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request of the Governor

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1 IN THE HOUSE

BY THE RESOURCES COMMITTEE

2 SENATE CS FOR CS FOR HOUSE BILL NO. 854

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 TENTH LEGISLATURE - SECOND SESSION

5 A BILL

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

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

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 AS 38.05.180 is repealed and re-enacted to read:

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

11 that

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

14 (A) maximize the economic and physical recovery of the  
15 resources;

16 (B) maximize competition among parties seeking to ex-  
17 plore and develop the resources;

18 (C) maximize use of Alaska's human resources in the  
19 development of the resources;

20 (2) it is in the best interests of the state to encourage an  
21 assessment of its oil and gas resources and to allow the maximum flexi-  
22 bility in the methods of issuing leases to

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

26 (B) minimize the adverse impact of exploration, develop-  
27 ment, production, and transportation activity.

28 (b) The commissioner shall annually prepare and submit to the  
29 legislature, between the first and the 15th day of each regular legis-

1       lative session, a proposed oil and gas leasing program specifying as  
2       precisely as practicable the location of tracts proposed to be offered  
3       for oil and gas leasing during the third and fourth calendar years  
4       following the calendar year in which the proposed program is submitted  
5       to the legislature.

6               (c) Except as provided in (d) of this section, no oil and gas  
7       lease issued by the commissioner shall be valid unless it was included  
8       in a proposed leasing program submitted to the legislature during the  
9       third and fourth calendar years preceding the year in which the lease is  
10      issued, except that an area proposed for leasing in the fourth calendar  
11      year after the year in which the program is submitted to the legislature  
12      may be leased if the commissioner resubmits the area to the following  
13      regular legislative session.

14              (d) The commissioner may issue oil and gas leases in an area that  
15      has not been included in a leasing program submitted, in accordance with  
16      (b) of this section, to the legislature if

17              (1) the land to be leased was previously subject to a valid  
18      state or federal oil and gas lease; or

19              (2) the land to be leased is contiguous to land already under  
20      state, federal or private lease and the commissioner makes a written  
21      finding, after hearing, that leasing of the land would result in a  
22      substantial probability of early evaluation and development of the land  
23      to be leased; or

24              (3) the land to be leased is adjacent to land owned or con-  
25      trolled by another party on which a discovery of commercial quantities  
26      of oil or gas has been made, and where the commissioner finds, after  
27      hearing, that there is a reasonable probability that the land to be  
28      leased contains oil or gas in communication with the oil or gas dis-  
29      covered on the land of the other party.

1 (e) Simultaneously with submission of the leasing program required  
2 under (b) of this section, the commissioner shall submit to the legis-  
3 lature a report containing the following:

4 (1) the schedule of all lease sales held during the preceding  
5 calendar year, the bidding method or methods utilized, and an analysis  
6 of the results of the bidding;

7 (2) a description of all lease sales to be held during the  
8 current and next two succeeding calendar years and, if determined, the  
9 bidding methods to be used;

10 (3) the reasons a particular bidding method has been  
11 selected.

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

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

27 (2) a cash bonus bid with a fixed royalty share reserved to  
28 the state of not less than 12 1/2 per cent in amount or value of the  
29 production removed or sold from the lease and a fixed share of the net

1 profit derived from the lease of not less than 30 per cent reserved to  
2 the state;

3 (3) a fixed cash bonus with a royalty share reserved to the  
4 state as the bid variable but not less than 12 1/2 per cent in amount or  
5 value of the production removed or sold from the lease; royalty share as  
6 a bid variable shall be used only when the commissioner determines there  
7 is evidence that unleased acreage is subject to drainage by offsetting  
8 walls;

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

11 (5) a fixed cash bonus with a fixed royalty share reserved to  
12 the state of not less than 12 1/2 per cent in amount or value of the  
13 production removed or sold from the lease with the share of the net  
14 profit derived from the lease reserved to the state as the bid variable.

15 (g) The share of the net profit derived from a lease reserved to  
16 the state under (f) of this section is royalty sale proceeds for the  
17 purposes of the Alaska permanent fund under AS 37.10.065 and the Alaska  
18 renewable resources development fund under AS 37.11.020.

19 (h) The commissioner may include terms in any oil and gas lease  
20 imposing a minimum work commitment on the lessee. These terms shall be  
21 made public before the sale, and may include appropriate penalty pro-  
22 visions to take effect in the event the lessee does not fulfill the  
23 minimum work commitment.

24 (i) The commissioner may provide for the establishment of an  
25 exploration incentive credit system under which a lessee of state land  
26 drilling an exploratory well on that land may earn credits based upon  
27 the footage drilled and the region in which the well is situated. The  
28 commissioner may also provide for credits to be earned by persons per-  
29 forming geophysical work on state land, if that work is performed during

1 the two seasons immediately preceding an announced lease sale and on  
2 land included within the sale area and the geophysical information is  
3 made public following the sale. Credits may not exceed 50 per cent of  
4 the cost of the drilling or geophysical work. Credits may be used  
5 during a limited period established by the commissioner and may be  
6 assigned during that period. Credits may be applied against (1) oil and  
7 gas royalty and rental payments payable to the state or (2) taxes pay-  
8 able under AS 43.55. No credit may exceed 50 per cent of the payment  
9 toward which it is being applied. Amounts due the Alaska permanent fund  
10 (AS 37.10.065) and the Alaska renewable resources development fund (AS  
11 37.11.020) shall be calculated before the application of credits under  
12 this subsection.

13 (j) To prolong the economic life of an oil and gas field, the  
14 commissioner shall adopt regulations for all bidding methods to allow  
15 reduction of royalty on leases within the field to compensate for in-  
16 creasing costs in the later stages of production decline. The commis-  
17 sioner may not grant a reduction of royalty until two years' initial  
18 production from the field has occurred and each lessee requesting the  
19 reduction has made a clear showing that the revenue from all hydro-  
20 carbons produced from the field is insufficient to produce a reasonable  
21 rate of return with respect to that lessee's total investment in the  
22 field.

23 (k) The commissioner shall define all terms and adopt all regula-  
24 tions necessary for a reasonable understanding and evaluation of a  
25 particular bidding method before the public announcement of the terms of  
26 proposed sale employing that method.

27 (1) Subject to the provisions of AS 31.05, the commissioner may,  
28 at his discretion, enter into an agreement whereby, with the consent of  
29 the lessee, the state's royalty share of oil and gas production may be

1 stored or retained in storage by the lessee, or the commissioner may  
2 enter into an agreement with one or more of the affected field lease  
3 holders to trade current royalty production from a field for a like  
4 amount, kind, and quality of future production, on the condition that  
5 the state receives back its stored or traded royalty share during the  
6 first half of the estimated field life or no later than 15 years after  
7 start of production, whichever is sooner.

8 (m) An oil and gas lease must cover a reasonably compact area not  
9 exceeding 5,760 acres, and must be for a period of five years. The  
10 commissioner shall grant a lease for 10 years when he finds that the  
11 longer period is necessary to encourage exploration and development in  
12 areas where environmental conditions severely restrict operations. An  
13 oil and gas lease shall be automatically extended if and for so long  
14 thereafter as oil or gas is produced in paying quantities from the lease  
15 or, if the lease is committed to a unit approved by the commissioner. A  
16 lease issued under this section covering land on which there is a well  
17 capable of producing oil or gas in paying quantities does not expire  
18 because the lessee fails to produce oil or gas unless the lessee is  
19 allowed reasonable time to place the well on a producing status. Upon  
20 extension, the commissioner may increase lease rentals so long as the  
21 increased rental rate does not exceed 150 per cent of the rate for the  
22 preceding year. If drilling has commenced on the expiration date of the  
23 primary term of the lease and is continued with reasonable diligence,  
24 including such operations as re-drilling, sidetracking, or other means  
25 necessary to reach the originally proposed bottom hole location, the  
26 lease continues in effect until 90 days after drilling has ceased and  
27 for so long thereafter as oil or gas is produced in paying quantities.  
28 An oil and gas lease issued under this section which is subject to  
29 termination by reason of cessation of production does not terminate if,

1 within 60 days after production ceases, reworking or drilling operations  
2 are commenced on the land under lease and are thereafter conducted with  
3 reasonable diligence during the period of nonproduction.

4 (n) The commissioner may establish by regulation that after a well  
5 has been plugged and abandoned, the rental rate which was in effect  
6 during the year of abandonment is maintained for the remainder of the  
7 term. Rental is payable in advance and continues until income to the  
8 state from royalty or net profit share exceeds rental income to the  
9 state for that year. Oil and gas leases shall provide for payment to  
10 the state of rental on the following basis:

- 11 (1) for the first year, \$1.00 per acre;
- 12 (2) for the second year, \$1.50 per acre;
- 13 (3) for the third year, \$2.00 per acre;
- 14 (4) for the fourth year, \$2.50 per acre;
- 15 (5) for the fifth and following years, \$3.00 per acre.

16 (o) Upon timely application as provided by regulation, the state  
17 may issue to the holder of a federal or private lease, a state shore-  
18 lands lease covering land within the exterior boundaries of the federal  
19 or private lease which has been excluded on the basis of navigability or  
20 which is later administratively or judicially determined to be shore-  
21 land. The term of such a state shoreland lease shall be the same as the  
22 term of the federal or private lease.

23 (p) To conserve the natural resources of all or a part of an oil,  
24 or gas pool, field, or like area, the lessees and their representatives  
25 may unite with each other, or jointly or separately with others, in  
26 collectively adopting or operating under a cooperative or a unit plan of  
27 development or operation of the pool, field, or like area, or a part of  
28 it, when determined and certified by the commissioner to be necessary or  
29 advisable in the public interest. The commissioner may, with the con-

1 sent of the holders of leases involved, establish, change, or revoke  
2 drilling, producing, and royalty requirements of the leases and adopt  
3 regulations with reference to the leases, with like consent on the part  
4 of the lessees, in connection with the institution and operation of a  
5 cooperative or unit plan as he determines necessary or proper to secure  
6 the proper protection of the public interest. The commissioner may  
7 require oil and gas leases issued under this section to contain a pro-  
8 vision requiring the lessee to operate under a reasonable cooperative or  
9 unit plan, and he may prescribe a plan under which the lessee must  
10 operate. The plan must adequately protect all parties in interest,  
11 including the state.

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

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

24 (s) When separate tracts cannot be individually developed and  
25 operated in conformity with an established well-spacing or development  
26 program, a lease, or a portion of a lease, may be pooled with other  
27 land, whether or not owned by the state, under a communitization or  
28 drilling agreement providing for an apportionment of production or  
29 royalties among the separate tracts of land comprising the drilling or

1 spacing unit when determined by the commissioner to be in the public  
2 interest. Operations or production under the agreement are considered  
3 as operations or production as to each lease committed to the agreement.

4 (t) The commissioner may, on conditions which he prescribes,  
5 approve drilling, or development contracts made by one or more lessees  
6 of oil or gas leases, with one or more persons, when, in his discretion,  
7 the conservation of natural resources or the public convenience or  
8 necessity requires it or the interests of the state are best served.  
9 All leases operated under approved drilling or development contracts,  
10 and interests under them, are excepted in determining holding or control  
11 under sec. 140 of this chapter.

12 (u) To avoid waste or to promote conservation of natural resources  
13 the commissioner may authorize the subsurface storage of oil or gas  
14 whether or not produced from state land, in land leased or subject to  
15 lease under this section. This authorization may provide for the pay-  
16 ment of a storage fee or rental on the stored oil or gas, or, instead of  
17 the fee or rental, for a royalty other than that prescribed in the lease  
18 when the stored oil or gas is produced in conjunction with oil or gas  
19 not previously produced. A lease on which storage is so authorized  
20 shall be extended at least for the period of storage and so long there-  
21 after as oil or gas not previously produced is produced in paying quan-  
22 titles.

23 (v) Each oil or gas lease issued by the state must contain a  
24 provision requiring the lessee to furnish the Department of Labor a  
25 quarterly report regarding the employment of state residents on the  
26 leased property. The commissioner of labor shall adopt regulations  
27 necessary to implement this subsection.

28 (w) Notwithstanding any other provision of this section, land  
29 which has been offered for lease within the previous five years and

1 which received no bids at competitive sale may be, at the discretion of  
2 the commissioner, immediately offered for lease, under regulations  
3 adopted by him, upon terms appearing most advantageous to the state;  
4 however, noncompetitive leasing is prohibited. The commissioner shall  
5 establish a royalty as he determines to be in the public interest but  
6 not less than 12 1/2 per cent. A lease must provide for payment to the  
7 state of rental but need not adhere to the rental schedule in (n) of  
8 this section nor to the 5,760-acres-per-lease limitation in (m) of this  
9 section. The lease term may not exceed five years except as provided in  
10 (m) and (o) of this section.

11 (x) A lessee conducting or permitting any exploration for, or  
12 development or production of, oil or gas on state land shall provide the  
13 commissioner access to all noninterpretive data obtained from that lease  
14 and shall provide copies of that data, as the commissioner may request.  
15 The confidentiality provisions of sec. 35 of this chapter apply to the  
16 information obtained under this subsection.

17 (y) A noncompetitive lease existing at the effective date of this  
18 Act shall be extended for a period of two years and so long thereafter  
19 as oil and gas is produced in paying quantities. A noncompetitive lease  
20 extended under this subsection is subject to the regulations in force at  
21 the expiration of the initial five-year term of the lease. No extension  
22 may be granted, however, unless within a period of 90 days before the  
23 expiration date an application for extension is filed by the record  
24 title holder or an assignee whose assignment has been filed for ap-  
25 proval, or an operator whose operating agreement has been filed for  
26 approval.

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

28 (b) When mineral land is to be leased, in addition to any other  
29 notice given, notice must also be given as provided in secs. 305 and 345

1 of this chapter.

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

3 (c) No person may take or hold at one time phosphate leases on  
4 state land [LANDS] exceeding in the aggregate 10,240 acres. No person  
5 may take or hold sodium leases or permits during the life of sodium  
6 leases on state land [LANDS] exceeding in the aggregate acreage 5,120  
7 acres, except that the commissioner may, where it is necessary in order  
8 to secure the economic mining of sodium compounds, permit a person to  
9 take or hold sodium leases or permits for up to 15,360 acres. No person  
10 may take or hold at any one time oil or gas leases exceeding in the  
11 aggregate 500,000 acres granted on tide and submerged land [LANDS] and  
12 500,000 acres on all land [LANDS] other than tide and submerged land  
13 [LANDS], including leases held both as lessee and under option or  
14 operating agreement from others. Where more than a single person holds  
15 an interest in an oil or gas lease, each person shall be charged only  
16 with that percentage of the total acreage which corresponds to its  
17 percentage share of the total beneficial interest in the lease.

18 \* Sec. 4. AS 38.05.335(c) is amended to read:

19 (c) The commissioner shall require each bidder for the competitive  
20 leasing of oil and gas lands to submit with his bid a deposit of money  
21 equal to 20 per cent of the bonus [AMOUNT BID].

22 \* Sec. 5. AS 38.05.140(d) is amended to read:

23 (d) The commissioner, for the purpose of encouraging the greatest  
24 ultimate recovery of coal, [OIL, GAS,] oil shale, phosphate, sodium,  
25 potassium, sulphur, and geothermal resources and in the interest of con-  
26 servation of natural resources, after public hearing, or, when the  
27 state's title to land beneath navigable waters has been legally  
28 challenged by the United States and litigation initiated, may waive,  
29 suspend, refund, or reduce the rental, or minimum royalty, or reduce the

1 royalty on an entire leasehold, or on any tract or portion of a lease-  
2 hold segregated for royalty purposes, whenever in his judgment it is  
3 necessary to do so in order to promote development, or whenever in his  
4 judgment the lease cannot be successfully operated under its terms. If  
5 the commissioner, in the interest of conservation, directs or assents to  
6 the suspension of operations and production under a lease granted, the  
7 payment of acreage rental or of minimum royalty prescribed by the lease  
8 may be suspended during the period of suspension of operations and pro-  
9 duction. The term of the lease shall be extended by adding the period  
10 of suspension to the lease.

11 \* Sec. 6. AS 38.05.145(b) is repealed.

12 \* Sec. 7. TRANSITIONAL PROVISIONS. By the 15th day of the First Session  
13 of the Eleventh Legislature the commissioner of natural resources shall  
14 submit a proposed oil and gas leasing program to the legislature in accor-  
15 dance with AS 38.05.180(b), except that the proposed program shall cover all  
16 areas to be leased in 1979 through 1983. No lease, except as authorized  
17 under AS 38.05.180(d), shall be issued during 1979, 1980, or 1981 unless the  
18 land to be leased was included in this proposed leasing program.