same as the term of the federal or private lease, but may not exceed five years.

(m) To conserve the natural resources of all or a part of an oil or gas pool, field, or like area, whether or not the part is then subject to a cooperative or unit plan of development or operation, lessees and their representatives may unite with each other, or jointly or separately with others, in collectively adopting or operating under a cooperative or a unit plan of development or operation of the pool, field, or like area, or a part of it, when determined and certified by the commissioner to be necessary or advisable in the public interest. The commissioner may, with the consent of the holders of leases involved, establish, change, or revoke drilling, producing, rental minimum royalty, and royalty requirements of the leases and adopt regulations with reference to the leases, with like consent on the part of the lessees, in connection with the institution and operation of a cooperative or unit plan as he determines necessary or proper to secure the proper protection of the public interest. The commissioner may require oil and gas leases issued under this section to contain a provision requiring the lessee to operate under a reasonable cooperative or unit plan, and he may prescribe a plan under which the lessee must operate. The plan must adequately protect all parties in interest, including the state.

(n) A plan authorized by (m) of this section, which includes land owned by the state, may contain a provision vesting the commissioner, or a person, committee, or state agency with authority to modify from time to time the rate of prospecting and development and the quantity and rate of production under the plan. All leases operated under a plan approved or prescribed by the commissioner are excepted in determining holdings or control under sec. 140 of this chapter. The provisions of this section concerning cooperative or unit plans are in addition to, and do not affect AS 31.05.

(o) Producing acreage on a known geologic structure of a producing oil or gas field is excluded from chargeability as against the acreage limitation provisions of sec. 140 of this chapter.

(p) When separate tracts cannot be individually developed and operated in conformity with an established well-spacing or development program, a lease, or a portion of a lease, may be pooled with other land, whether or not owned by the state, under a communitization or drilling agreement providing for an apportionment of production or royalties among the separate tracts of land comprising the drilling or spacing unit when determined by the commissioner to be in the public interest. Operations or production under the agreement are considered as operations or production as to each lease committed to the agreement.

(q) The commissioner may, on conditions which he prescribes, approve drilling, or development contracts made by one or more lessees of oil or gas leases, with one or more persons, when, in his discretion, the conservation of natural resources or the public convenience or necessity requires it or the interests of the state are best served. All leases operated under approved drilling or development contracts, and interests under them, are excepted in determining holding or control under sec. 140 of this chapter. Drilling or development contracts may include, at the discretion of the commissioner, provisions authorizing the state to share in the costs of exploration.

(r) To avoid waste or to promote conservation of natural resources, the commissioner may authorize the subsurface storage of oil or gas whether or not produced from state land, in land leased or subject to lease under this section. This authorization may provide for the payment of a storage fee or rental on the stored oil or gas, or, instead of the fee or rental, for a royalty other than that prescribed in the lease when the stored oil or gas is produced in conjunction with oil or gas not previously produced in paying quantities.

(s) Each oil or gas lease issued by the state must contain a provision requiring the lessee to furnish the Department of Labor a quarterly report regarding the employment of state residents on the leased property. The commissioner of labor shall adopt regulations necessary to implement this subsection. No lease issued under this chapter is valid unless it contains provisions requiring the employment of qualified Alaska residents in accordance with AS 38.40.030, and complies in all respects with the requirements of ch. 40 of this title.

(t) Notwithstanding any other provision of this section, land which has been offered for lease within the previous five years but which received no bids at competitive sale may be, at the discretion of the commissioner, immediately offered for lease, under regulations adopted by him, upon terms appearing most advantageous to the state, including leasing noncompetitively. The commissioner shall use a sliding scale royalty based upon such formulae as he determines to be in the public interest but not less than 12 1/2 per cent at the beginning of production from the lease in amount or value of the production removed or sold from the lease or unit area encompassing the lease. A lease must provide for payment to the state of rental but need not adhere to the rental schedule in (k) of this section nor to the 5,760-acres-per-lease limitation in (j) of this section. The lease term may not exceed five years except as provided in (j) and (k).

(u) The commissioner may, by regulation, restrict joint bidding by major or multi-national oil and gas companies to encourage competition.

(v) The state has the right to purchase not more than 16 2/3 per cent of the volume of oil and up to 100 per cent of the volume of gas produced from a lease issued in accordance with this section, at the regulated price, or, if no regulated price applies, at the fair market value at the point of sale, except that any oil or gas obtained by the state as royalty or net profits shall be credited against the amount that may be purchased under this subsection. Oil and gas purchased under this section may be used by the state in the same manner as it uses its royalty oil and gas.

(w) A lessee or permittee conducting any exploration for, or development or production of, oil or gas on state land shall provide the commissioner access to all data obtained from that activity and shall provide copies of specific data, as the commissioner may request.

* Sec. 2. AS 38.05.135(b) is repealed and re-enacted to read:

(b) When minerals are to be leased, in addition to any other notice given, notice must also be given as provided in secs. 305 and 345 of this chapter.

* Sec. 3. AS 38.05.140(c) is amended to read:

(c) No person may take or hold at one time phosphate leases on state lands exceeding in the aggregate 10,240 acres. No person may take or hold sodium leases or permits during the life of sodium leases on state lands, exceeding in the aggregate acreage 5,120 acres, except that the commissioner may, where it is necessary in order to secure the economic mining of sodium compounds, permit a person to take or hold sodium leases or permits for up to 15,360 acres. No person may take or hold at any one time oil or gas leases exceeding in the aggregate 500,000 acres granted on tide and submerged lands, and 200,000 [500,000] acres on all land [LANDS] other than tide and submerged land [LANDS], including leases held both as lessee and under option or operating agreement from others. <u>A person has five years from the effective date of this Act to conform to the 200,000-acre upland limitation.</u> Where more than a single person holds an interest in an oil or gas lease, each person shall be charged only with that percentage of the total acreage which corresponds to its percentage share of the total beneficial interest in the lease.

* Sec. 4. AS 38.05.145(b) is repealed.