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AMERADA HESS CORPORATION

LEON HESS
Chairman of the Board

1185 AVENUE OF THE AMERICAS
NEW YORK NEW YORK 10036
(212) 997-8400

March 2, 1988

Senator John B. Coghill
Alaska State Legislature
Senate Resources Committee
Box V
Juneau, Alaska 99511

Dear Senator Coghill:

I regret that I must decline your invitation to testify at the Senate Resources Committee hearings next Monday, March 7, regarding legislation to encourage oil and gas development activities in Alaska.

I believe fervently in the need for legislation to encourage development of smaller, offshore Alaskan oil fields. I am convinced there are many, isolated smaller fields in the immediate vicinity of Seal Island and Northstar which will be oil bearing. Historically, similar discoveries have been made in various parts of the world. Prudhoe Bay was the original large discovery, and special legislation should be considered to enable future smaller discoveries to come to the market so that Alaska may continue to benefit from its valuable potential oil reserves. The local jobs that will be created, and the auxiliary effect on the Alaskan economy of the substantial capital investments that will be made, will greatly benefit the people of Alaska, both now and far into the future. The State should act now to encourage development. Because of the hostile operating environment, the lead time for development in Alaska is much longer and the costs are much higher.

Governor Cowper had advised me that he does not at this time believe it is in the best interests of the people of Alaska to support any legislative changes. Under no circumstances will I promote taking any action that the Governor of Alaska would not fully support as being in the best interests of all concerned. Unfortunately, this particular bill has been proposed to your Committee without my knowledge that it presented the same proposal made to Governor Cowper. This was not authorized.

Senator John B. Coghill
Page 2

After I received your letter, I telephoned Governor Cowper to ascertain whether he had changed his views. If he had requested me to testify because he supported the bill, I would be very happy to come to Alaska to appear before your Committee.

I do appreciate your invitation and hope you will understand why I cannot attend. I will not be a party to promoting legislation which the Governor does not want to support.

Very truly yours,

Leon Hess

cc: Governor Steve Cowper

Cotton Copy

MEMORANDUM

Division of Policy
Office of the Governor

To: Rep. Mike Navarre

Date: Feb. 24, 1988
(Rev.)

From: R.A. Fineberg, Policy Analyst
Division of Policy

Subject: Speech by ARCO's Wykoff to Indonesia Petroleum Assn.

Attached is an October 1987 speech by ARCO President Robert Wykoff to the Indonesia Petroleum Association. Note in particular this statement at page 5:

"Even though taxes are generally higher in foreign countries than in the U.S., the overall economics of overseas exploration are still attractive."

In view of all the recent arguments that tax breaks are necessary to promote North Slope development, I thought it might be interesting to compare Indonesia and Alaska in terms of oil production and revenues and Alaska. At 1.3 million barrels per day, Indonesia's production is approximately two-thirds that of Alaska. Indonesia's oil revenue (\$3.8 billion in 1986 and \$4.5 billion estimated for 1987) is more than twice that of Alaska.¹

When federal taxes are added, Indonesia's total tax bite is conservatively estimated to be more than 50% higher than that the companies face in Alaska. In other words, for every three oil tax dollars ARCO pays in Indonesia, it pays less than two dollars on the North Slope.

¹ For production, see Petroleum Intelligence Weekly, Aug. 31, 1987, p. 2; for revenue, see Petroleum Intelligence Weekly, Dec. 7, 1987, p. 3.

功夫

#100 US - 2 vol. Series
energy laws Asia

I J

THE OIL INDUSTRY TODAY -

ADAPTING FOR TOMORROW

BY ROBERT E. WYCOFF

PRESIDENT

ARCO

SIXTEENTH ANNUAL CONVENTION OF

THE INDONESIAN PETROLEUM

ASSOCIATION

JAKARTA, INDONESIA

TUESDAY, OCTOBER 20, 1987

11:00 A.M.

11/11/87

Handwritten scribble

Handwritten mark

Handwritten scribble

PROF DR. SUBROTO, MR. RAMLY, MR MOFFET
EXCELLÉNCIES, LADIES AND GENTLEMEN

I AM ALWAYS VERY HAPPY TO COME BACK TO THIS LOVELY COUNTRY. AND I AM HONORED TO HAVE THIS OPPORTUNITY TO TALK TO THE MEMBERSHIP OF THE INDONESIAN PETROLEUM ASSOCIATION ABOUT THE FUTURE OF THE OIL INDUSTRY AS WE SEE IT AT ARCO, THOUGH THAT VISION MAY AT TIMES BE A TRIFLE MORE CLOUDED THAN THE BEAUTIFUL SKIES THAT ARE SO TYPICAL OF THESE ISLANDS.

BUT IT IS A VISION WHICH IS TERRIBLY IMPORTANT TO ALL OF US HERE TODAY. THE BROAD MEMBERSHIP OF THE INDONESIAN PETROLEUM ASSOCIATION REFLECTS THE IMPORTANCE OF INDONESIA IN THE OIL INDUSTRY. THERE IS HARDLY A COMPANY OF ANY SIZE WHICH IS NOT REPRESENTED IN SOME WAY IN INDONESIA. THERE ARE IN FACT ABOUT 200 COMPANIES WHO HAVE AN INTEREST IN EXPLORATION OR PRODUCTION.

FOR ARCO, INDONESIA HAS BEEN A LAND OF OPPORTUNITY. WE HAVE BEEN SUCCESSFUL HERE IN DISCOVERING PROLIFIC FIELDS OF OIL AND GAS.

WE HAVE ALSO FOUND TO AN ALMOST UNPRECEDENTED DEGREE THE VERY DESIRABLE AND SOMEWHAT UNCOMMON QUALITIES OF STABILITY, HONOR AND FAIR DEALING. IN THE TURBULENCE OF THE INTERNATIONAL OIL BUSINESS, INDONESIA HAS BEEN AN ISLAND OF RATIONALITY AND WISDOM. FOR THAT WE'RE GRATEFUL.

DESPITE THE PROBLEMS THAT CAME TO THIS COUNTRY AS THE PRICE OF OIL FELL SHARPLY A YEAR AND A HALF AGO, INDONESIA AND HER PEOPLE CONTINUED TO CLING TO A REALISTIC VISION OF THE FUTURE. THEY CONTINUED TO REALIZE THAT ENERGY WOULD BE THE FIRM FOUNDATION ON WHICH THE PROGRESS OF TOMORROW COULD BE

BUILT.

THIS HUGE NATION OF 170 MILLION, FIFTH LARGEST IN THE WORLD, HAS WEATHERED THE IMPACT OF THE CRUDE PRICE DROP AND, LIKE THE REST OF US IN THE BUSINESS, WELCOMED THE PRICE REVIVAL THAT WE BEGAN TO EXPERIENCE SIX MONTHS AGO.

NOW THE QUESTIONS THAT ALL OF US FACE TOGETHER IS HOW STABLE THAT PRICE WILL PROVE TO BE IN THE FUTURE, AND HOW WE WILL PARTICIPATE TOGETHER IN FINDING AND DEVELOPING THE LARGE REMAINING PETROLEUM RESOURCES OF INDONESIA. IN BOTH RESPECTS, I BELIEVE WE CAN LOOK FORWARD TO A BRIGHT FUTURE.

WITH RESPECT TO PRICES I FIND MYSELF IN BASIC AGREEMENT WITH DR. SUBROTO. BARRING A MAJOR UPHEAVAL IN THE PERSIAN GULF, I THINK THE PRICE WILL PROVE TO BE STABLE IN THE \$20 RANGE. IT MAY BOB UP AND DOWN A BIT, BUT ALWAYS RETURN, IN THE NEXT FEW YEARS AT LEAST, TO THE VICINITY OF THE 20-DOLLAR MARK. WHEN I SAY VICINITY, I MEAN WITHIN 2 OR 3 DOLLARS, MORE OR LESS.

IN A FEW YEARS, SUPPLY AND DEMAND WILL PROBABLY BE A GOOD DEAL CLOSER TO EQUILIBRIUM THEN THEY ARE TODAY. IF SO, THE WORLD PRICE OF CRUDE CAN BE EXPECTED TO GO UP SUBSTANTIALLY, TO PERHAPS AS HIGH AS \$30 IN 1987 DOLLARS.

APPEARANCES TO THE CONTRARY, WHAT I HAVE JUST SAID IS DEFINITELY NOT A FORECAST OF "BUSINESS AS USUAL". NO ONE WITH ANY SENSE WHO HAS BEEN WHAT WE HAVE BEEN THROUGH IN THE PAST TWO YEARS CAN TALK OF ANYTHING IN THE PETROLEUM INDUSTRY AS BEING THE "USUAL" THING.

THE WORLD CRUDE PRICE CONTINUES TO BE AN EXPRESSION OF ECONOMIC AND POLITICAL FORCES THAT ARE IN MANY RESPECTS AT ODDS WITH EACH OTHER. AT THE CENTER OF THE ACTION IS OPEC, WHOSE MEMBERS, OFTEN SEEM TO BE DIVIDED IN THEIR APPROACH TO PRICE AND SUPPLY POLICY.

A CRISIS OF THE KIND WE EXPERIENCED TWICE IN THE 1970S IS CLEARLY A POSSIBILITY.

CERTAINLY, NO ONE CAN CONTEMPLATE THE PRESENT SITUATION IN THE PERSIAN GULF WITH ANYTHING BUT APPREHENSION. AND THE ENERGY POLICY OF THE UNITED STATES. -- PERHAPS I SHOULD SAY ENERGY NON-POLICY-- CONTINUES TO DRIVE UP OUR NEED FOR IMPORTED OIL, THUS ADDING TO THE GENERAL TENSION.

BUT UNLESS WE HAVE A MAJOR CONFLAGRATION AND LONG TERM INTERRUPTION OF PRODUCTION IN THE MIDDLE EAST, IT SEEMS TO US THAT THERE ARE GOOD REASONS TO SUPPOSE THAT OIL PRICES WILL BE STEADY UNTIL THE MID-90S WHEN THEY WILL RISE--AS WORLD DEMAND FOR CRUDE NEARS THE PRODUCTION CAPACITY OF THE EXPORTING COUNTRIES.

FOR ONE THING, WE BELIEVE THAT HOWEVER MUCH THE OPEC COUNTRIES MAY SEEM TO BE DIVIDED, THEIR ACTIONS HAVE NOT BEEN SO MUCH A RANDOM, EMOTIONAL RESPONSE TO POLITICAL IMPULSES AS A CALCULATED, RATIONAL REACTION TO ECONOMIC FORCES.

BACK IN 1983, FOR EXAMPLE, IT WAS OBVIOUS TO ANYONE WHO TOOK THE TIME TO LOOK THAT THE SAUDIS' MARKET SHARE COULD NOT CONTINUE TO DROP INDEFINITELY-- AND IT DID NOT. THEY REGAINED THEIR COMMAND OF THE MARKET BY RADICAL INCREASES IN THEIR PRODUCTION RATES, UNDER THEIR NETT BASIC PRICING

APPROACH.

THE PRICE CORRECTION THAT TOOK PLACE WAS DRASTIC, YET NECESSARY. AND NOW WE BELIEVE THAT THE OPEC LEADERSHIP WILL RESIST THE IMPULSE TO DRIVE PRICES TOO HIGH AS THEY DID IN THE 1970S. THE RESULT THEN WAS NOT WHAT THEY WANTED, WITH DEMAND CURTAILED AND EXCESSIVE ALTERNATE SUPPLY OF OIL AND OTHER ENERGY SOURCES DRAWN TO THE MARKET FROM NON-OPEC SOURCES BY EXCESSIVELY HIGH PRICES.

OUR VIEW IS THAT OPEC WILL WORK HARD TO PREVENT THAT FROM HAPPENING AGAIN. BY THE SAME TOKEN, IT HAS DEMONSTRATED IN THE PAST YEAR THAT IN THE FACE OF A PRICE COLLAPSE IT CAN RESTRICT ITS PRODUCTION BY JUST ENOUGH TO RAISE PRICES TO TODAY'S MORE REASONABLE LEVELS.

SO WE THINK THEY'LL BE ABLE TO HOLD IT AT A REASONABLE LEVEL OF PRODUCTION, A LEVEL SUITED TO MAINTAIN A MANAGEABLE PRICE. SOME CHEATING WILL PROBABLY OCCUR, THERE MAY BE SOME PERIODS OF PRICE VOLATILITY, BUT NOT ENOUGH, IN OUR VIEW, TO DISRUPT THE OVERALL STRATEGY.

IF WE'RE RIGHT AND THE PRICE OF CRUDE REMAINS STABLE AT AROUND \$20, WHAT DOES THAT IMPLY FOR THE OIL INDUSTRY-- AND PARTICULARLY FOR THE INDUSTRY HERE IN INDONESIA?

CERTAINLY, IT'S A FAR DIFFERENT WORLD THEN THOSE EXHILARATING DAYS OF THE LATE 1970S WHEN VISIONS OF \$100-A-BARREL CRUDE DANCED IN OUR HEADS.

TODAY THE INDUSTRY IS MUCH MORE CAUTIOUS IN ITS INVESTMENTS, BUT WE ARE BEGINNING TO SEE SIGNS OF RECOVERY. ARCO FOR ONE IS A LOT MORE DISCRIMINATING ABOUT THE SORT OF RISK WE ARE

WILLING TO ACCEPT.

BUT WE ARE FINDING OUR SEA LEGS IN THIS NEW WORLD --- AND, NOW THAT WE HAVE HAD TIME TO ADJUST OUR STRATEGIES AND LOOK AT OUR OPTIONS, WE CAN BEGIN TO SEE A LOT OF SOLID OPPORTUNITY OUT THERE, BOTH AT HOME AND OVERSEAS. I THINK MUCH OF THE INDUSTRY IS EXPERIENCING A SIMILAR REBIRTH OF WHAT I WOULD CALL A REALISTIC OPTIMISM.

LAST SUMMER, AS WE ALL KNOW TOO WELL, U.S. DRILLING ACTIVITY WAS DOWN TO THE LOWEST LEVEL SINCE WORLD WAR II, BUT IT'S CLIMBING AGAIN. WE'RE NOT EXPECTING TO RETURN TO THE DRILLING LEVELS OF THE 70'S AND EARLY 80'S, BUT I AM CONVINCED THERE IS A LOT OF OIL AND GAS-- PARTICULARLY GAS-- LEFT TO BE FOUND IN THE U.S., AND WE'RE LOOKING.

BUT WE'RE PUTTING MORE EMPHASIS NOW ON THE INTERNATIONAL ASPECT OF OUR BUSINESS AND FOR GOOD REASON. WE, ALONG WITH MOST OF THE INDUSTRY, ARE FINDING IT GENERALLY MORE ECONOMICALLY TO EXPLORE FOR OIL AND GAS IN OVERSEAS LOCATIONS SUCH AS INDONESIA.

THE OVERRIDING FACTOR IS THE CHEAPER FINDING COST. EVEN THOUGH TAXES ARE GENERALLY HIGHER IN FOREIGN COUNTRIES THAN IN THE U.S., THE OVERALL ECONOMICS OF OVERSEAS EXPLORATION ARE STILL ATTRACTIVE.

SO THAT WE FEEL THE PRESENT PRICE ENVIRONMENT IS MORE THAN STRONG ENOUGH TO SUPPORT A REASONABLY ACTIVE WORLDWIDE EXPLORATION PROGRAM.

OF COURSE, IT ALSO HELPS QUITE A BIT THAT THE TECHNIQUES WE'RE USING NOW ARE A WHOLE LOT MORE SOPHISTICATED THAN THEY

USED TO BE. WE JUST KNOW A LOT MORE ABOUT WHAT'S DOWN THERE AND HOW TO GET IT OUT.

THESE TECHNIQUES WILL HAVE THE EFFECT OF EXTENDING THE PETROLEUM ERA MUCH FURTHER INTO THE 21ST CENTURY THAN SEEMED POSSIBLE AS RECENTLY AS 10 YEARS AGO.

IT NOW APPEARS TO MOST PEOPLE THAT EVEN IN THE U.S., IN MANY RESPECTS A TIRED AREA, WE WILL NEVER COME CLOSE TO ACTUALLY "RUNNING OUT" OF OIL. AS WE COMBINE NEW RECOVERY TECHNIQUES WITH HIGHER PRICES, U.S. PRODUCTION WILL BE STRONG FOR DECADES TO COME.

BUT EVEN WITHOUT HIGHER PRICES-- THERE IS EVEN MORE REASON FOR OPTIMISM INTERNATIONALLY- AND ESPECIALLY HERE IN INDONESIA.

BEAUSE FOR THOSE OF US AT ARCO, AND I KNOW THIS IS TRUE OF ALL OF THE PRODUCER/CONTRACTORS REPRESENTED HERE TODAY, ANY VISION OF THE FUTURE THAT DID NOT INCLUDE A POSITION HERE IN INDONESIA WOULD BE DIFFICULT TO IMAGINE.

WE'VE BEEN HERE A LONG TIME, AND, LIKE MANY OF YOU HAVE ENJOYED GOOD SUCCESS. LAST YEAR WE PARTICIPATED IN THE START UP OF THREE NEW FIELDS AND WE'RE LOOKING RIGHT NOW AT SOME VERY GOOD EXPLORATION PROSPECTS OFFSHORE BALI.

BUT WE REALIZE THAT THE FUTURE OF THE OIL INDUSTRY HERE HAS SOME OF THE CHARACTERISTICS OF THE UNITED STATES. SOME PARTS OF INDONESIA, LIKE MOST OF THE U.S., ARE WELL BEYOND THE INITIAL STAGES OF FLUSH PRODUCTION.

FROM NOW ON, THE OIL IS GOING TO COME HARDER BUT, WORKING TOGETHER, WE CAN MAKE IT WORK — AND THAT'S THE IMPORTANT THING.

THE EXPERIENCE AND KNOWLEDGE THAT ARCO AND THE OTHER COMPANIES ARE GAINING IN THE U.S. RIGHT NOW CAN BE APPLIED HERE.

AS WE CONTINUE TO DEVELOP NEW UNDERSTANDINGS OF CONCEPTS SUCH AS STRATIGRAPHIC TRAPS, HORIZONTAL DRILLING, DEEP-WATER EXPLORATION AND ENHANCED OIL RECOVERY, THAT INFORMATION WILL ENABLE INDONESIA TO FIND AND RECOVER NEW RESERVES OF OIL IN THE MATURE AREAS, AND TO REACH OUT TO THE MORE REMOTE FRONTIER AREAS FOR OIL AND GAS PROSPECTS THAT WE ALL KNOW ARE THERE.

THIS BLEND OF EXPERIENCE AND NEW TECHNOLOGY HAS ENABLED ARCO TO ADD MORE THAN A BILLION NET BARRELS OF OIL IN OUR FIELDS ON THE NORTH SLOPE— MORE THAN REPLACING OUR PRODUCTION SINCE STARTUP TEN YEARS AGO.

HERE IN INDONESIA, VARIOUS SECONDARY AND EOR TECHNIQUES CAN ALSO BE APPLIED TO MATURE FIELDS, OFFERING THE PROSPECT OF GREATLY EXTENDING THEIR PRODUCTIVE LIVES.

NEW DEVELOPMENTS IN SEISMIC TECHNOLOGIES ALSO OFFER EXCITING POSSIBILITIES FOR DISCOVERIES IN EXISTING PRODUCING AREAS AS WELL AS INDONESIA'S FRONTIER AREAS.

AS WE CONSIDER THE WAYS IN WHICH THE INTERNATIONAL ENERGY MARKETS WILL DEVELOP THROUGH THE 1990S, IT SEEMS APPARENT TO ME THAT INDONESIA IS VERY WELL POSITIONED TO TAKE ADVANTAGE OF THE GROWTH THAT IS SURE TO TAKE PLACE IN THE CONSUMPTION

OF NATURAL GAS.

IN SOME RESPECTS, NATURAL GAS IS THE "SLEEPER" IN THE ENERGY ECONOMY.

BACK IN THE 70S, WHEN SOME PEOPLE THOUGHT OIL PRICES WOULD RISE AS HIGH AS \$100 A BARREL THE IDEA WAS THAT THERE WERE NO EFFECTIVE SUBSTITUTES FOR OIL OTHER THAN HIGH-COST SYNTHETICS DEVELOPED FROM COAL, SHALE OR BIOMASS.

THEIR PRICE -- HIGH THEN, HIGH TODAY -- WAS CONSIDERED TO BE THE ONLY THING SETTING THE UPPER LIMITS ON THE PRICE OF OIL.

WELL, THAT TURNED OUT TO BE WILDLY INCORRECT. WE KNOW THERE ARE ALTERNATIVES TO OIL THAT ARE AVAILABLE AND AT A PRICE WELL BELOW THAT OF THE SYNTHETICS. CONSERVATION IS ONE AND NATURAL GAS IS ANOTHER.

GAS WILL CERTAINLY BE A MAJOR PLAYER BECAUSE THERE'S A LOT OF IT AROUND. IN BTU TERMS, GAS RESERVES ARE NOW EQUAL TO 80 PERCENT OF KNOWN DEPOSITS OF OIL -- BUT THE POTENTIAL FOR FUTURE DISCOVERIES IS MUCH GREATER FOR GAS THAN OIL.

WE REALLY HAVEN'T AIMED OUR EXPLORATION AT GAS, BUT THAT'S CHANGING. AS ENERGY DEMAND FIRMS, THERE WILL BE REASON TO LOOK FOR IT FAR MORE INTENSIVELY THAN WE HAVE IN THE PAST.

AND AT THE DEEPER DEPTHS WE'RE DRILLING TODAY, CHANGES FOR FINDING OIL TEND TO DIMINISH BUT GAS PROSPECTS ACTUALLY INCREASE AS YOU GO DEEPER.

FINDING GAS IS ONE THING, OF COURSE; MARKETING IT IS ANOTHER, CHIEFLY BECAUSE OF THE DIFFICULTY IN TRANSPORTING

IT FROM ONE PLACE TO ANOTHER.

IN THE CASE OF ARCO INDONESIA, WE INTEND TO AVOID THAT PROBLEM BY DEVELOPING MARKETS HERE IN INDONESIA. WE HAVE A LARGE DISCOVERY IN THE KANGEAN ISLAND GROUP WHICH WE HOPE TO BRING ON STREAM IN THE NEAR FUTURE FOR POWER GENERATION AND OTHER USES IN EAST JAVA.

THIS WOULD FREE UP ADDITIONAL OIL AND COAL FOR EXPORT AS WELL AS PROVIDE A LOW COST, RELIABLE ENERGY SUPPLY FOR THE SURABAYA AREA OF EAST JAVA.

WE BELIEVE GAS WILL BECOME INCREASINGLY IMPORTANT AS THE INDONESIAN GOVERNMENT CONTINUES ITS ADMIRABLE EFFORT TO ENCOURAGE ITS USE AS A SUBSTITUTE FOR OIL.

AND WE CAN SEE THE POSSIBILITY OF DEVELOPMENT OF GAS-TO-GASOLINE TECHNOLOGY AS A PARALLEL TO THE USE OF COMPRESSED NATURAL GAS IN CARS IN THE JAKARTA AREA.

AS MORE GAS IS DISCOVERED HERE IN INDONESIA AND ELSEWHERE IN THE WORLD IT'S NOT TOO DIFFICULT TO ENVISION A HUGE INCREASE IN BOTH LNG, AND PIPELINE TRAFFIC FOR LOCAL MARKETS. GROWING ASEAN CONSUMPTION WOULD BE SERVICED FROM INDONESIA, AUSTRALIA, MALAYSIA, CHINA AND PERHAPS EVEN ALASKA SOMETIME IN THE FUTURE.

IN REVIEWING THESE DEVELOPMENTS THAT I'VE SKETCHED HERE THIS MORNING, IT SEEMS FAIR TO SAY THAT THE WORD PETROLEUM INDUSTRY IS CAPABLE OF ADAPTING TO THE CURRENT PRICE ENVIRONMENT AND BUILDING TOWARD THE FUTURE ON PERHAPS A MORE REALISTIC BASIS THAN WAS THE CASE 10 YEARS AGO.

OIL IS STILL THE LARGEST INDUSTRY IN THE WORLD. THERE IS STILL A LOT OF OIL AND GAS TO BE FOUND. AND EVEN IF THE QUARRY IS A BIT MORE ELUSIVE THAN IT USED TO BE, THANKS TO RECENT AND CONTINUING TECHNOLOGICAL ADVANCES, WE'RE FAR BETTER EQUIPPED FOR THE HUNT.

CERTAINLY THAT IS TRUE IN INDONESIA. THERE ARE OPPORTUNITIES FOR US HERE THAT PRICE AND TECHNOLOGY CAN BRING TO REALITY TO THE BENEFIT OF EVERYONE CONCERNED.

AND YET, AS THE RELATIONSHIPS THAT THE CONTRACTORS HAVE ENJOYED HERE OVER THE YEARS HAVE PROVEN, MONEY AND TECHNOLOGY AREN'T THE ONLY KEYS TO SUCCESS.

THERE IS ALSO COOPERATION. THERE IS UNDERSTANDING. THERE IS RECOGNITION OF THE PRIORITIES OF EACH PARTY TO THE AGREEMENTS THAT WE HAVE HAD IN INDONESIA AND HOPE TO GO ON ENJOYING FOR YEARS TO COME.

THE SPIRIT OF COOPERATION BETWEEN PERTAMINA AND THE PRODUCER/CONTRACTORS WILL, I'M SURE REMAIN MUCH AS IT HAS BEEN AS WE PROCEED TOGETHER INTO THIS NEW ENERGY ERA.

WE RECOGNIZE AT THE SAME TIME THAT SOME ELEMENTS OF THE CONTRACTS MUST CHANGE EVEN AS THE FIELDS HAVE CHANGED. ADJUSTMENTS WILL BE NECESSARY TO MAKE IT ATTRACTIVE FOR THE PRODUCER TO OPERATE IN THE COUNTRY, AND PARTICULARLY TO APPLY THE HIGHLY PROSPECTIVE BUT COSTLY NEW TECHNOLOGIES NOW BEING DEVELOPED.

FOR THAT REASON, WE'RE MUCH ENCOURAGED THAT STEPS ARE BEING TAKEN TO EXTEND PRODUCTION-SHARING CONTRACTS DUE TO EXPIRE

IN THE NEXT FEW YEARS. HERE THIS MORNING PRESIDENT SOEHARTO HAS EXPRESSED AGREEMENT IN PRINCIPLE WITH THIS STEP. WHILE TERMS ARE STILL IN NEGOTIATION, WE ARE CONFIDENT THAT THE QUESTIONS WILL BE RESOLVED SATISFACTORILY.

IN CLOSING, I WOULD LIKE TO EXPRESS MY APPRECIATION TO THE LEADERSHIP AND MEMBERS OF THE INDONESIAN PETROLEUM ASSOCIATION FOR KINDLY INVITING ME TO BE HERE TODAY.

IPA HAS BEEN A POSITIVE FORCE IN THE INDONESIAN OIL STORY SINCE ITS INCEPTION IN 1971. YOUR ROLE AS A BRIDGE BETWEEN THE PRODUCER AND THE GOVERNMENT IS CRUCIAL TO THE CONTINUED SUCCESS OF OUR COMBINED ENTERPRISE.

I AM SURE I SPEAK FOR ALL THE PRODUCERS WHEN I SAY THAT WE HAVE ENJOYED OUR LONG AND PLEASANT RELATIONSHIP, AND CAN ONLY HOPE THAT IT CONTINUES FOR MANY YEARS TO COME.

THANK YOU.

STEVE COWPER
GOVERNOR



STATE OF ALASKA
OFFICE OF THE GOVERNOR
JUNEAU

January 28, 1988

Mr. Leon Hess
Chairman
Amerada Hess Corporation
1185 Avenue of the Americas
New York, NY 10036

Dear Leon,

This is a somewhat tardy reply to your proposal to provide tax and royalty relief for the Seal Island leases. I have decided against the proposal, and I want to explain my reasons.

First off, I appreciate the spirit in which this proposal was made. You and Ron were very clear about your objectives and realistic about the political implications that would attach. I like a direct approach and normally do things that way myself.

As you know, any decision I make in this area must reflect a state policy which applies to the whole industry. At this time there are a number of outstanding leases which were purchased at a time when oil price projections were more sanguine than they are today. Many of those leases provided for a net profit share in lieu of larger up-front bonuses, as was the case with Amerada Hess at Seal Island.

Your proposal would benefit the state because of the jobs which would be created. It's hard to tell about the effect on state revenues, which also translates into jobs. That would depend on a judgment as to whether TAPS would otherwise be filled to capacity; if so, the oil produced under this incentive program would displace other oil on which the state was receiving its regular revenues. For the next few years, I am informed that TAPS will probably be operating at its nominal maximum capacity of 2.1 million bpd. If that's right, then the effect will be close to a wash in terms of jobs, although my stated preference is for private-sector employment.

RECEIVED

FEB 03 1988
DIVISION OF OIL & GAS
ANCHORAGE, ALASKA

Mr. Leon Hess

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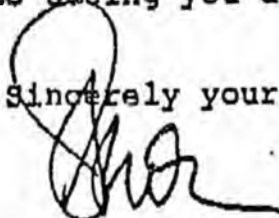
January 28, 1988

The political effects of this proposal must be assessed as well. While we are looking at the possibilities of incentives, given the current TAPS throughput the major producers are saying they don't want any of that kind of help. There is also the question of interference with the normal developmental order which is established mainly by relative cost. Thirdly, a lot of people don't want to establish any kind of incentive regime. They're already mad at the effect of the so-called "economic limit factor" legislation of 1981.

For the moment at least, my judgment is that when all the above factors are considered, a major departure from current policy isn't warranted. I know you and Ron disagree with this analysis but that's where I come down on it.

I hope things are otherwise well with you, the company, and the Jets, and I look forward to seeing you again in the near future.

Sincerely yours,



Steve Cowper
Governor

DELIVER TO: <u>Michelle Watts</u>	LOCATION: <u>C.O.</u>
FROM: <u>Jim Mason</u>	LOCATION: <u>Oil & Gas</u>
TELEPHONE/TELECOPIER # <u>586-2779</u>	TOTAL NUMBER OF PAGES <u>2</u>
TRANSMITTING ON/SPEED _____	DATE: <u>2/19</u> TIME <u>10:30</u>
PHONE FOR PROBLEMS-NAME/NUMBER _____	
COMMENTS: <u>Please call Ted Farquhar. He will</u>	

461-3711

John T. Hughes.

prob. of dev't of these prospects.

- public use estimate
- field size limit? - talked about the idea - A-H was int'd -
- need to exempt anything that's unratified
interest is not to cover West Sak.

Milne ft - has produced - not eligible -

Sen. Escs. is why on a bill - 1/1/78 - wd allow Milne -

Kay Brown -

- 1) end relief in '94 (provision in the bill) - K sugg's use it or lose it clause
- 2) ratchet back on tax + reg; vs 0 -
- 3) oil price cap? - when price exceeds a threshold relief wd end.
(AH sez \$34) -

dev't plan -

CO. has spent \$83 million ~~so~~ so far - the bill is intended to spur new dev't - NPS regs shd allow all drilling costs, not just the dev't costs -

detail - Parsons + Co. - Hess will bury - \$1.2 b. ^{field cost} + \$300m

- for pipeline will forgive 20% of the ^{cost} but not the pipeline - what is ELF for the field? being reviewed now - FERC will allow recovery of pipeline costs - so not a concern - state will need to run the dev't plan. will hv. authority to go along the dev't plan -

1990/1995 - ext'n of expl'y unit -

knowing the resv is not good news -

Reame - eventually releasing the act's -

DOR rev. program - 50% - only \$1/bbl incr. in price paid

The AH has essentially condemned the lease

State won't get 73% NPS

also won't get 20% royalty

so releasing us'll lose ~~to~~ state money

price expectations in 1974 were so much diff't -

∴ lkg at royalty + serv. tax - state makes much more -

dev't phase - 1000 jobs direct - 3-6 yrs. ?

prod'n phase - not known - > speculative -

* 1.2 b bps what? how many wells? how many bpd?

Hess will say all Ark. jobs - Bayonne ^{NJ} refinery -

labor is solid on this bill, vs. Conoco w/ bad record
aggressive training program in St. Croix.

local hire provision -

→ 2 > delineation wells are needed - \$40 m.

Hess has committed to labor to work in good faith to hire local

Memo - Lenny - say labor supports the bill

Precedent.

UK - soon gas field - wells N of gas field ^{that discover} are excused
 mining (12.5%) for life of the field - 1st 20 k ^{ppd} ~~up~~ up
 to 75 m. by by are exempt fr. serv for the life of field -
 Ca, Wyo., NM, Ks. - hv passed inciv legis'n - Ak is in
 "shrinking mining" of states that hvnt -
 a typical state inciv psy is on ~~serv~~ ^{serv} side - usu a wildcard
 w/ some deadline ~~the~~ problem is exempt fr. serv for a while -

→ [A-H annual reports] -

NPS lsg reg

dev't vs. explor'n inc'vs -

NS is unique bec. there are numerous fields known, delineated,
 warding. -

7 explor'n wells last yr. (AOGCE) -

many leases are ~~gas~~ unexplored - owners know it's hopeless
 to drill into dev't infrastructure, inc'vs fr dev't of smaller
 fields.

→ need > information about the field

emp. benefit of dev't much hr than for explor'n -

AK has bn investing in No. Sea recently - investment climates?

ENHANCING RESOURCE DEVELOPMENT

Alaska's strength is its abundance of natural resources, including substantial deposits of oil and gas throughout the state. Alaska faces a major problem in developing these resources, the high cost of development. This high cost is a result of the harsh environment, remoteness to markets, and a current "fixed cost factor" public policy. Future activity by the oil and gas industry will be controlled by three factors; oil prices, the ability of Alaska to preferentially attract limited corporate investment dollars, and the discovery and/or development of new petroleum reserves. The state can influence the investment climate, particularly for smaller resource development, by adopting policies that will attract investment and encourage development of these resources.

Not all fields are created equal. Alaska is blessed with the largest and fourth largest fields in the United States. Because the state receives more than two-thirds of its general fund revenues these two fields, they are a dominant factor in determining policy. Having these large fields, and using them as a benchmark for public policy, is a mixed blessing. Revenues for the state will be maximized for the short term during peak production, but the search for and development of additional reserves for the long term replacement of declining production from the major fields may be stifled by the short term objectives.

Statistically, the number of small accumulations will be much greater than the number of large accumulations. It must be recognized that most of the replacement production for the decline from Prudhoe Bay will come from smaller fields. Public policy which does not recognize the diseconomies of scale for smaller fields will result in these smaller fields remaining undeveloped. Small fields must be perceived as economic by companies making investment decisions. With limited investment capital, and with numerous opportunities both nationally and internationally compet-

ing for their dollars, the investment options that provide the best apparent profit potential will attract the investment capital.

In Alaska, smaller fields must provide the same services as larger fields. Because of the diseconomies of scale, smaller fields require both more capital investment per barrel of reserves to develop the field, and the operating cost, measured on a dollar per barrel basis, will also be greater. Thus, the smaller fields, on a per barrel basis, provide greater investment in Alaska, and provide more jobs for Alaskans, than large fields. Unfortunately, their tax structure and royalty structure has been established on a large field concept.

Alaska is at a crossroads concerning economic policy for the state. One branch leads towards increased taxation and increased state spending in an attempt to stimulate the state economy. The other option is to provide incentives to attract investment dollars by private industry, which in turn will create jobs in the private sector. The measurement of a healthy economy should be based on private sector investment and jobs, not on state spending. Economic health and longevity are best promoted by encouraging the search for and development of new fields, which maximizes utilization of Alaska's strengths.

The State of Alaska and the oil industry are a partnership in developing the state's resources. The partnership will prosper when both parties are gaining economic benefits. Encouraging the development of smaller resource accumulations will benefit the state by providing investment capital, jobs, and incremental royalty and taxes compared to the present status. The oil industry will benefit by being able to economically and profitably develop resources that are now perceived as uneconomic.

Oil price will always be the determining factor in investment decisions, but, with oil prices in the \$18-25/BBL range, incentives can stimulate investment in and development of smaller re-

source accumulations. For example, the threshold oil price for positive earnings at Milne Point can vary from \$18/BBL to \$25/BBL depending upon the royalty rate and tax structure. The potential impact of incentives on both the future development of Milne Point and the State's economy are shown in Attachment I. It must be understood that these values are estimates, and the perception of future oil prices will always play the most important role in investment decisions in Alaska because of its unique "Cost" position with respect to other parts of North America and the world.

The Milne Point case is just one example of the potential benefits of a public policy program that encourages the development of smaller resource development. Smaller resources must be perceived as economic before they will be explored and developed. The perception that other fields like Milne Point can be economic, and will be encouraged to be economic by appropriate public policy, is important. If twenty fields similar to Milne Point were developed in the next ten years, they would provide 4000-5000 direct jobs. If these jobs are multiplied by the trickle-down factor, a substantial number of private sector jobs would be added within the state.

Specific items that can be legislated to enhance the exploration for the development of smaller resources are:

- o Re-establish the discovery royalty. During the search for oil in Cook Inlet, 16 drilling rigs were racing against one another to get the discovery royalty. When was the last time the total state had 16 rigs working?
- o Encourage the use of Exploration Incentive Credits in future lease sales. In the recent State Sale 54, about 40% of the bids submitted involved companies not currently producing in Alaska. This was also the first State Sale in many years to offer a fixed royalty rate and EIC's.

- o Establish lead agency permitting. HB 212 and SB 280 introduced in 1987 would accomplish this goal.
- o Provide Royalty Incentives for low gravity crude. The West Sak sands on the North Slope contain an estimated 24-40 billion barrels of oil in place. At the present time this zone, which contains more oil in place than Prudhoe Bay, is not being produced or field tested.
- o Clarify the Commissioner of the Department of Natural Resources's authority to use royalty alterations to enhance productivity. The two year restriction in Title 38 was intended for use when royalty was a bid variable. Language should be added to clarify this intent.
- o Develop an Economic Limit Factor which is responsive to field size. The ELF is an excellent concept in recognizing that the tax burden should be reduced on lower productivity wells. This same logic can be extended to lower productivity fields.

Attachment II includes specific amendments to Title 38 and Title 43 which would accomplish these suggested incentives.

**MILNE POINT UNIT
IMPACT OF INCENTIVES**

ATTACHMENT I

**Current
Royalty, Taxes**

**12 1/2% Royalty
Current Taxes**

**5% Royalty
Modified Taxes**

For Next Five Years

Threshold Oil Price	\$22-25/BBL	\$20-22/BBL	\$18-20/BBL
Investment	\$35 MM	\$65 MM	\$300 MM
No. Wells Drilled	10-15	20-30	130-150 <i>200</i>
New Employment	25-30	50-60	200-250

For Life Of Field

Field Life	5-7 Yrs	10-12 Yrs	20-25 Yrs
State Royalty	\$40-45 MM	\$50-60 MM	\$60-70 MM
State Taxes	\$25-30 MM	\$40-50 MM	\$20-25 MM

1/2008 5% discount

20-25 MM

AS 38.05.180 amended by adding a new subsection to read:

(aa) The lessee of a state oil and gas lease on which a discovery well has been drilled shall be entitled to withhold a discovery royalty award of 60% of the oil and gas royalty otherwise payable to the state for that lease for a period of ten years from date of discovery provided that all of the following criteria are met:

1) The well must be drilled at a surface location at least 20 miles from the surface location of any other well which has been tested in commercial quantities or is presently capable of producing in commercial quantities; 2) a discovery test in commercial quantities has been witnessed by an agent of the state; 3) the discovery test interval is located entirely under the lease for which the award is given; 4) the discovery test is completed within one year from the date of first penetration of the producing zone in that well, and 5) applications for the award is made within 180 days of the completion of the commercial test.

AS 38.05.180(i) amended as follows:

(i) The commissioner SHALL (may) provide for the establishment of an exploration incentive credit system under which a lessee of state land drilling an exploratory well on that land may earn credits based upon the footage drilled and the region in which the well is situated. The commissioner SHALL (may) also provide for credits to be earned by persons performing geophysical work on state land, if that work is performed during the two seasons immediately preceding an announced lease sale and on land included within the sale area and

the geophysical information is made public following the sale. Credits may not exceed 50 percent of the cost of the drilling or geophysical work. Credits may be used during a limited period established by the commissioner and may be assigned during that period. Credits may be applied against (1) oil and gas royalty and rental payments payable to the state or (2) taxes payable under AS 43.55. A credit may not exceed 50 percent of the payment toward which it is being applied. Amounts due the Alaska permanent fund (AS 37.13.010) shall be calculated before the application of credits under this subsection.

AS 38.05.180 amended by adding a new subsection to read:

(bb) To encourage the development of the state's heavy oil resources, the Commissioner may reduce the base royalty by 50% on any lease for production from a zone containing crude oil with an API gravity of 20° or less. This reduced royalty rate shall apply for a maximum of 5 years. The last year that this reduced rate shall apply is calendar year 1997.

AS 38.05.180(j) amended as follows:

(j) To prolong the economic life of an oil and gas field, the Commissioner shall adopt regulations for all bidding methods to allow reduction of royalty on leases within later stages of production decline. The Commissioner may not grant a reduction of royalty on leases where the royalty rate was used as a bidding variable until two years' initial production from the field has occurred and each lessee requesting the reduction has

made a clear showing that the revenue from all hydrocarbons produced from the field is insufficient to produce a reasonable rate of return with respect to that lessee's total investment in the field.

TITLE 43 AMENDMENT

AS 43.55.013 amended as follows:

(b)(1) The economic limit factor for oil production of a lease or property shall be the lesser value computed according to the following two formula(s):

$$(1-[PEL/TP]) \exp ([460 \times WD]/PEL);$$

or $(1-[PEL/TP]) \exp ([55,000,000 \times WD]/[PEL \times TP/Days])$

where: PEL = the monthly production rate at the economic limit;

TP = the total production during the month for which the tax is to be paid;

WD = the total number of well days in the month for which the tax is to be paid;
[and]

Days = the number of days in the month for which the tax is to be paid; and

where "exp" indicates that the expression following it is an exponent.

AS 43.55.103(d) is amended to read:

(d) The monthly production rate at the economic limit for a lease or property is [presumed to be] 300 barrels times the number of well days for the lease or property during the month for which the tax is to be paid. [The taxpayer may rebut this presumption at a formal hearing under AS 43.05.240 by providing clear and convincing

evidence of a different monthly production rate at the economic limit for the lease or property. The hearing shall be held before February 15 of the year or within six months after commencement of oil production for a lease or property. The monthly production rate at the economic limit for the lease or property based upon the clear and convincing evidence of the taxpayer shall be calculated by dividing the value determined under (f) of this section into the average monthly direct operating cost determined under (e) of this section and shall be used for purposes of this section for all oil production during that calendar year from the lease or property.]

AS 43.55.013(e) and (f) are repealed.



Official Business

Alaska State Legislature

House of Representatives

Committee on Resources

Chairman Alvin Osterback

Pouch V
State Capitol
Juneau, Alaska 99811

16 March 1978

MINUTES

The House Resources Committee was called to order at approximately 1:30 p.m. in Court Room A of the Court Building by Chairman Alvin Osterback.

Members Present

Osterback, Chairman
Snider, Vice-Chairman
Akers
Eliason
Malone
Miller
Smith
Bennett

Members Absent

Urion

HB 854 Leasing of State land for oil and gas development

Testimony: Bob LeResche, Commissioner of Department of Natural Resources, stated that this bill represents a rejuvenation of the lease program including; 1) long term lease schedule, 2) published regulations providing for pre-leasing procedures, 3) HB 854. This bill fulfills the State's need for stability and predictability of oil and gas leasing program. There were several assumptions agreed upon for HB 854:

1. State needed a new look at the lease law to be comprehensive for 10 to 30 years
2. broad base of options for leasing methods
3. would provide for steady sales
4. report to the legislature as provided for in the bill
5. flexibility to hold joint sales with the Federal government
6. want to understand better what resources are for sale
7. protect social and environmental values affected by leasing
8. what the state to get away from reliance on cash bonus

He stated the major points of the bill:

1. require that Department of Natural Resources have a 5 year lease program
2. provides the State with a variety of leasing methods
 - a. State can work closely and compete with the Federal government
 - b. allow the State to adapt to changing conditions
 - c. creates certain tools

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AGG 1115677

3. create strong incentives for timely exploration and development of State acreage
 - a. lease terms reduced from 10 to 5 years
 - b. escalated lease rentals
4. reduced maximum acreage one person can hold
5. encourage broad base in Alaska oil exploration
 - a. reduction of acreage limit
 - b. have authority to restrict joint bidding in certain circumstance
6. left the unitization statute alone
7. stronger protection to take State royalty oil in kind--previously 1/8, now 1/6, also 100% gas discoveries
8. State right to secure information regarding exploration of State land
9. changed treatment of non-competitive leasing; acreage will not be offered non-competitively until first offered competitively.

This bill is a product of a thorough analysis of all leasing system used today. The key to the health of oil and gas in the state is amount of acreage made available in a predictable fashion without continual public questioning--made especially possible by the establishment of the 5 year lease agreement.

Jack Roderick, Deputy Commissioner of Department of Natural Resources stated that the State presently has two methods of leasing; 1) competitive leases offered on a bonus bid, 2) non-competitive leases offered through a simultaneous filing period. HB 854 puts forth 5 methods in which lease:

1. bonus bid system
2. royalty bidding with sliding scale
3. net profits form
4. work commitment
5. withholding of acreage

A provision provides that if a Commissioner uses one system more than 50% of the time in a year, he must report to the legislature.

Roderick explained the various methods of bidding:

1. a fixed royalty not less than 12 1/2% and a cash bonus, a sliding scale royalty
2. the bonus is fixed, a sliding royalty is bid upon
3. net profit is fixed, is possible to also fix the royalty and bid on the cash bonus
4. State tells lessee the type/amount of work that needs doing--highest bidder for a 5 year period receives the lease. Bid dollars are spent in exploration--State receives only the rent
5. land withholding which is possible currently under Alaska statutes

Roderick basically went through the bill illustrating the high points. He reemphasized that HB 854 classifies everything as competitive.

Milton Lipton, consultant for W.J. Levy & Associates, stated that introducing other alternatives hypothecates a great deal of money and diminishes the amount of funds that could be used for exploration. He explained his views on bidding variables; --bonus bidding means substantial dollars to the lessing party and diminished dollars for exploration

--royalty variable inflexible to the cost of the operation--this is un-attractive except in highly proven areas where costs are known
--net profit is attractive to firms and the State. The system would be done by regulation and doesn't have to be complicated. Also, there is no Federal taxation on net profits that go to the State but there still is State tax liability. There might be more interest from broader base of firms because of deferrment of payments to the State.

--work commitment bidding means the company that spends the most amount of money obtains the lease. Lipton has reservations. Whatever type of bid (i.e. sliding scale royalty) the Commissioner decides upon, the company would get a minimum work commitment so that the company can hold the lease by working it. His contribution to the entire area should be counted toward his work commitment as the State has learned something about the area.

--page 6, line 4, (d), to abate royalty is to save field (oil). If royal is in a lease as incentive, by bringing high royalty down, there will be a possible premature abandonment.

--page 6, line 15, (f), industry may want to block this section but the idea to withhold acreage is sound.

--(t), non-competitive awarding of acreage previously up for bid but received no bids could be abused--not good, but appreciates the sentiment

--(v), 100% gas rights could be a bad proposition as the gas and oil firms wouldn't know what the State might do. The State may discourage Alaskan exploration by keeping this in.

--(w), access to data: 1) must insure confidentiality, 2) and there should be a time lapse of perhaps years before disclosure to prevent firms' loss of bid. The department should have maximum access to data.

--page 12, line 19, (c) --Lipton feels that a change in 500,000 acres to 200,000 acres may be too drastic a cut as implementing a five year lease, progressive dead rentals and minimum work commitment would minimize the ability to build up acreage by the oil companies.

Mark Singletary, ARCO attorney, finds (a) - (f), pages 1 and 2 as a monumental task and subject to litigation--recommends legal review. Page 6, (f), concerning the "checkerboard" concept--feels there to be no real advantage to this subsection. He prefers to retain up front bonus bidding as this offers simplicity and security to a company who has a "hard row to hoe" in terms of looking and not finding. He also objected to the State claiming up to 100% of natural gas that is found.

A general discussion ensued where Malone stated that this bill provides the State with the knowledge of known income over a long period of time. He feels item (f) to be too broad but in general, in sympathy with the objectives.

With no further testimony, Chairman Alvin Osterback adjourned the Committee at approximately 4:40 p.m..

By: Jackleen Allen, Staff

Verified by: Susan Hunter, AA

AGG 1115679

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HOUSE RESOURCES COMMITTEE

TAPE #71

3/16/78

TESTIMONY OF JACK RODERICK, DEPUTY COMMISSIONER

DEPARTMENT OF NATURAL RESOURCES

There is a provision allowing the reduction of royalty during the later stages of the field. As you know that becomes very important in your declining fields to have the ability to reduce royalties, but it can't be reduced until two years have passed from initial production. I know Mr. lipton will probably speak to that -- of the inherent danger there is that a person will come in and bid a high royalty immediately when he goes on production comes to the commissioner and says please reduce my royalty; I can't make any money.

And the fellow who bid second to him of course has an (legitimate) objection because he bid what it was worth and another man came and bid more and found it wasn't economical as the second man predicted and yet comes to the commissioner and requests a reduction of royalty. That's one of the dangers of royalty bidding. That (clears) can be changed but in any event the commissioner should have the right to reduce royalties in declining years but on the

other hand, the state doesn't want to be in the position where it's helping uneconomic operators.

No questions from the Committee.

AGC 1115681

20652

HOUSE RESOURCES COMMITTEE
3/16/78
TAPE 71
TESTIMONY OF MILTON LIPTON
CONSULTANT FOR W. J. LEVY & ASSOCIATES

The higher royalty is bid the sooner it becomes a burden against the value of production therefore and the more onerous it becomes.

I'll come back to that in the context of abatement of royalty later on. But for this reason the royalty itself is an unattractive aspect of costs. Royalty bidding per se is an unattractive bidding variable excepting possibly in highly proven areas where the people who are bidding competitively have reasonably good expectations as to what would be found and fairly good knowledge of what costs may be and therefore instead of the royalty bidding a shot in the dark the royalty bidding can be made on a reasonably intelligent basis.

Not regarded as attractive among the alternatives.

I turn now from the bidding variables to the subject of the reduction of royalties. The commissioner's right to abate the royalty when this is a means of prolonging the productive life of the field. That's the item on page six subparagraph (d) and Jack Roderick referred to it and I feel obliged to speak about it because he said Mr. Lipton was going to talk about it. The commissioner has had that right to abate royalty under

your statute for some time. Our quarrel with this is not that the commissioner has the right to abate royalty it's that if you have in your lease sale the royalty as the bidding variable you have created an incentive for the competing companies to bid as high a royalty as possible and then in effect what you are doing is you are bringing the point of time when this high royalty that you invited into bid now becomes onerous and he's threatening to stop production. So he goes to the commissioner and he says let us abate this royalty. I think there is an incongruity between inducing the companies to bid the highest royalty possible and then creating the situation where they are almost driven to ask sooner than they otherwise would have for possible abatement of royalty and you're faced with a dilemma that if you don't abate the royalty it may result in premature abandonment of production before you would like it. It's not just abandoning production it becomes even more important earlier in the life of a field when the company is considering should we invest money to sustain the life of the field. Re-working the wells, for example, all the other things, drilling some in-field wells on a lease. Then the high royalty may become a burdensome thing and he decides that he is not going to make that investment unless the royalty is abated.

I think that one has to consider very carefully whether you use royalty bidding or the abatement of royalty or whether you stipulate in advance wherever royalty is the bid variable there

shall not be abatement of royalty. You create an incongruity between these two clauses in the lease.

AGC 1115684

20655

✓ w/ Bruce etc. re Ct. intro of inciv's bill -

HB 471 Eason, Carol, Larry, Mike K, Royce, Feinberg.

Admin / DO+G said no way on this part inciv among others.
want to avoid mkg Leon the villain -

bought leases below value - Phillips did a memo on it - avail. soon -
Jim wants Ed to do 2 things -

simple cover letter - impress. to prod. rev. implications on royalty
valid to look at # fields that wd be affected - Seal Island
wd only be aff'd - recov. exp. of 350 mn bbls (recov.) -
don't know how the infrastruc wd be constructed - figure
on some rate of return (10% min) - produce profile -

for Seal minimum 28.6 m barrels -

wd rev. no roy's parts this century -

would hist'l data - antiz. bonuses w/ another bidding system in
1979 -

by using NPS - prob; saved \$314 m - just on bonuses -

→ foregone revenues - 78.5 m. (A-H); Perm. Fund losses -

→ when do leases lapse? 1990/91 -

will rebid them later?

→ who does Sec. 3 affect? - Exxon, Nizakuk, Pt Thompson - nonprod.
West Sak - Mike K. ↳

→ Lipton testig on 78 AS 38 A's allowing NPS - get it. Steve Porter

technical problems of admin. .. potential of productivity no royalties at all. -

dev't acc'd already inc's in 2 A-H leases ~ \$97/8 m - 6 wells at about \$20m ea. + interest.

all costs - can't really figure - used only pot'l problem -
The incentive to gold-plate -

→ any precedent for this anywhere?

Swopie has info DOR doesn't

FOIA req. to Gov's Ofc / DNR / DOR for info they have?

HB 421 = Pt Thomson -

→ cheat showing - foregone revenue - who else bid on tracts?

cost of this bill in bbls

pot'l revenue if leases are not dev'd by 1990

→ lease provision regarding the expiration or loss if not prod'g or unitized - what other lease provisions?

→ Texas Eastern has asked to abrogate work commitment

→ confidence in reserve estimates? Hess est'd 600+ -

Texas Eastern is a gas pipeline co. in Houston, didn't know about Hess proposal -

Shell

unit history - unit req'ts - A-H will be operator?

prob. 100,000 bbls/day -

→ who wants the pipeline?

Hess - what to expect -

→ will ind. that outside fed'l acq'g might be worth 1/5 + dev'g w/ this strike -

→ fiscal note? PF impact

cd displace royalties leaving oil in TAPS if dev'd soon

Oil and Gas Topics of Interest

Discussion topics for the Senate Oil and Gas Committee. Prepared February 1988 by the Division of Oil and Gas.

Leasing Schedule--New Sales. This year the department added four sales to the state's five-year oil and gas leasing program (1988 to 1992). The four new sales are North Slope Sale 66A (exempt), Cook Inlet Sale 67A (exempt), White Hills Sale 61 and Beaufort Sea Sale 68. The state's 1988 leasing schedule is shown below.

Sale Number	Sale Name	Proposed Date
54	Kuparuk Uplands	January 1988*
55	Demarcation Point	June 1988
66A	North Slope Exempt	June 1988
52	Beaufort Sea	January 1989
56	Alaska Peninsula	June 1989
67A	Cook Inlet Exempt	June 1989
59	Cook Inlet	January 1990
57	North Slope Foothills	June 1990
64	Kavik	January 1991
65	Beaufort Sea	June 1991
61	White Hills	January 1992
68	Beaufort Sea	June 1992

*Sale 54 was held January 26, 1988--see discussion below.

North Slope Sale 66A will be the state's first sale to take advantage of AS 38.05.035(e)(7), which was passed by the legislature last year. The statute allows the department to hold an exempt acreage sale without writing a best interest finding if one has been issued previously for the area within 36 months of the sale date.

The proposed Sale 66A acreage is located within an area known as the "Kuparuk Uplands," and includes acreage previously leased, but subsequently relinquished, from sales 45A, 47 and 48. The department received a number of industry requests for an exempt acreage sale in this area. The sale area includes approximately 219,913 acres of land.

Cook Inlet Sale 67A will include eligible lands in the Cook Inlet region that have been specifically nominated by industry. The actual lands that will be offered in the sale have not yet been identified by the department. Eligible lands in the lower Susitna Valley, on the Kenai Peninsula and submerged lands in Cook Inlet may be offered.

Proposed Lease Sale 61 was previously scheduled for September 1990. The sale area consists of approximately 875,000 acres located immediately south of acreage offered in sales 47, 48 and 54. The Trans-Alaska Pipeline System lies to the east of the sale area and to the west is the Colville River.

Proposed Sale 68 consists of approximately 393,000 acres of state-owned tide and submerged lands offshore of the NPRA, including some submerged lands whose ownership is currently disputed. The sale is centered around Barrow, extending from Tangent Point in the east to near Nulavik in the west. Beaufort Sea lands offered previously in sales 50, 52, and 55 may also be offered for lease in the sale.

The state's current leasing schedule provides for two to three sales each year. It is a more modest schedule than leasing programs proposed during the early 80's, when at least three sales, and as many as five sales, were offered each year. The department believes the current schedule provides an optimum number and mix of sales. It is composed of sale acreage near areas of known oil production, primarily on the North Slope and in Cook Inlet. That acreage has the greatest likelihood for holding future oil and gas discoveries. The schedule will allow industry to devote its tight exploration budgets to areas of state land having the best oil and gas potential.

Kuparuk Uplands Sale 54. Sale 54 was held January 26, 1988. It included 89 tracts, or approximately 421,808 acres, lying between the Colville River and the area of Kuparuk Uplands Sale 48. It also included acreage in the Colville River delta.

The sale utilized cash bonus bidding with a fixed 12.5% royalty, and included a 15% Exploration Incentive Credit (EIC). The sale earned \$4.6 million, or an average bid of \$13.83 per acre. Eleven bidding groups submitted 164 bids on 72 tracts.

Lessees will earn EIC's at a rate of \$300 per foot drilled for the first exploratory well per tract, provided that credits do not exceed 15% of the total exploratory well costs. The credits must be earned and used within five years of the effective date of the lease.

Camden Bay Sale 50 Litigation. The department currently is involved in litigation concerning Camden Bay Sale 50, held June 30, 1987. The lawsuit was brought by the Trustees for Alaska, Northern Alaska Environmental Center, National Parks and Conservation Society, Wilderness Society and Sierra Club.

Briefs were filed in Superior Court late last year. The judge assigned to the case is Judge John Bosshard, III. To date, the court has not set a date for oral argument. The department, however, anticipates resolution of the suit within the next few months.

Demarcation Point Sale 55. Sale 55 is the next sale on the state's leasing schedule. The sale is located offshore of the Arctic National Wildlife Refuge (ANWR) between the Hulahula River (west of Kaktovik) and the Canadian border. The department anticipates that industry interest in the sale will be high. The preliminary finding for the sale was issued February 4, 1988. Following public and agency review of the preliminary finding, the final finding and decision of the director will be issued on April 25, 1988.

As with Sale 50, the department expects that a decision to proceed with Sale 55 will be controversial. Debate will center on the sale's effect on ANWR and the importance of the sale area for bowhead whales and subsistence hunting.

The division currently is conducting its pre-sale evaluation in order to select an appropriate bidding method for the sale. The division's evaluation of the sale area will be aided greatly by data from two exploratory wells drilled nearby on adjacent lands and new computer equipment recently purchased to process seismic data.

The two exploratory wells that have been drilled near the Sale 55 area are Tenaco's Aurora well and the KIC well in ANWR. In November 1987, Tenneco, in partnership with 10 other companies, began drilling its Aurora prospect just beyond the three-mile limit, about 22 miles northeast of Kaktovik. Because of an agreement with the Department of the Interior, the division has access to the information from this well as it is being drilled. The KIC well, which is located about 14 miles southeast of Kaktovik, was drilled by the Arctic Slope Regional Corporation in association with Chevron, Standard Alaska Production Company and BP Alaska. The confidentiality period for the KIC well is scheduled to end April 24, 1988. At that time, the division will have access to the well data. The data from both wells are important because they provide the only available direct information about the subsurface of the sale 55 area and adjacent lands.

With the purchase of the new computer equipment, the division now has the capability of digitally reprocessing seismic data in order to improve its quality. The equipment will allow the division to conduct a more in-depth analysis of available data, and should greatly improve the pre-sale evaluation for this and all other future sales.

Leasing & Development in ANWR. A number of bills have been introduced in Congress concerning oil and gas development on the ANWR coastal plain. H.R. 39 (Rep. Udall) and S. 1804 (Roth, Bradley and Chafee) would prohibit oil and gas leasing on the coastal plain by including it in the national wilderness system. On the other side, S. 1217 and H.R. 1082 (respectively, the Murkowski-Stevens and Young bills), would open ANWR to oil and gas leasing. H.R. 3601, sponsored by Congressman Jones (N. Carolina), is an "exploration-only" bill--allowing only four exploratory wells to be drilled on the coastal plain, the results of which would be evaluated before determining whether or not to proceed with leasing. A bill recently introduced by Senator Johnston (Louisiana) authorizes a competitive oil and gas leasing program in ANWR, but provides Alaska with only 50% of the resulting revenues. A possible amendment to that bill, by senators Wirth, Evans and Bumpers, calls for a two to three year moratorium on leasing, until a comprehensive study can be conducted to provide Congress with adequate energy policy information. Another House bill expected to be introduced by Congressman Anderson (California) calls for leasing, but also reduces the state's share of the revenue from 90% to 50%.

Division personnel have testified before U.S. Congressional committees and Alaska legislative committees in support of opening ANWR to further exploration and development. These committees include the U.S. House Subcommittee on Water and Power Resources, the U.S. Senate Committee on Energy

and Natural Resources, and the Alaska Senate and House Resources Committees and the Joint Oil and Gas Committee. Personnel have also given presentations to various professional and civic organizations, including the Resource Development Council (RDC), the Free Committee of the Anchorage Women's Auxiliary, and the Public Lands Committee of the Interstate Oil Compact Commission (IOCC).

The division also is providing information to interested individuals and organizations to explain the state's position on the ANWR land exchanges.

Beaufort Sea Lease Boundary. The jurisdictional boundary dispute between the state and federal governments (United States v. Alaska, No. 84 Original in the United States Supreme Court) continues to be a problem when planning lease sales in the Beaufort Sea; nor is there any indication how long it will be before the dispute is resolved. The suit has been pending for eight years. Moreover, the parties have now waited more than one year for the Court's Special Master to issue his recommended decision in the case. Beyond the Special Master's recommendation, the Supreme Court's briefing, argument and decision process must occur before a final judgment is rendered.

Eventually, a judicially decreed state/federal boundary in the Beaufort Sea will result from resolution of United States v. Alaska. In the interim, the division is attempting to negotiate an agreement with the federal government that would fix existing state/federal leasing boundaries in the Beaufort Sea. These efforts were initiated in 1986, and discussions continued throughout 1987. The division would like to avoid the costs and legal uncertainty associated with adjusting existing lease boundaries after the state/federal boundary is fixed by judicial decree. Accordingly, we believe the state/federal jurisdictional boundary should be established using the same geographic data used to determine any previously agreed-on state/federal leasing boundary; or, at a minimum, the leasing boundary should be fixed for the life of the oil and gas lease.

Lacking a decreed state/federal boundary, the state and federal governments must negotiate an agreement under Section 7 of the Outer Continental Shelf (OCS) Act to lease the disputed lands. Section 7 agreements have been successfully negotiated for OCS sales 71 and 87. However, no agreement could be reached for Sale 50. As a result, the state pulled back its seaward leasing boundary to a conservative position to avoid the possibility of an injunction to delay the sale. Currently, discussion is occurring between the Minerals Management Service (MMS) and the division for a Section 7 agreement for OCS Sale 97. However, given the extremely late invitation by MMS to enter into a Section 7 agreement for Sale 97, it is unlikely that our differences can be worked out in time to sign an acceptable agreement prior to the final notice of sale, which is due in March 1988.

Use of Explosives in the Marine Environment. The use of explosives for seismic operations in the marine environment was prohibited by the state in 1975. In 1985, the division published a report stating that the limited use of explosives is necessary if reasonable quality seismic data are to be obtained from areas where non-explosive energy sources are ineffective. The department concluded, however, that insufficient information was available

concerning the effects of explosives on juvenile salmon to warrant a change in state policy at that time. The division's report recommended that a test be conducted to determine the effects of explosives on juvenile salmon.

In 1986, the Alaska Oil and Gas Association (AOGA) conducted a study to test the effects of linear explosive detonations on juvenile fish, especially salmonoids. The results of the AOGA study were published in October 1987 and concluded that the best estimate of the lethal range for juvenile salmon from a linear explosive is 150 meters. The study recommends that more information about the seasonal distribution of fish be gained in Alaskan waters where linear explosives are needed to acquire seismic data.

The division is presently reviewing the study, and will request comments and recommendations from the departments of Fish & Game and Environmental Conservation. Following the study's review, the division will recommend to the cabinet whether or not to pursue a change in state policy. If a decision is made to pursue a change in state policy, the division will hold public meetings in affected communities to explain its recommendation and to solicit comments on the subject.

Royalty Oil Export. Last year, the department successfully concluded a one year contract to sell for export 97% of the state's daily royalty oil production (3,600 barrels per day) from the fields on the west side of Cook Inlet. Those fields are Granite Point, MacArthur River, North Trading Bay and Trading Bay fields. Delivery began in July of 1987 to Chinese Petroleum Corporation of Taiwan, which agreed to pay a premium of \$1.83 per barrel above what the state would have received had it left the oil in-value. The department issued a solicitation for offers in January 1988 for another one year contract, which will follow the expiration of the Chinese Petroleum Corporation contract. The proposal calls for a new contract to be signed by June 1988, with a date for first delivery scheduled for December 1988.

Free Trade with Canada. There is broad agreement between the governments of Canada and the United States to assure the freest possible bilateral trade in energy, including nondiscriminatory access for the United States to Canadian energy supplies and secure market access for Canadian energy exports to the United States. The federal government has agreed to allow exports of Alaskan oil to Canada, up to 50 thousand barrels per day on an annual average basis, subject to a condition that such oil be transported from Alaska on U.S. flag ships. Given the restrictions on state government (such as the six month notice provision under the terms of the lease to the producers), it is improbable that state royalty oil will be part of this export at least in the near term.

AOGA Stipulation Study. In response to a request by AOGA, the state's resource agencies, in conjunction with the Division of Governmental Coordination, are preparing a letter explaining the state's rationale behind various stipulations attached to oil and gas development projects. The letter is presently in draft form. Once finalized, the letter will represent the consensus of the resource agencies concerning the need for the state's lease

stipulations. The letter also will invite AOGA, if it disagrees with the state's rationale, to conduct a stipulation cost/benefit analysis for the state's further consideration.

Oil and Gas Incentives Analysis. The division recently concluded a review of ways to stimulate petroleum activity in the state. In addition to reviewing the state's taxing and leasing policies as well as incentives currently available in Alaska, the division reviewed legislative and administrative incentive programs enacted by the other petroleum producing states and Canadian provinces to provide exploratory and development-related assistance to the oil industry.

As most "lower 48" oil producing states have a limited land base, the majority of states that enacted incentive programs utilized severance tax relief as the primary means to stimulate petroleum activity. In addition, because most of the production in these states comes from stripper wells (ie. wells that produce less than 10 barrels of oil per day (bopd)), the states generally adopted programs designed to postpone the abandonment of this production and ultimate loss of oil reserves.

Canadian provinces have adopted a variety of incentive programs, ranging from outright credit or cash grant programs to royalty/tax holidays and price sensitive sliding scale tax formulas to stimulate economic activity. Currently, the royalty/tax rates in Canadian provinces vary from 10% to 44% depending on the type of oil.

In comparison with the other oil producing states and provinces, Alaska is already providing numerous incentives for exploration and development. In the wake of declining world oil prices, the state has offered some of the lowest minimum bid and per acre rental terms available for competitive leases issued anywhere in the United States. In addition, most of the state's leases are encumbered with only the statutory minimum one-eighth royalty share of oil for the state. The state also has offered Exploration Incentive Credits (EIC's) [AS 38.05.180(i)] in state oil and gas lease sales, most recently in Sale 54, to share some of the risks associated with drilling exploratory wells. Since 1982, the state has granted credits amounting to almost \$36.6 million.

In the past, the state also had a discovery royalty provision which reduced, for a period of ten years beyond the date of discovery, the state's royalty to 5% from production allocated to a lease where the discovery involved a new geological structure (see Laws of Alaska, 1959, Chapter 169, page 243). The discovery royalty program was an incentive to encourage oil companies to come to Alaska, then a newly formed, cash-poor state. It generated significant drilling activity in Cook Inlet and thus accelerated oil and gas exploration and development of state lands. The discovery oil provision was repealed in 1969, but remains in effect for some state leases issued before 1969. To date, ten wells have been certified as discovery wells, and two applications are pending certification.

Finally, under AS 38.05.180(j), the state may allow for a reduction of royalty to compensate for increasing cost in the later stages of production decline. The reduction, however, cannot be granted until two years of initial production from a field has occurred. The lessee also must clearly show that

the revenue from all hydrocarbons produced from a field is insufficient to provide a reasonable rate of return with respect to the lessee's investment in the field.

NGL Settlements. A controversy has developed between the state and North Slope producers of the Prudhoe Bay, Lisburne and Kuparuk fields concerning the processing fee deducted from the reported value of sales gas and natural gas liquids (NGL's) produced from those fields. The controversy centers on what processing fee, if any, is deductible from the producer's royalty payments.

Three gas facilities are currently operating on the North Slope. These facilities, and particulars, are as follows:

- a. Prudhoe Bay facility: December 1986 startup; December 1987 production was 54,048 BPD NGL's.
- b. Lisburne Reservoir facility: June 1987 startup; December 1987 production was 2,206 BPD NGL's.
- c. Kuparuk Reservoir facility: April 1985 startup; December 1987 production was 3,625 BPD NGL's.

All three facilities also produce "dry" natural gas for unit use and marketing. The NGL's and some natural gas are being sold, and royalties are being reported to the state. The Prudhoe Bay gas facility also produces fluids (e.g., ethane and propane) used in enhanced oil recovery operations in the field.

North Slope producers have submitted pricing proposals to the state for the NGLs and sales gas processed by these facilities. The pricing proposals would be used to determine a "lease plant split" processing allowance for each operator. The proposed processing allowances suggested by these producers are:

a. <u>Sadlerochit facility:</u>	ARCO:	\$0.30/MCF (Sales Gas) \$4.39/bbl (NGLs)
	Exxon:	\$0.45/MCF (Sales Gas) \$2.54/bbl (NGLs)
	Standard:	\$0.75/MCF (Sales Gas) \$7.34/bbl (NGLs)
b. <u>Lisburne facility:</u>	ARCO:	\$0.32/MCF (Sales Gas) \$19.21/bbl (NGLs)
	Exxon:	\$0.47/MCF (Sales Gas) \$19.99/bbl (NGLs)
c. <u>Kuparuk River facility:</u>	ARCO:	\$0.24/MCF (Sales Gas) \$7.79/bbl (NGLs)

The processing allowance, if accepted by the state, would be deducted on a per barrel basis from the royalties paid to the state by each producer. In the case of the Lisburne facility, however, the proposed processing allowance is greater than the reported selling price of crude oil at Pump Station #1. Consequently, the difference between the proposed processing allowance and the crude oil price would then be deducted from the total royalties owed the state from all production.

The state has issued a formal notice of its disagreement with the processing allowances proposed for the Prudhoe Bay and Lisburne facilities. The state's position concerning the Kuparuk River facility currently is being drafted. For the Prudhoe Bay facility, the state has proposed a deduction of \$0.31/bbl if the liquids are to be reported as NGL's. Alternatively, the state proposed a deduction of \$0.67/bbl if the liquids are to be reported as oil. The \$0.67/bbl figure represents the agreed to Prudhoe Bay oil field cost allowance. At Lisburne, the state has proposed a deduction of \$0.67/bbl, the standard oil field cost allowance in the Prudhoe Bay Unit.

Thus far, ARCO and Exxon have rejected the state's counter proposals. As both sides appear firm in their respective positions, resolution of the processing allowance proposals appears headed for litigation.

Niakuk and Endicott Discovery Royalty Certification Applications. On May 22, 1987, Standard Alaska Production Company filed an application for certification of its Sag Delta No. 4 well as a discovery in the Endicott reservoir. For administrative reasons, the application was processed in conjunction with a similar request for Standard's Niakuk No. 5 well, which was submitted on August 27, 1987. The affected leases were issued on January 24, 1967 at Competitive Oil and Gas Lease Sale 18, and consequently would qualify for discovery royalty under the statutes.

If approved, the royalty rate for production from each lease would be reduced from 12 1/2 percent to 5 percent for a 10-year period beginning from the date of each respective discovery. The reduced royalty period for the Endicott discovery lease (Sag Delta No. 4 well) would be from April 1, 1978 through March 31, 1988. Because production from this lease began in October 1987, the royalty reduction for the Endicott discovery lease would only be effective for about 6 months. The Niakuk reduced royalty period would be from May 1, 1985 through April 30, 1995. Although no oil has yet been produced from the Niakuk reservoir, a portion of the oil production from the Lisburne unit has been allocated to the Niakuk discovery lease.

STEVE COWPER
GOVERNOR



STATE OF ALASKA
OFFICE OF THE GOVERNOR
JUNEAU

JWS - J. Egan

January 28, 1988

Mr. Leon Hess
Chairman
Amerada Hess Corporation
1185 Avenue of the Americas
New York, NY 10036

Dear Leon,

This is a somewhat tardy reply to your proposal to provide tax and royalty relief for the Seal Island leases. I have decided against the proposal, and I want to explain my reasons.

First off, I appreciate the spirit in which this proposal was made. You and Ron were very clear about your objectives and realistic about the political implications that would attach. I like a direct approach and normally do things that way myself.

As you know, any decision I make in this area must reflect a state policy which applies to the whole industry. At this time there are a number of outstanding leases which were purchased at a time when oil price projections were more sanguine than they are today. Many of those leases provided for a net profit share in lieu of larger up-front bonuses, as was the case with Amerada Hess at Seal Island.

Your proposal would benefit the state because of the jobs which would be created. It's hard to tell about the effect on state revenues, which also translates into jobs. That would depend on a judgment as to whether TAPS would otherwise be filled to capacity; if so, the oil produced under this incentive program would displace other oil on which the state was receiving its regular revenues. For the next few years, I am informed that TAPS will probably be operating at its nominal maximum capacity of 2.1 million bpd. If that's right, then the effect will be close to a wash in terms of jobs, although my stated preference is for private-sector employment.

RECEIVED

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DIVISION OF OIL & GAS
ANCHORAGE, ALASKA

Mr. Leon Hess

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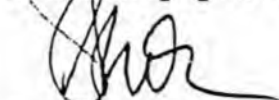
January 28, 1988

The political effects of this proposal must be assessed as well. While we are looking at the possibilities of incentives, given the current TAPS throughput the major producers are saying they don't want any of that kind of help. There is also the question of interference with the normal developmental order which is established mainly by relative cost. Thirdly, a lot of people don't want to establish any kind of incentive regime. They're already mad at the effect of the so-called "economic limit factor" legislation of 1981.

For the moment at least, my judgment is that when all the above factors are considered, a major departure from current policy isn't warranted. I know you and Ron disagree with this analysis but that's where I come down on it.

I hope things are otherwise well with you, the company, and the Jets, and I look forward to seeing you again in the near future.

Sincerely yours,



Steve Cowper
Governor

MEMORANDUM

State of Alaska

DEPARTMENT OF NATURAL RESOURCES
DIVISION OF OIL AND GAS

TO: James E. Earl
Director

DATE: February 19, 1988

FILE NO:

TELEPHONE NO: 762-2589

FROM: Ed Phillips
Petroleum Economist

SUBJECT: Minimum Fiscal Impacts
of the Hess Proposal as
Represented by HB 471.

HB 471 introduced by Representative Gruenberg appears to be a clone of an earlier proposal offered to the state by Leon Hess for royalty and tax relief at Seal Island. HB 471 would generalize the applicability of royalty and tax relief to other North Slope "reserves" particularly Pt. Thomson and West Sak. In an earlier memo the Hess Proposal and its cost in barrels of oil for the Seal Island prospect only was specifically analyzed. With minor changes that analysis is produced below. The issues raised in the analysis are still valid. The fiscal cost of applying the proposed statute could be substantial and the gains possibly chimerical.

As is often the case, the potential "costs" of the proposal are more easily discernible than the potential benefits. The potential "costs" of the proposal are the foregone royalties and taxes. These would amount to about 25 to 30% of the gross production for the period before capital recovery or December 31, 1999, whichever is less. These revenues would be forgiven during the peak production phase of the typical field. The potential benefits result from transforming fields from submarginal status to profitable. This transformation in itself does not assure that benefits equal or exceed costs. In some cases, the forgiveness may only shift forward by a year or two a particular field's development. In this case it is hard to argue the wisdom of the forgiveness. In other cases the forward shifting of development and production may be much more dramatic. Until we have more evidence of which phenomenon is more likely it will be exceedingly difficult to assess the potential benefits of this proposed legislation.

Assumptions

1. Recoverable reserves at North Star/Seal Island are estimated to be 350 million barrels. State leases have an estimated 80% of recoverable reserves. The remaining reserves are on federal leases.
2. Project must earn after tax 10% real rate of return to be feasible.
3. All state leases have 20% royalty rate.
4. Peak production at 100,000 barrels a day through first four years, then production declines at 15% per year. Total field life is 16 years.
5. Time value of production is evaluated at three interest rates, 5%, 10% and 15%.
6. Price assumed to be constant so that analysis is done in terms of barrels of oil. This is the index number for measuring costs.

Methodology

1. Compute the present value of production as of time zero. Then lag time zero for various delays that apply discount factors to the delays. The present value is stated in terms of "discounted" barrels. For example, the present value of 350 million barrels of oil produced over a sixteen year period at 5% discount equals approximately 217 million barrels of oil as a present value equivalent. At 10% this value drops to 192 million barrels, and at 15% 171 million barrels. (The method used for these calculations is readily found in Newendorp, Paul D. "Decision Analysis for Petroleum Exploration," Petroleum Publishing Company, Tulsa, Oklahoma, 1974, Appendix I, pp: 651-659.)
2. Payback (recovery of invested capital) was estimated by two methods. First, the "Rule of 72" was used. This "rule" allows one to estimate payback by dividing the rate of return into the number 72. For example, if a particular investment earns 10% per year, it will payback in approximately 7.2 years. The "Rule of 72" is a quick and dirty way to compute doubling times for compound interest rates. The other method used was to divide the rate of return into 100. This works reasonably well for uniform cash flows. (This method is illustrated in Megill, Robert E., "Exploration Economics," Petroleum Publishing Co., Tulsa, Oklahoma, 2nd Ed., 1979, pp. 83-84.) Finally, doubling times for compound interest were computed directly. These techniques will yield estimates of undiscounted payback on original investment, thus they represent minimal estimates of payback periods. Capital recovery calculations permit payback with imputed interest and represent a maximum estimate of payback.

This analysis does not forecast a rate of return for Seal Island. It only examines the conditional statement that if Seal Island earns X rate of return, then payback will take approximately Y years. This proposition is evaluated for 10 and 15 percent rates of return (ROR). This methodology can be used for any ROR.

3. "Cost" to the state is measured in terms of undiscounted oil as well as the present value of royalty barrels foregone during payback period under the North Star (Seal Island) proposal. This simple methodology can easily be extended to include severance taxes. The inclusion of these taxes adds about 50% to the annual cost estimates, but shortens the payback period. Another potential "cost" to the state is from the delay in development and production at Seal Island due to submarginal economics attributable to state's royalty and severance taxes. This delay cost is measured for 5, 10, 15 and 20 year delays, at 0, 5, 10 and 15% discount rates.
4. Caveat: This methodology is admittedly crude, but very little data are available to justify a more sophisticated, yet questionably more accurate approach. This approach will, at least, frame the discussion in more analytical terms.

Results

- Given an assumed 350 million barrels of recoverable reserves, the state's 20% royalty share would be 56 million barrels of undiscounted oil. (This total could be as high as 84 million barrels with the inclusion of the severance tax.) In discounted barrels this claim drops to 34.6 million barrels at 5%, 30.7 million at 10% and 27.4 million at 15% if the field could start producing as of today.

Table I

Present Value Barrels
Royalty Share

Discount Rates	Delay Times					
	0 Years (millions of BBls)	5 Years (millions of BBls)	10 Years (millions of BBls)	15 Years (millions of BBls)	20 Years (millions of BBls)	
0	56	56	56	56	56	
5	34.6	27.1	21.2	16.7	13.1	Δ 8.1
10	30.7	19.1	11.8	7.4	4.6	Δ 7.2
15	27.4	13.6	6.8	3.4	1.7	Δ 5.1

- The reality of Seal Island economics and construction schedules vitiate columns one and two as possibilities. The maximum gain to the state if the delay is reduced by 10 years, is equivalent to 8.1 million royalty barrels of oil (Column 3 minus Column 5 at a 5% discount rate). At discount rates of 10 and 15 percent the gain associated with expedited development is less.
- What is the royalty "cost" to the state of waiting until payback in order to capture this "gain"? The cost depends upon the rate of return on investment. If the rate of return is 10%, simple payback can take from 7.2 years by the "Rule of 72" or 11.5 years if operators are allowed a 10% rate of return on their investment before payback is complete. This would imply a minimum of 76% of recoverable reserves or about 16.1 million present value royalty barrels (42 million actual barrels) would be produced at no royalty value to the state. The maximum estimate would be about 17.4 million royalty barrels (46 million actual barrels). This means that about 82% of the field's recoverable reserves would be produced before the state would begin to receive its royalty share. The "actual" barrel estimates were derived from the field's estimated production profile as stated in Assumption 4.

At higher rates of return, simple (interest free) payback is less onerous. Payback can be achieved in five years if the project earns 15%. With this ROR payback even with imputed interest of 10% is achieved in about eight years. The cost is between 12.5 to 15.6 million present value royalty barrels (28.6 million to 41 million actual barrels).

Including a severance tax forgiveness does not change the actual barrel sacrifice by the state, but it does increase the present value barrel cost. This result follows directly from the greater "upfront" sacrifice by the state at peak production rates. The implied gain is faster payback, hence earlier reimposition of the royalty and severance tax.

Thus, for the present value equivalent of approximately 16 to 17 million barrels, (42 to 46 million actual barrels) one could argue that production would be hastened by 10 years. But that would be giving the operator benefit of all of the best assumptions. What if, in reality, the state was only purchasing a year or two in expedited development? The cost is still the same, but the benefits decline considerably. Whereas costs were only double the benefits where production was hastened by 10 years (16 million cost, 8 million benefits), the benefits approach zero as the delay difference declines. Suppose allowing payback only reduced delay by 5 years from 15 to 10 years, then the gain is only 4.5 million present value bbls at most. (Column 3 minus Column 4.) If production was only affected by one year, the benefit is reduced to 1 million barrels. The cost is still 16 million barrels.

Some caveats are important. The preliminary results outlined here may be sensitive to assumptions about field size and decline rates. Given economics of scale and concomitant longer, peak production periods, it is likely that payback would occur earlier for a significantly larger field. (This effect would follow from a higher ROR associated with the larger field.) A rapid real increase in oil prices would also change this result by increasing the ROR. The relationship between the ROR and payback would not change.

Conclusion

1. For a minimum royalty oil cost of 28.6 to 46 million barrels the state may get something.
2. Unless real oil prices substantially increase, the state will receive no royalty payments from the proposed development in this century.

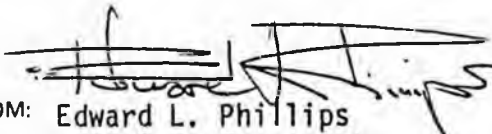
MEMORANDUM
DEPARTMENT OF NATURAL RESOURCES

State of Alaska
DIVISION OF OIL AND GAS

TO: James E. Eason
Director

DATE: January 8, 1988

FILE NO:


FROM: Edward L. Phillips
Petroleum Economist

TELEPHONE NO: 762-2589

SUBJECT: Hess Proposal, or
"Foregone Conclusions"

One point overlooked in the Amerada Hess discussion is the "savings" already transferred to Amerada Hess by the state as a result of the net profit bidding system employed in Sale 30. At the date of the sale (12/12/79), price expectations were extremely bullish. The Iraq/Iran war had been underway for a few weeks and spot oil prices, reflecting the uncertain outlook of the war, were in the \$35.00 to \$40.00 a barrel range. Market contract prices were moving up, and many price forecasters saw no end in sight. For example, the March 1980 Department of Revenue forecast projected the price of Saudi Marker Crude at \$46.43 in 1985, \$57.91 in 1990, and \$143.17 in 1996 (a perfect example of the power of compounding). Parenthetically, yesterday's (7 January 88) Saudi spot price was \$16.40. Markets have little tolerance for the compounding process. This forecast was not, by any means, off the wall--but represented a "middle of the pack" estimate.

The petroleum potential of the Beaufort Sea looked extremely attractive (profitable) with the price expectations of the period. Against this background, the winning bidders at Seal Island paid a total of \$19.2 million in bonus payments for the state tracts overlying the prospects. Amerada Hess paid \$6.9 million for its two tracts. In addition, the net profit share (NPS) bids ranged from 85.26% to 93.2%.

At that time, our analysis indicated that the same tracts, if sold on a bonus bid basis with a 20% royalty, were worth an estimated \$333 million, and possibly much more. The state/federal price assumptions used for the presale analysis were relatively conservative.

One could argue that the NPS bidding system permitted "savings" to the winning bidders of approximately \$314 million. Specifically, Amerada Hess paid \$6.9 million for tracts the state estimated to be worth about \$120 million. Thus, NPS bidding saved Amerada Hess over \$113 million, and possibly much more. In fact, it is not clear that Amerada Hess possessed the financial resources to win the tracts under a conventional leasing system. The major North Slope operators (ARCO, Sohio, Exxon) had deeper pockets, and were clearly better positioned to bid higher cash bonuses had the cash bonus been the bidding variable for the state tracts, as it was for the adjacent federal tracts overlying the Seal Island structures.

As a conceptual exercise, one can compute the true savings to Amerada Hess by looking at what the \$113 million could have earned them over the eight year time period since the sale. At a 10% rate of return (ROR), Amerada Hess would have earned almost \$129 million since the sale. If their ROR was 15%, their earnings would approach \$233 million.

James E. Eason
January 8, 1988
Page 2

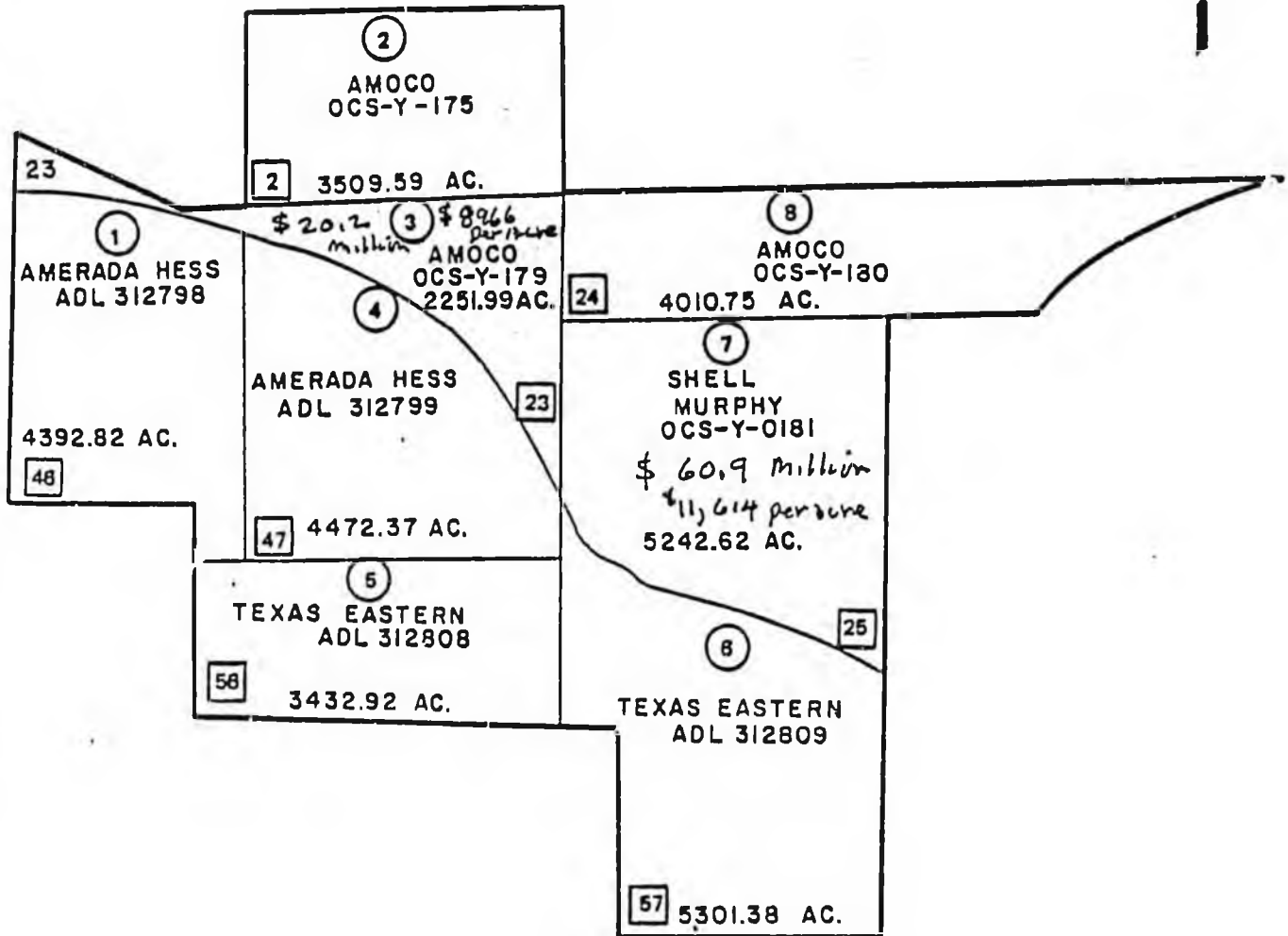
Thus, to this point in time the major sacrifice has been by the state in foregone bonuses and Permanent Fund contributions, including potential interest earnings. The Permanent Fund share of the estimated foregone bonuses would be \$78.5 million. This amount would have accrued to \$219.53 million by January of this year.

The current proposal appears to extend the state's sacrifice to a "foregone" conclusion.

Attachment

1269E

State Leases Bonus Bid = \$875.00 per acre
 Federal Leases Bonus Bid = \$10,808 per Acre
 Fed Royalty 16 $\frac{2}{3}$ % + Sliding Scale Royalty to
 Max of 65 %



LEGEND
 UNIT OUTLINE ———
 LEASE BOUNDARY ———
 UNIT TRACT NO. (1)
 LEASE SALE BF (2)
 TRACT NO.

NO SCALE

**EXHIBIT B
 SEAL UNIT
 BEAUFORT SEA, ALASKA**

December 3, 1987

MEMORANDUM

TO: Jan

SUBJECT: State Chamber Speech

Making Alaska more competitive in the truly international market for limited oil industry investment capital will increase economic activity, increase employment both in primary and secondary industries, and increase long term income to the state at a time when Alaska needs it the most.

Currently the Division of Oil and Gas is reviewing incentive legislation from several other states and Canadian provinces, and they have indicated that specific recommendations will be made to Commissioner Brady and the Governor in mid-December.

My own review of much of the same legislation has concluded that there are several incentives which could be particularly effective in Alaska. The general scope of these different types of incentives are summarized in the handout.

When we talk about incentives we need to consider the 3 R's: RESOURCE, RESERVE, & ROYALTY. You start with a resource in the ground. It doesn't become a reserve until someone drills and discovers it. The state then gets the royalty after production begins. What we are trying to accomplish with incentives is provide the impetus to change reserves into royalties and economic development for those situations where it wouldn't happen under current economic conditions.

(HERE IS THE TEXT OF THE HANDOUT. EACH SECTION IS FOLLOWED BY ADDITIONAL INFORMATION FOR YOU TO PRESENT)

SEVERANCE TAX EXEMPTIONS AND ROYALTY HOLIDAYS: Encourage development of new reserves by offering limited time severance tax exemptions and royalty holidays for new wells drilled during a specified time period. Such a program could be designed so that the exemption would be reduced if oil prices rise above a predetermined level.

(This would be similar to:

1. Alberta's Crude Oil Royalty Holiday Program which allowed for the greater of a 12-month royalty-free period for each eligible well to a maximum of \$1 million per well, or a royalty exemption determined by applying a formula to the specific characteristics of the well.
2. Saskatchewan's Royalty/Tax holiday. During the period January 1, 1987 to June 30, 1988, eligible wells and projects will receive a three year royalty or tax holiday. During the period July 1, 1988 to June 30, 1989 eligible wells and projects will receive a two year royalty or tax holiday.
3. Louisiana's Severance Tax Exemption Plan provided that wells drilled between July 15, 1986 and July 15, 1987 will pay no severance taxes through 1990, and provided an incentive to drill marginal wells on known reservoirs. Louisiana's Economic Acceleration Plan provides no tax on development through 1989 for discoveries after July, 1986 and has no production limits on its exemption which provides a significant incentive to explore for new prospects.
4. These two programs in Louisiana were enacted in 1986 to provide a significant incentive to drill new wells. It obviously worked since in 1987 the state of Mississippi felt compelled to enact very similar legislation in an effort to compete with Louisiana for limited drilling activity.

DISCOVERY ROYALTY: Could be structured much the same as the state's previous discovery royalty statutes, which were repealed by the Legislature in 1969. Would allow a limited time reduction in the royalty rate for a producer who discovers and produces oil and gas from a state lease within a specific timeframe.

(The Discovery Royalty statute was repealed by the Legislature following the discovery of the reserves at Prudhoe Bay. Under a discovery royalty a lessee would be entitled to withhold a discovery royalty award, say 60% for example, from the oil and gas royalty payable to the state for that lease for a specified period of time, such as 10 years.)

EXPLORATION INCENTIVE CREDITS: Currently AS 38.05.180(i) allows the Commissioner of the Department of Natural Resources to utilize exploration incentive credits. Expanded use of exploration credit incentives to include additional qualifying leases could be extremely effective in stimulating new drilling activity. This could be accomplished under existing state law.

(Two points:

1. On April 1, 1987 Alberta instituted an Exploratory Drilling Assistance Program. This program allows 50% of the cost of an exploratory well to receive credits. These credits can be used to reduce royalty payments, or they can be transferred to another operator.
2. As a very encouraging first step, the State of Alaska's Division of Oil and Gas has announced that it intends to make credits available for those leases which will be offered in Kuparuk Uplands Sale 54, which is scheduled for this January. According to the Division, this will be the first time that exploration credits have been offered without linking the credits to net profit share lease terms.

ENHANCED OIL RECOVERY: Enhanced recovery projects are more capital and labor intensive than primary operations, and the multiplier effect on overall economic activity is much greater. Enhanced recovery projects could be exempted from severance taxes for limited time periods. In addition, the current gas plant investment tax credit could be expanded to a broader based investment tax credit system that could enhance the attractiveness of large projects such as enhanced oil recovery.

(Some additional points:

1. Particular to Alaskan conditions, enhanced recovery incentives should be targeted at development of reserves which otherwise wouldn't be developed, either secondary production from an existing field or initial production from a field which is uneconomic under current conditions.
2. The average recovery efficiency for oil production in the United States is 32.1%, which means that over two thirds of the oil in place will remain in the ground.
3. The federal government's Enhanced Recovery Act of 1979 provided an economic incentive to undertake enhanced recovery programs. During the four plus years this program was effective, a total of 425 enhanced recovery projects were initiated in the United States.
4. Earlier this year Oklahoma enacted legislation which exempts all EOR production from severance taxes until either the payback is completed or three years have passed.
5. Incentives such as these could be designed to improve the economics of the largest undeveloped oil accumulations in Alaska, West Sak and Ugnu Sands.

NEW TAX COURT: Currently there are roughly \$1.5 billion in outstanding disputed tax assessments according to the

Department of Revenue. A report released earlier this year by Common Sense exposed many of the inefficiencies in the current system which have been in large part a cause of this problem.

The current system for appealing disputed tax assessments is perceived by many as being unfair to taxpayers within the state, which has created a negative impact on Alaska's business climate.

The tax court legislation which has been drafted establishes a new division within the superior court system, and allows the taxpayer the option of appealing directly to that court rather than going through what is perceived as an unnecessarily long and unfair process within the Department of Revenue.

The tax court legislation makes the appeal process more uniform with the federal appeal process, and should significantly reduce the inequities in the way tax disputes are currently resolved.

THE OTHER TWO HANDOUTS ARE:

1. Oil Price Watch Indicators.
2. RDC Economic Development Legislation

ATTACHMENT I

LOUISIANA SEVERANCE TAX EXEMPTION PROGRAM (STEP) AND LOUISIANA ECONOMIC ACCELERATION PROGRAM (LEAP)

STEP Well - Any oil well that is spudded and completed during the time period from July 15, 1986 through July 15, 1988; and is certified by the Louisiana Office of Conservation, will be exempt from state severance tax on the first 50 barrels of oil produced each day. Each qualified STEP Well is limited to a maximum exemption of 10,000 barrels per annual period based on the date of first production. This exemption will last through July 15, 1990, but does not apply during any month in which the value of the oil produced exceeds \$21.00 per barrel. No severance tax exemption will apply to production obtained as a result of a well being deepened, side tracted, or recompleted after July 15, 1988. It is likely, however, that attempts to restore production from an oil well drilled within the STEP period by reworking operations will qualify for continued STEP treatment.

In order to certify a well as a STEP Well, a producer must provide the following to the Louisiana Office of Conservation:

1. Evidence supporting the date the well was spudded (must be on or after July 15, 1986);
2. Evidence supporting the date drilling was completed (must be on or before July 15, 1988):
3. Production information establishing the wells capacity to produce;
4. Documentation that the well is classified as an oil well;
5. Evidence supporting the price being received for the oil produced; and
6. Certification that "to the maximum extent possible," at least 10% of the service contracts related to the well drilling have been made available to minority-owned businesses and at least 5% of the service contracts have been made available to women-owned businesses.

In order for the producer to claim the exemption on a certified well, Form O-4 must be filed with the Department of Revenue and Taxation each month indicating the wells activity during the previous month. This form must be filed by the last day of the month following production and must be accompanied by a copy of the Producers report and the Office of Conservations certification of qualified wells. Even though the exemption will not apply during any month in which the value of the oil exceeds \$21.00 a barrel, a report must still be filed to report the total production from the well and to reflect that none of the production for that month is eligible. If for any month this procedure is not followed, the exemption for that month will be lost.

LEAP Well - Any oil or natural gas discovery well that is drilled, completed, and produced as a "wildcat well" during the time period from July 1, 1986 through January 1, 1990; and is certified by the Louisiana Office of Conservation, will be exempt from state severance tax until January 1, 1990, or until the posted price of West Texas Intermediate Crude equals or exceeds

ATTACHMENT I

LOUISIANA SEVERANCE TAX EXEMPTION PROGRAM (STEP) AND LOUISIANA ECONOMIC ACCELERATION PROGRAM (LEAP)

\$29.50 per barrel, whichever occurs first. Also exempt would be a subsequent "developmental well" in the same field during the same time period referenced above.

A wildcat well is drilled in search of oil or natural gas accumulations located in a non-productive area, away from a known productive geological structure. Upon successful completion, the wildcat well is then recognized as a discovery well. A "developmental well" must be drilled and completed to a pool previously discovered by a wildcat well.

The exemption does not include a well drilled in a contiguous fault segment of a sand that was either producing or capable of producing prior to July 1, 1986; or to a well subsequently recompleted in a sand previously penetrated from a well that was drilled, completed, and/or produced prior to July 1, 1986.

The certification process for a LEAP Well includes a public hearing where an application is filed by the producer. The application must include:

1. Identification of the potential production zone, its depth, location, geology, and engineering data. Such data must show that the production reservoir is geologically separated (structurally, and/or stratigraphically) from the nearest reservoir that has produced, or is known to have been capable of producing hydrocarbons.
2. Geological and engineering evidence - including electric logs, structure maps, isopachs, bottom hole pressure and production history - supporting classification as a geologically separated reservoir.
3. Certification that, to the maximum extent possible, Louisiana residents were employed during the exploration and production activities undertaken in connection with the well.
4. Certification that, to the maximum extent possible, at least 10% of the operator's service contracts related to the well were made available to minority owned businesses.

ATTACHMENT II

MISSISSIPPI SEVERANCE TAX INCENTIVES

Oil: Any well for which drilling is commenced after March 15, 1987, and before July 1, 1988, and for which qualification has been obtained from the Mississippi State Tax Commission, shall be exempt from the 6% severance tax to the following extent: The exemption shall apply to the first 50 barrels of oil removed from the ground each day for wells drilled to a depth of 12,000 feet or less and shall apply to the first 100 barrels of oil removed from the ground each day for wells drilled to a depth greater than 12,000 feet below the surface. This exemption will last until June 30, 1990, but does not apply during any month that the average value of oil, as determined by the State Tax Commission, exceeds \$25.00 per barrel.

Enhanced Recovery Production: Oil production from an enhanced recovery project where carbon dioxide (CO₂) is used will be taxed at a reduced rate of 3% provided that such CO₂ is transported by pipeline to the oil well site. Gas, including CO₂, used in an enhanced oil recovery method is exempt from severance tax.

Natural Gas and Condensate: Any well for which drilling is commenced after March 15, 1987, and before July 1, 1988, and for which qualification has been obtained from the Mississippi State Tax Commission, shall be exempt from the 6% severance tax for a period of two years beginning on the date of first sale of production from such well.

ATTACHMENT III

MONTANA TAX INCENTIVES

Severance Tax Exemptions

Oil:

New Production: New production is exempt for 2 years following notification made to the Department of Revenue after March 31, 1987 and before July 1, 1991. New production is defined as coming from any well that has not produced during the 5 years immediately preceding the first month of qualified new production; and on which notification was made after March 31, 1987. The exemption terminates when it is certified that the price of WTI crude oil has reached \$25 per barrel.

Stripper: The first 5 barrels of average daily production from a stripper are exempt from severance tax. Production after the first 5 barrels is taxed at a reduced rate of 3% for production from April 1, 1987 through March 31, 1989. A stripper is defined as any well that produces less than 10 barrels per day determined by dividing the amount of production from a lease or unitized area for the year prior to the current calendar year by the number of producing wells and by dividing the resulting quotient by 365. The exemption and the reduced rate will terminate when it is certified that the price of WTI has reached \$30 per barrel.

The tax on other petroleum and mineral or crude oil production continues to be taxed at 5%, except production from a tertiary recovery project which is taxed at 2.5%.

Gas:

Low Production: The first 30,000 cubic feet of average daily production of natural gas from a well that has produced 60,000 cubic feet or less of natural gas per day for the calendar year prior to the current tax year is exempt from tax, and the remainder of natural gas produced from such well is taxed at 1.59%. The prior year production calculation is determined by dividing the prior calendar year production by the number of producing wells and by dividing the resulting quotient by 365.

All other natural gas is taxed at 2.65% of total gross value.

Net Proceeds Exemptions

New Production: New production of natural gas, petroleum, or other crude or mineral oil is exempt from the oil and gas net proceeds tax for the first 12 months of production. New production is defined as the production of natural gas, petroleum, or other crude or mineral oil from any well:

ATTACHMENT III

MONTANA TAX INCENTIVES

New Production: (Cont'd.)

- that has not produced during the 5 years immediately preceding the first month of qualified new production; and
- on which proper notification has been given.
- effective after 1986 per s.b. 66.

Qualified Gas: Natural gas produced from a well 5,000 feet deep or deeper, for which drilling was completed after December 31, 1976 but before April 1, 1987 is exempt from 1/2 of net proceeds tax for 3 years if the gas produced from the well is:

- placed into a natural gas distribution system for delivery to consumers after diligent completion of the well; and
- distributed by a natural gas distribution system serving only natural gas consumers a majority of which are within Montana or at least 10,000 natural gas consumers within Montana.

The 3 year exemption period begins when natural gas from a qualifying well is first placed into a natural gas distribution system.

ATTACHMENT IV

NORTH DAKOTA OIL EXTRACTION TAX INCENTIVES

New Well: Any well that is drilled and completed after April 27, 1987 and is qualified by the North Dakota Industrial Commission, will be exempt from the 6.5% OET for a period of 15 months from the well completion date. This exemption applies both to new wells spudded and to existing wells that are deepened provided that each well is completed to a separate and distinct reservoir. After the 15 month period, new wells will be taxed at a reduced rate of 4%.

Qualified Waterflood: To qualify for the reduced OET rate of 4%, a well must be certified by the North Dakota Industrial Commission and be located on a secondary recovery project which meets the following specifications set forth by the state:

1. It must have been unitized after April 27, 1987;
2. It must employ waterflooding; and
3. It must have achieved an average production level of at least 25% above the normal recovery level for a period of six consecutive months.

Qualified Tertiary: To be eligible for the reduced OET rate of 4%, a well must be certified by the North Dakota Industrial Commission, must be located on a qualifying tertiary recovery project, and must have achieved a production level of at least 15% above the normal recovery level for a period of no less than one month.

Qualified Stripper: In order to qualify for the Stripper Well Exemption, a property must be certified by the North Dakota Industrial Commission and average daily production (based on calendar days) for any consecutive 12-month period after December 31, 1972:

1. Cannot exceed ten barrels per day for wells a depth of 6,000 feet or less; or
2. Cannot exceed fifteen barrels per day for wells a depth of more than 6,000 feet but not more than 10,000 feet; or
3. Cannot exceed twenty barrels per day for wells a depth of more than 10,000 feet.

The Stripper Well incentive will continue indefinitely. The other incentives, however, will continue until the average price of West Texas Intermediate Cushing Oil is thirty-three dollars or more between June 1st and October 31st of any given year. At such time, the 15 month exemption will be eliminated effective November 1st. All qualified new wells, waterflood wells, and tertiary wells will be taxed at 4% for the remaining two months of that year, and effective January 1st of the following year will be taxed at 6.5%.

ATTACHMENT V

OKLAHOMA SEVERANCE TAX INCENTIVES

Enhanced Recovery: Any incremental production which results from an enhanced recovery project shall be exempt from gross production tax from the project beginning date until project payback is achieved for new enhanced recovery projects or until project payback is achieved but not to exceed a period of 36 months for tertiary enhanced recovery projects existing on the effective date of this act. (Effective July 1, 1988.)

ATTACHMENT VI

WYOMING SEVERANCE TAX INCENTIVE

Wildcat Well: Oil and gas produced from a wildcat well drilled and completed after January 1, 1987 and on or before December 31, 1989, is exempt from severance taxes for 4 years commencing the date of first production from the well. A wildcat well is any well so designated by the Wyoming Oil and Gas Conservation Commission. Such wildcat wells must be well outside of known fields or new well which are determined by the commission to have discovered oil or gas in a pool not previously proven productive. (Effective 3-17-87.)

LAWS AFFECTING STATE SEVERANCE TAX
ENACTED 1987

ALASKA:

HB 124

WOULD INCREASE FROM .125¢ TO .4¢ PER BARREL THE "OIL AND GAS" CONSERVATION TAX, AND EXTEND THE TAX TO COVER EACH 50 MCF UNIT OF GAS. SIGNED INTO LAW 6-12-87.

KANSAS:

SB 1

PROVIDES SEVERANCE TAX RELIEF BASED ON THE PRICE OF OIL (AS OIL PRICES GO UP OR DOWN, EXEMPTIONS FROM THE SEVERANCE TAX WOULD RISE OR FALL). SIGNED INTO LAW.

MISSISSIPPI:

SB 2111

PROVIDES FOR AN EXEMPTION FROM OIL AND GAS SEVERANCE TAX ON CERTAIN PRODUCTION FROM NEW WELLS. SIGNED INTO LAW.

MONTANA:

HB 776

EXEMPTS STRIPPER WELLS AND, FOR THE FIRST 2 YEARS OF PRODUCTION, ALL OTHER WELLS PRODUCING PETROLEUM, NATURAL GAS, OR OTHER MINERAL OR CRUDE OIL FROM SEVERANCE TAXES AND LOWERS THE SEVERANCE TAX RATE TO 3 PERCENT FOR CERTAIN STRIPPER WELLS. SIGNED INTO LAW.

SB 066

REDEFINES "NEW PRODUCTION" OF NATURAL GAS, PETROLEUM OR OTHER CRUDE OR MINERAL OIL FOR PURPOSES OF DETERMINING THE NET PROCEEDS TAX. SIGNED INTO LAW.

SB 383

PROVIDES A PERMANENT HOLIDAY FROM THE NET PROCEEDS TAX ON THE FIRST 12 MONTHS OF PRODUCTION FROM NEW OIL OR GAS WELLS. SIGNED INTO LAW.

NEW MEXICO:

CS/HB 360

REDUCES NATURAL GAS SEVERANCE TAX FROM CURRENT 16.3 CENTS AN MCF TO 14 CENTS DURING NEXT FISCAL YEAR (STARTING JULY 1); 12 CENTS FOLLOWING YEAR; 10 CENTS THE YEAR AFTER THAT, AND 3.75% OF VALUE AFTER THE END OF THAT FISCAL YEAR (JUNE 30, 1990). ALSO, 3.75% ON PRODUCTION FROM WELLS WHICH BEGIN PRODUCING GAS AFTER MAY 1, 1987. SIGNED INTO LAW.

AMERADA HESS CORPORATION
INTEROFFICE CORRESPONDENCE

JUNE 15, 1987

TO: P. A. DYSERT
FROM: MARILYN O. ADAMSON
SUBJECT: STATE SEVERANCE TAXES - 1987

AT THE REQUEST OF M. B. BIANCHI, I AM FORWARDING THE ATTACHED INFORMATION ON LAWS AFFECTING SEVERANCE TAXES WHICH WERE PASSED BY STATE LEGISLATURES DURING THE 1987 LEGISLATIVE SESSION. WE DO NOT RECEIVE INFORMATION ON ALL STATES, AND HAVE NOT RECEIVED OFFICIAL FINAL REPORTS FROM SEVERAL; HOWEVER, THIS SHOULD BE REASONABLY COMPLETE FOR ALL LEGISLATURES EXCEPT LOUISIANA, WHICH IS NOT YET ADJOURNED. PLEASE ADVISE IF YOU WISH FURTHER DEAL OF ANY OF THESE ENACTMENTS, AS THE LEGAL DEPARTMENT HAS FULL COPIES OF MOST OF THESE BILLS IN ITS FILES.



MARILYN O. ADAMSON

MOA:SGB

ATTACHMENT

CC: M. B. BIANCHI
D. F. MCCARTHY
D. G. STEVENSON
W. R. TENNANT
A. A. VANMIEGHEM

**LAWS AFFECTING STATE SEVERANCE TAX
ENACTED 1987**

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NORTH DAKOTA:

SB 2078

PROVIDES A TWO-YEAR EXEMPTION FROM THE 6.5% EXTRACTION TAX FOR ANY WELL STARTED AFTER MARCH 31, 1987 AND COMPLETED PRIOR TO JULY 1, 1989. SIGNED INTO LAW. } M. = 1/21

SB 2079

PROVIDES FOR A STRIPPER WELL DEFINITION BASED ON YIELD AND WELL DEPTH; PROVIDES FOR A 15-MONTH MORATORIUM FROM THE 6.5% EXTRACTION TAX ON ALL NEW WELLS; PROVIDES A 2.5% REDUCTION IN THE 6.5% EXTRACTION TAX FOR ALL NEW OIL AFTER THE EXPIRATION OF THE MORATORIUM PERIOD, AS WELL AS FOR NEW QUALIFYING SECONDARY AND TERTIARY RECOVERY PROJECTS; AND TIE ALL OF THE EXTRACTION TAX REDUCTIONS EXCEPT THE STRIPPER WELL REDEFINITION TO A TRIGGER PRICE OF \$33 WEST TEXAS INTERMEDIATE (WTI) CRUDE OIL. WHEN WTI CRUDE OIL IS PRICED AT \$33 OR MORE FOR THE BASE PERIOD, THE FULL 6.5% EXTRACTION TAX WILL AGAIN APPLY. SIGNED INTO LAW.

OKLAHOMA:

HB 1139

EXEMPTS FROM THE GROSS PRODUCTION TAX THE OIL PRODUCTION FROM ENHANCED RECOVERY PROJECTS UNTIL PROJECT PAYBACK IS ACHIEVED OR FOR 36 MONTHS FOR TERTIARY PROJECTS. SIGNED INTO LAW.

WYOMING:

HB 55

PROVIDES FOR A FOUR-YEAR, 4% SEVERANCE TAX EXEMPTION FOR ANY OIL OR GAS WELL DRILLED IN 1987 AND 1988. SIGNED INTO LAW.

HB 275

ALLOWS SEVERANCE TAXES ON CARBON DIOXIDE TO BE A DIRECT CREDIT AGAINST SEVERANCE TAXES ON OIL PRODUCED BY INJECTION OF THE GAS. SIGNED INTO LAW.

HB 347

EXEMPTS FROM TAXATION SPECIFIED FLARED OR VENTED GAS, REINJECTED GAS AND GAS CONSUMED ON LEASE WITHOUT SALE. SIGNED INTO LAW.

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State of Alaska
MEMORANDUM

Office of the Governor

Division of Policy

P.O. Box AM, Juneau, AK, 99811
Tel. 465-3568 / Mail Stop 0161

TO: Rep. Drew Pearce

DATE: 19 March 1987

FROM: Gregg Erickson
Senior Economist

SUBJECT: Shares of Alaska Oil Revenue.

I have enclosed OMB's most recent (April 11, 1986) analysis of the shares of net revenue from oil production and transportation in Alaska during the FY 82-85 period. Oil industry Alaska profits over this 4-year period (net of capital charges, costs, royalties and taxes) totaled \$22,103 million.

The profits earned in Alaska can be compared with the \$6 billion in oil industry invested in Alaska over the same period. Testimony of Harold Heinze, House Finance transcript, April 12, 1985, p. 130.

I have also provided copies of our correspondence with Exxon regarding the "shares" analysis.

cc: Rep. Cotten
Mary Halloran

file
oil Revenue

**STATE, FEDERAL AND INDUSTRY SHARES OF ALASKA OIL
RESOURCE INCOME: FISCAL 1982-1985**
(millions of dollars except as noted)

	[1]	[2]	[3]	[4]	[5]	[6]	[7]	[8]
Fiscal	Total	State	Sever.	Total	Total	Total	Total	Windfall
year	Revenue	Royalty	Conser.	Prop.	Oper.	Deprec.	Acquis.	Profits
			tax	tax	Costs		Costs	Tax
1982	\$16,456	\$1,553	\$1,581	\$276	\$940	\$602	\$1	\$2,018
1983	\$15,470	\$1,448	\$1,494	\$307	\$1,101	\$780	\$1	\$1,018
1984	\$14,955	\$1,409	\$1,393	\$358	\$1,259	\$998	\$1	\$412
1985	\$15,136	\$1,390	\$1,389	\$397	\$1,449	\$1,093	\$1	\$70

	[9]	[10]	[11]	[12]	[13]	[14]	[15]	[16]
Fiscal	Uncap.	Explore.	Admin.	Other	Total	State	Corp.	Federal
Year	Interest	Costs	Costs	Deducs.	Deducs.	Taxable	Petrol	Taxable
	Expense					Net	Income	Income
						Income	Tax	
1982	\$721	\$191	\$236	\$149	\$8,268	\$8,188	\$669	\$7,519
1983	\$676	\$204	\$252	\$142	\$7,423	\$8,047	\$236	\$7,811
1984	\$614	\$219	\$265	\$136	\$7,064	\$7,891	\$265	\$7,626
1985	\$566	\$234	\$278	\$130	\$6,997	\$8,139	\$169	\$7,970

	[17]	[18]	[19]	[20]	[21]	[22]	[23]
Fiscal	Federal	Oil	Total	Total	---Share of Oil Income---		
Year	Corp.	Industry	Federal	State	State	Federal	Industry
	Income	Alaska	Tax	Tax &			
	Tax	Profits	Royalty	Royalty			
1982	\$2,098	\$5,421	\$4,116	\$4,079	30%	30%	40%
1983	\$2,140	\$5,671	\$3,158	\$3,485	28%	26%	46%
1984	\$2,242	\$5,384	\$2,654	\$3,425	30%	23%	47%
1985	\$2,343	\$5,627	\$2,413	\$3,345	29%	21%	49%

SOURCES AND FORMULAS --

Column [1]: Vincent Wright, chief of research, to Mary Nordale, Commissioner of Revenue, Memorandum of October 31, 1985, Table 3.

Columns [2] & [3]: January 1986 DOR Revenue Sources, p. 39.

Columns [4] to [12]: Vincent Wright, loc. cit.

Column [13]: sum of columns [2] through [12]

Column [14]: column [1] - column [13]

Column [15]: Revenue Sources, p. 39.

Column [16]: column [14] - column [15].

Column [17]: column [16] * (production-weighted average tax rate - 1982 = .279; 1983 = .274; 1984 = .294; 1985 = .294). Company effective rates for '82-84 from R. McIntire and R. Folen, "Corporate Income Taxes in the Reagan Years," Oct. 1984, pp. 32-36; '85 estimated by OMB.

Column [18]: column [16] - column [17].

Column [19]: column [8] + column [17].

Column [20]: sum of columns [2], [3], [4], and [15].

Column [21]: (column [18])/(sum of columns [18], [19], and [20]).

Column [22]: (column [19])/(sum of columns [18], [19], and [20]).

Column [23]: (column [20])/(sum of columns [18], [19], and [20]).

Joseph M. Wilson, Esq.
Louis R. Veerman, Esq.
Guess & Rudd
510 L Street, Suite 700
Anchorage, Alaska 99501
(907) 276-5121

Attorneys for Plaintiff

IN THE SUPERIOR COURT FOR THE STATE OF ALASKA
THIRD JUDICIAL DISTRICT AT ANCHORAGE

STANDARD ALASKA PRODUCTION)
COMPANY,)
)
Plaintiff,)
)
v.)
)
STATE OF ALASKA, DEPARTMENT)
OF REVENUE,)
)
Defendant.)
_____)

Case No. 3A11-87-_____ Civ.

COMPLAINT FOR DECLARATORY JUDGMENT

Plaintiff, Standard Alaska Production Company (the "Taxpayer"), by and through its counsel, Guess & Rudd, brings this action for declaratory relief against the State of Alaska, Department of Revenue (the "Department"), and alleges as follows:

INTRODUCTION

1. This is an action for a judgment declaring that the Department lacks authority to assess an amount of tax greater than the amount assessed within the applicable statute limiting the Department's authority to make assessments. Accordingly, certain tax assessments the Department has made against the Taxpayer are invalid because they (i) are barred by the statute limiting the Department's assessment powers, (ii) are inconsistent with the Department's regulations, (iii) lack statutory authority, and (iv) amount to a denial of due process of law.

JURISDICTION

2. This action presents an actual controversy over which this Court has jurisdiction pursuant to AS 22.10.020(b).

3. This action also presents a challenge by an interested party to the validity of a regulation of an administrative agency over which this Court has jurisdiction pursuant to AS 44.62.300.

4. The issues presented are purely legal in nature and do not involve the application of agency expertise.

PARTIES

5. The Taxpayer is a corporation organized and existing under the laws of the State of Delaware and is qualified to do business in the State of Alaska, having paid its corporate taxes and filed its biennial report last due. The Taxpayer's business within the State consists primarily of oil and gas exploration, development and production operations.

6. The Department is a department within the executive branch of the State of Alaska, established pursuant to Article III, Section 22 of the Constitution of the State of Alaska.

GENERAL ALLEGATIONS

7. The Taxpayer has been and continues to be required to file returns and pay various taxes imposed by the State of Alaska pursuant to Title 43, Alaska Statutes.

8. The Department regularly audits the tax returns of taxpayers engaged in the oil and gas business in Alaska.

9. The Department issues assessments for additional tax when it appears upon audit that a return filed under Title 43 has understated the amount of tax due.

10. AS 43.05.260(a) provides for a three-year limitation period on assessments.

11. The Department was required to make an initial determination of income under AS 43.21 on or before August 15th of the year following the taxable year (the "Original Assessment"), and was authorized to amend the Original Assessment or any subsequent amended assessments up to three years from the date of the Original Assessment. AS 43.21.050, 15 AAC 21.700(e).

12. Under 15 AAC 21.810(1) the Department may amend an assessment "no later than" three years from the date the tax return was due or filed, whichever is later.

13. The Taxpayer timely filed its oil and gas corporate income tax return for the 1978 taxable year (the "1978 Return") on June 15, 1979.

14. The time period for amending assessments related to the Taxpayer's 1978 Return expired under AS 43.05.260(a) either on June 15, 1982, as provided in 15 AAC 21.810(1), or on August 15, 1982, as provided in 15 AAC 21.700(e).

15. The Department audited the 1978 Return and, on August 15, 1979, issued an Original Assessment. On December

31, 1981, the Department timely issued an "Amended Notice of Assessment" (the "First Amended Assessment") for the Taxpayer's 1978 taxable year.

16. On February 24 and 28, 1984, more than four and one-half years after the Taxpayer filed its 1978 Return and received the Original Assessment, the Taxpayer received from the Department undated documents captioned "Amendments to Audit Narrative" and accompanying schedules (the "Second Amended Assessment"), which purported to increase substantially the amount set forth in the First Amended Assessment. The Second Amended Assessment was untimely because it was not issued by either June 15 or August 15, 1982.

17. In February 1985, more than five and one-half years after the Taxpayer filed its 1978 Return and received the Original Assessment, the Taxpayer received a document dated February 4, 1985, captioned "Amended Notice and Demand for Payment" (the "Third Amended Assessment"), which again purported to assess, for the Taxpayer's 1978 taxable year, an amount of tax in excess of the amount set forth in the First Amended Assessment. The Third Amended Assessment was untimely because it was not issued by either June 15 or August 15, 1982.

18. The Taxpayer timely protested the First, Second, and Third Amended Assessments, and ultimately withdrew its protest to the Second Amended Assessment, as the Department has agreed that the Third Amended Assessment superceded and replaced the Second Amended Assessment.

19. In issuing the Second and Third Amended Assessments, the Department has interpreted AS 43.05.260 to permit the assessment of additional taxes after the three-year limitation period, but only if the Taxpayer exercises its rights to obtain administrative and judicial review of an assessment by filing a protest.

20. The Department's interpretation of AS 43.05.260 constitutes a "regulation" within the meaning of AS 44.62.300.

21. The Department's issuance of the Second and Third Amended Assessments has created uncertainty as to the Taxpayer's legal rights and duties under AS 43.05.260 for its 1978 taxable year. This uncertainty would be resolved by issuance of the declaration sought in this Complaint.

22. The Department's issuance of the Second and Third Amended Assessments has subjected the Taxpayer to a threat of injury, in that the Department is seeking to hold the Taxpayer

liable for additional income taxes with respect to its 1978 taxable year, and may seek to hold the Taxpayer liable for still more additional taxes for that year, without any effective time limit or closure of that year, unless this Court declares the Department's interpretation of AS 43.05.260 to be invalid and the Second and Third Amended Assessments void.

23. Even if the Taxpayer ultimately prevails on the substantive tax issues raised in the Second and Third Amended Assessments, the Taxpayer will have been damaged by virtue of having been forced: (i) to divert legal, accounting and operating personnel from their normal duties to prepare and review the exhaustive factual and legal analyses necessary to adequately evaluate and prepare the Taxpayer's defense with respect to the substantive tax issues raised, and (ii) to incur substantial outside counsel fees for representation during administrative appeal proceedings.

24. In view of the Department's interpretation of AS 43.05.260, there is no way for the Taxpayer to determine whether amounts timely assessed for any taxable year subsequent to 1978 will later be increased by assessments issued after the three-year limitation period of AS 43.05.260(a) has expired.

25. The Department's interpretation of AS 43.05.260 has also created uncertainty as to the Taxpayer's legal rights and duties under AS 43.05.260 with respect to years subsequent to 1978, which would be eliminated by issuance of the declaration sought in this Complaint.

26. The Department's interpretation of AS 43.05.260 subjects the Taxpayer to a threat of injury in that the Taxpayer could be held liable for additional Alaska taxes for any taxable year.

27. The Department controls the timing of the final administrative decision, and thus the duration of the period during which the Department claims jurisdiction to reaudit taxpayers' returns and raise the amount of tax assessed. For example, the Department has never issued even an informal conference decision in the Taxpayer's 1978 oil and gas corporate income tax case, even though informal conferences were held on the matter in 1983 and 1984.

FIRST CLAIM FOR RELIEF

28. The Taxpayer incorporates by reference paragraphs 1-27 of this Complaint.

29. The Third Amended Assessment is invalid because it purports to amend the First Amended Assessment after expiration of either of the periods provided under 15 AAC 21.700(e) and 15 AAC 21.810(1).

SECOND CLAIM FOR RELIEF

30. The Taxpayer incorporates by reference paragraphs 1-27 of this Complaint.

31. The Third Amended Assessment is invalid because barred by the three-year limitation period of AS 43.05.260(a).

THIRD CLAIM FOR RELIEF

32. The Taxpayer incorporates by reference paragraphs 1-27 of this Complaint.

33. The Third Amended Assessment is invalid because it lacks statutory authority.

FOURTH CLAIM FOR RELIEF

34. The Taxpayer incorporates by reference paragraphs 1-27 of this Complaint.

35. The Department's interpretation of AS 43.05.260 constitutes a "regulation," and is invalid under AS 44.62.030 because it is inconsistent with AS 43.05.260.

FIFTH CLAIM FOR RELIEF

36. The Taxpayer incorporates by reference paragraphs 1-27 of this Complaint.

37. The Department's attempts to assess amounts greater than the amount assessed within the three-year limitation period of AS 43.05.260(a) whenever taxpayers exercise their right to obtain administrative and judicial review of an assessment amount to a denial of the Taxpayer's rights to due process of law guaranteed by Article XIV, Amendments to the Constitution of the United States, and Article I, §1 of the Constitution of the State of Alaska.

WHEREFORE, the Taxpayer requests that this Court:

1. declare either (i) that 15 AAC 21.700(e) prohibits the assessment of any amount in excess of the amount assessed within three years of the date of the Original Assessment, or (ii) that 15 AAC 21.810(1) prohibits the assessment of any amount in excess of the amount assessed within three years from the date the return was due or filed, whichever is later; and

2. declare that AS 43.05.260 prohibits the assessment of any amount in excess of the amount assessed within the three-year limitation period of AS 43.05.260(a), and

3. declare that there is no statutory authority for assessment of any amount in excess of the amount assessed within three years from the date the return was due or filed, whichever is later, and

4. declare that the Department's interpretation of AS 43.05.260, to the effect that assessment of amounts in excess of the amount assessed within the three-year limitation period of AS 43.05.260(a) are permitted, is inconsistent with AS 43.05.260 and, therefore, is invalid, and

5. declare that the Department's interpretation of AS 43.05.260, as applied to the Taxpayer, is void as violative of the Taxpayer's due process rights under Article XIV, Amendments to the Constitution of the United States, and Article I, §1 of the Constitution of the State of Alaska, and

6. award the Taxpayer costs and attorneys' fees necessarily incurred in bringing this action.

DATED this 23rd day of January, 1987.

GUESS & RUDD
Attorneys for Plaintiff

By: _____
Joseph M. Wilson
Louis R. Veerman

7855K

STATE OF ALASKA

DEPARTMENT OF REVENUE

OFFICE OF THE COMMISSIONER

STEVE COWPER, GOVERNOR

P.O. BOX 5
JUNEAU, ALASKA 99811-0400
PHONE: (907) 465-2300

April 27, 1987

The Honorable Ben Grussendorf
Speaker of the House
Alaska State Legislature
P.O. Box V
Juneau, AK 99811

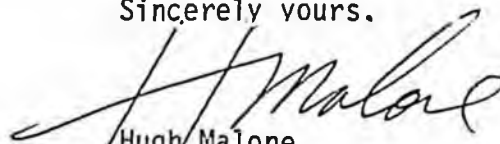
Re: Alaska's Economic Limit Factor Legislation CS HB 164 (Finance) am In
the context of actions in other states

Dear Mr. Speaker:

The following information has been provided to the Governor's office on actions in other states on their oil and gas tax issues. I am providing this to you for your information.

Alaska's situation of being dependent on one primary source of revenue is unique. I believe it is important to understand how oil and gas taxation is being dealt with in other states in the appropriate context. If you have questions on the attached information please call me or Mr. John Hansen in the Department of Revenue Audit Division.

Sincerely yours,


Hugh Malone
Commissioner of Revenue

HM:mkw
87-86

cc: The Honorable Steve Cowper
Members of the Senate
Members of the House of Representatives

Attachments: Hugh's letter of April 27 to Governor Cowper covering Senate President Jan Faiks' memo of April 10 and Jan Faiks' memo of April 10 to all Legislators on oil and gas tax reductions in other states.



Alaska State Legislature

SENATE

Office of the President

P.O. Box V
State Capitol
Juneau, Alaska 99811

April 10, 1987

MEMORANDUM

TO: All Legislators

FROM: Senator Jan Faiks, *Jan Faiks*
President of the Senate

SUBJECT: Oil and Gas Tax Reductions in other States

Legislatures in other resource states are trying to mitigate the tax burden on the oil and gas industry. This is done to encourage continued exploration and production during the current market situation facing the industry, and thus offset negative impacts on the states' economies and employment levels. Here is summary of what some of the states are doing:

Kansas - HB 2405 would exempt from property or ad valorem taxes all temporary abandoned oil or gas wells and the equipment or material used on the wells. SB 1, which would raise the severance tax exemption on low-production wells, has passed the Senate.

Louisiana - Severance Tax Exemption Plan, wells drilled between July, 1986 and July, 1987 pay no severance taxes through 1990. Economic Acceleration Plan, no tax on development through 1989 for discoveries after July, 1936. Both of these measures became law in 1986.

Mississippi - HB 620 which would provide an exemption from oil and gas severance taxes on certain production from new wells has passed the House.

Montana - SB 383 would exempt the first 24 months of production from new wells from the net proceeds tax.

North Dakota - HB 1667, which would have provided for a two-year moratorium from the extraction tax for all new well and a four-year moratorium from the extraction tax for wildcat wells, failed. SB 2078 which provides a two-year exemption from the 6.5% extraction tax for any well started after March 31, 1987 and completed by July 1, 1989 passed the Senate. SB 2079 which provides a gradual reduction over a five-year period in the 6.5% oil extraction tax to 3.5% and provides for a one-year moratorium from the 6.5% tax on all new wells drilled also passed the Senate.

Oklahoma - HB 1139 would exempt all EOR production from severance taxes until either the payback is completed or 3 years have passed, has passed the House.

Texas - HB 949 makes provisions relating to exempting oil and gas produced by stripper wells from production taxes.

Wyoming - HB 275 which allows severance taxes on carbon dioxide to be a direct credit against severance taxes on oil produced by injection of the gas, has passed both houses of the Legislature.

STATE OF ALASKA
DEPARTMENT OF REVENUE

M E M O R A N D U M

TO: The Honorable Steve Cowper
Governor

FROM: Hugh Malone *Hugh*
Commissioner of Revenue

DATE: April 27, 1987

SUBJECT: Senate President Jan Faiks Memorandum of April 10, 1987
on Oil and Gas Tax Reductions in Other States

Our Department has completed a cursory review and analysis of the various legislation that Senator Faiks points out other states have introduced to mitigate the effects of the current market condition on the oil and gas industry. In response, my staff has contacted the Department's of Revenue in each of these states to verify what is really happening.

We have found this memorandum to be incorrect in the factual analysis of each states legislation. The twelve pieces of legislation referenced in Senator Faiks memorandum generally apply to stripper wells with very low production. To qualify for tax exempt status, each well must be put into production within specific dates. Some states exempt the first 10 to 50 barrels of oil produced per day. More importantly states such as Texas only exempt oil production from tax when the price per barrel falls below a set amount. The fiscal impact of the various legislation is minimal to the states that have passed these bills.

Following is a review, state by state, of Senator Faiks' comments and the comments of other states tax authorities:

1. Kansas - HB 2405

Senator Faiks' memorandum states:

"... would exempt from property or ad valorem taxes all temporary abandoned oil or gas wells and the equipment or material used on wells."

Actual Status:

Applies to only temporary abandoned property. This property has already been given a zero evaluation if they are not producing, therefore would have no fiscal impact to the state. The bill has little chance of passing this session.

SB 1

Memorandum states:

". . . would raise the severance tax exemption on low-production wells, has passed the Senate."

Actual Status:

Applies only to stripper wells of 2,000 ft. depth producing five barrels a day or less, fiscal impact is minimal. Bill has little chance of passing. It has been stalled in House Committee. The combined loss of revenue if both bills did pass to the state would be \$5.5 million. The total revenue raised from oil and gas taxes in Kansas is approximately \$100 million which represents 6%-7% of their entire budget.

2. Louisiana -

Severance Tax Exemption Plan

Memorandum states:

". . . wells drilled between July, 1986 and July, 1987 pay no severance taxes through 1990."

Actual Status:

HB 673 applies only to new oil wells drilled between July 15, 1986 and July 15, 1987. Exempts severance tax on the first 50 barrels of oil per day and only until the well has produced 10,000 barrels. Applies only if price of oil is \$21.00 a barrel or lower. Is repealed in 1990. Fiscal impact will be minimal.

Economic Acceleration Plan

Memorandum states:

". . . no tax on development through 1989 for discoveries after July, 1986."

Actual Status:

This exemption covers only "wildcat wells." These are wells on certified new fields provided the price of oil stays below \$29.50 per barrel and the well is drilled between July 1, 1986 and July 1, 1990. Fiscal impact is minimal.

3. Mississippi - HB 620

Memorandum states:

". . . would provide an exemption from oil and gas severance taxes on certain production from new wells has passed the house."

Actual Status:

HB 620 did not pass.

Another bill, SB 2111, did pass. This bill provides an exemption for the first 50 barrels per day for wells with a depth of 12,000ft. or less and exempts 100 barrels for wells with a depth of 12,000ft. or greater, provided wells are drilled between March 15, 1986 and July 1, 1987 and the average price of oil is \$25.00 a barrel or less. Exemption expires June 30, 1990.

4. Montana - SB 383

Memorandum states:

". . . would exempt the first 24 months of production from new wells from the net proceeds tax."

Actual Status:

It has passed both houses and the Governor is expected to sign. However, the bill covers only the first 12 months of production and pertains solely to the mill rate calculation for county property tax purposes. Has no impact to state revenues.

5. North Dakota

HB 1667

"Failed"

SB 2078

Memorandum states:

". . . provides a two-year exemption from the 6.5% extraction tax for any well started after March 31, 1987 and completed by July 1, 1989 passed the Senate."

Actual Status:

This bill deleted an exemption for royalty owners interest from the oil extraction tax. It passed. This is a revenue positive tax measure expected to raise approximately \$4.6 million in the next two fiscal years.

SB 2079

Memorandum states:

". . . provides a gradual reduction over a five-year period in the 6.5% oil extraction tax to 3.5% and provides for a one-year moratorium from the 6.5% tax on all new wells drilled also passed the Senate."

Actual Status:

Provided for various rule and regulation changes. Provided for a 15 month exemption from oil extraction taxes and reduced the rates from 6.5% to 4% thereafter for new wells drilled after the bill passed. Also reduces rates from 6.5% to 4% on certain wells utilizing tertiary recovery systems and certified stripper wells. Only in effect if oil prices are below \$33.00 a barrel. Revenue impact is minimal. Expected to reduce oil revenues by \$4.66 million over the next two fiscal years. Both bills combined are expected to be revenue neutral.

6. Oklahoma - HB 1139

Memorandum states:

". . . would exempt all EOR production from severance taxes until either the payback is completed or 3 years have passed, has passed the House."

Actual Status:

This bill is sitting on the Governor's desk, he is expected to veto. The bill applies only to certain exploratory wells, at certain depths. Fiscal impact would reduce production taxes by less than 7%. Total revenues raised by oil production taxes account for less than 20% of the entire operating budget for the state.

7. Texas - HB 949

Memorandum states:

". . . make provisions relating to exempting oil and gas produced by stripper wells from production taxes."

Actual Status:

Bill is stalled in House and has little chance of passing. The Comptroller of Texas stated, "Texas can't afford to lose the \$18 million that this bill would be giving to the oil companies." The bill itself exempted only stripper wells, that is 10 barrels of oil or 60,000 cubic feet of gas produced in one day. The exemption only applying if the price of oil was \$14.00 a barrel or less

8. Wyoming - HB 275

Memorandum states:

". . . which allows severance taxes on carbon dioxide to be a direct credit against severance taxes on oil produced by injection of gas, has passed both houses of the legislature."

Actual Status:

This bill has now become law. It applies only to tertiary recoveries utilizing carbon dioxide gas and is only applicable as a credit when the severance tax has been already paid on the gas being utilized for the recovery process for oil which will have the tax applied to it. This could be viewed as a "double taxation" issue. The Wyoming Department of Revenue has projected that this legislation will have such a minimal impact they did not prepare fiscal notes for the bill.

Governor Cowper
April 27, 1987
Page 6

Alaska's dependency on oil and gas production is responsible for over 85% of our total revenue. This is in sharp contrast with the next highest state, Texas, which has an oil and gas dependency of about 20% for its state operating budget. The Comptroller of Texas stated in March of 1987 "That this over-reliance on severance taxes has twice proven an unreliable way to pay for state government. That's a lesson Texas cannot afford to learn a third time. Let's fix the problem."

How do other states raise revenue? Income and sales tax. Every state mentioned in Senator Faiks' memorandum has an income or sales tax. States with an income tax have received a windfall from the 1986 Tax Reform Act and many states are looking at ways to reduce some of those taxes accordingly.

In conclusion, we do not agree with Senator Faiks' portrayal of what the other oil and gas producing states are doing for the industry. We have requested from all states contacted copies of the bills. We can provide you with a more complete analysis should you so desire once we have received this additional information.

SC/HM/JNH/tb

10/7/86

HISTORY OF OIL AND GAS TAX LAW

Severance Taxes

In 1955 the Alaska Legislature enacted two bills which imposed a tax on the production of crude oil and natural gas in the state. One of those measures, which imposed a 1% tax on the gross value of production, was the foundation from which the state's existing oil and gas production properties tax evolved. The other statute, that has since been repealed, was a conservation tax of five mills for each barrel of oil and every 50,000 cubic feet of gas produced.

Between 1955 and 1967 no changes were made in the production taxes. Then, in 1967, the legislature convened in a special session to provide statutory relief for the victims of the Fairbanks flood. Faced with extraordinary costs associated with the Fairbanks disaster, the legislature enacted an additional one percent disaster severance tax on the gross value of oil and gas production.

In 1968 the legislature raised the "regular" production tax from one percent to three percent, but did not change the one percent disaster severance tax or the five mill conservation tax.

In 1970, the legislature, by amendment, embodied a progressive or "stairstepped" rate structure for oil based on average daily production per well. The rates were three percent on the first 300 barrels per day, five percent on the next 700, six percent on the next 1,500 and eight percent on the production exceeding 2,500 barrels per day. Gas production was taxed at four percent. Since the one percent disaster severance tax and the five mill conservation tax were simultaneously repealed, there was no increase in the overall nominal gas tax rate.

In 1972 the Joint Pipeline Impact Committee requested legislation be enacted to protect state revenues from unacceptably low wellhead prices at Prudhoe Bay. The committee anticipated that low prices would result from high pipeline tariffs that could stem from either inadequate tariff regulation or construction cost overruns, or both. In response to that request the legislature enacted a unit of production (cents-per-barrel) tax with a credit for royalties paid to the state. If the cents-per-barrel tax, minus the royalty credit, exceeded the tax collected under the existing

percentage-of-value method, then the cents-per-barrel tax would be payable. Litigation concerning the validity of this new tax began on the heels of enactment.

The 1973 Special Session of the Legislature made several changes to the 1972 law. The royalty credit provision was repealed. The effective tax rate that would apply to oil production was increased by increasing the effective floor of the cents-per-barrel tax from \$2.65 to \$3.375. Instead of four "stairsteps" there were three: the first 300 barrels a day from a well were taxed on the higher of five percent of the oil's value or \$0.16875 per barrel, the next 700 at six percent or \$0.2025 per barrel, and all production over 1,000 barrels a day at eight percent or \$0.27 barrel. In addition, the cents-per-barrel amounts increased or decreased by two cents for each degree of API gravity above or below 27 degrees. Thus a complete schedule of three unit-of-production rates (one for each "stairstep") could have been established for various API gravities. The whole schedule of rates was in turn to be increased or decreased monthly based on changes in the Wholesale Price Index for crude oil, published by the U.S. Bureau of Labor Statistics. The tax on gas production remained a simple four percent of value. In addition, an oil and gas regulation and conservation tax at a rate of \$0.00125 per barrel removed or sold was enacted during this legislative session.

In 1976 no changes were made to the production tax rates, but the legislature did replace the "cash price prevailing" language with "prevailing value" and enacted a section titled "Determination of Gross Value". The changes made it clear that value was to be determined by using reasonable costs of transportation to determine the value at the point of production. The legislature found the terms price and value were not necessarily synonymous and that taxable gross value was to be determined by subtracting reasonable transportation costs from the full consideration realized by the producer at the point of sale.

The production tax was amended again in 1977 when the legislature adopted an economic limit factor (ELF) for the purpose of reducing the effective production tax rate as the amount of production from a lease or property declines. The nominal tax rate for oil was set at 12.25 percent and 10 percent for gas. However, the effective rate was determined through the use of the ELF. The cents-per-barrel and cents-per-mcf rates were also subject to the ELF. Nominally they were 6.4 cents per mcf (corresponding to a 64 cent per mcf floor), 60 cents per

barrel for "old oil" (a \$4.90 per barrel floor) and 80 cents for all other oil (a \$6.53 per barrel floor). Before being reduced by the ELF, the cents-per-barrel amounts were adjusted up or down by a half-cent for each degree above or below 27 degrees per API gravity. There was no automatic escalator for the unit-of-production rates; instead, the Department was to recommend changes to the rates that were appropriate in light of transaction prices and market conditions. Also, the removed and sold standard that historically was used as the measure of taxable production was changed to a produced standard. At the same time, and as a result of Alaska's protracted royalty litigation with oil and gas producers in the Cook Inlet area, the definitions of the point of production were either established or better defined.

It is also noteworthy that some of the complexities of this 1977 legislation caused the Department of Revenue to promulgate the first production tax regulations.

The remaining major amendment to the production tax statute occurred in 1981. The nominal rate of tax on oil was changed from 12.25 percent to 15 percent on any oil produced after June 30, 1981 from a lease or property that was in commercial production prior to that date. The nominal rate on oil produced from a lease or property coming into production after that date was to be 12.25 percent during the first five years of production and 15 percent thereafter. Modifications also were made to the economic limit factors for both oil and gas. The major impact of this legislation changed the effective rate of this tax on over 90 percent of the oil produced in Alaska from approximately 11.5 percent to 15 percent.

On the following page is a summary of production events and tax changes by year beginning in 1954.

OIL AND GAS PRODUCTION AND TAX TIMELINE
9/19/86

- 1954 BLM ISSUED 272 OIL AND GAS LEASES
- 1955 ONE PERCENT OIL AND GAS PRODUCTION TAX
- 1955 CONSERVATION TAX OF FIVE MILLS PER BARREL
AND FOR EVERY 50,000 CUBIC FEET OF GAS
- 1957 SWANSON RIVER OIL FIELD DISCOVERED
- 1959 KENAI GAS FIELD DISCOVERED
- 1962 COOK INLET OIL DISCOVERED
- 1967 ONE PERCENT DISASTER SEVERANCE TAX
- 1968 OIL AND GAS PRODUCTION TAX INCREASED FROM ONE TO THREE
PERCENT
- 1968 PRUDHOE BAY OIL DISCOVERED
- 1970 THREE TO EIGHT PERCENT "GRADUATED" PRODUCTION TAX
(BASED ON PRODUCTION LEVELS)
- 1970 CONSERVATION AND DISASTER SEVERANCE TAX REPEALED
- 1970 GAS PRODUCTION TAX INCREASED TO FOUR PERCENT
- 1972 CENTS PER BARREL "FLOOR" ON PRODUCTION TAX
- 1973 20-MILL OIL AND GAS EXPLORATION, PRODUCTION AND PIPELINE
TRANSPORTATION PROPERTY TAX
- 1973 THREE TO EIGHT PERCENT PRODUCTION TAX (BASED ON LOWER
OUT-PUT LEVELS) PLUS TIED AN "ESCALATOR" TO THE CENTS
PER BARREL FLOOR.
- 1973 OIL AND GAS REGULATION AND CONSERVATION TAX
OF ONE-EIGHTH OF A CENT PER BARREL
- 1973 OPEC QUADRUPLED WORLD MARKET PRICE FOR CRUDE
- 1975 20-MILL RESERVES TAX
- 1977 -NOMINAL 10 PERCENT PRODUCTION TAX ON GAS
-NOMINAL 12.25 PERCENT PRODUCTION TAX ON OIL
-ADOPTION OF ECONOMIC LIMIT FACTOR (ELF)
- 1977 20-MILL RESERVES TAX EXPIRES
- June 20,* 1977 PRUDHOE BAY OIL BEGAN FLOWING THROUGH TAPS
- 1978 OIL AND GAS CORPORATE INCOME TAX (SEPARATE ACCOUNTING)

1979 PRUDHOE BAY WELL HEAD PRICES INCREASED FROM \$5.80 PER BARREL IN JANUARY TO \$10.57 IN JUNE AS A RESULT OF THE LOSS OF IMPORTS FROM IRAN

1981 -OIL AND GAS CORPORATE INCOME TAX (REPEAL SEPARATE ACCOUNTING AND ADOPTED MODIFIED APPORTIONMENT)
-15 PERCENT PRODUCTION TAX(ON ANY OIL PRODUCED AFTER JUNE 30, 1981 FROM A LEASE OR PROPERTY THAT WAS IN COMMERCIAL PRODUCTION PRIOR TO THAT DATE. THE NOMINAL RATE ON OIL PRODUCED FROM A LEASE OR PROPERTY COMING INTO PRODUCTION AFTER THAT DATE WAS TO BE 12.25 PERCENT DURING THE FIRST FIVE YEARS OF PRODUCTION AND 15 PERCENT THEREAFTER)

History of AS 43.21,
Oil and Gas Corporate Income Tax

1978 - 1981

In 1978, the Legislature enacted the Oil and Gas Corporate Income Tax, AS 43.21. Basically, 43.21 is a separate accounting method wherein all of the income and expense elements are defined by statute. Income is divided into three types: (1) income from oil and gas production; (2) income from oil and gas pipeline transportation; and (3) income from any other activities.

The determination of taxable income from oil and gas production starts with the calculation of gross income. Gross income from the production of oil and gas is basically the gross value at the point of production. There are several ways of determining that value including using actual prices or value received, posted prices in the same field or prevailing prices of oil and gas in the same field. The deductions from gross income in order to arrive at the net taxable income include:

- royalties paid in kind or in value
- production property taxes paid
- direct costs of operating the lease or property
- depreciation based on the units of production method
- amortization of lease acquisition payments and taxes paid prior to commencement of commercial production
- interest expense not capitalized during construction
- expenses of unsuccessful exploration of oil and gas in the state including acquisition costs, abandonment of properties, dry-hole costs (only subsequent to abandonment of a lease), and geological and geophysical exploration costs related to the abandoned properties
- general overhead and administrative expense
- income from the production of oil and gas which is divided among the regional native corporations under the Alaska Native Claims Settlement Act
- windfall profit tax

Interest and overhead are presumed not to exceed the corporation's total interest and overhead expenses multiplied by a fraction of which the numerator is the corporation's real and tangible personal property used directly in the production of oil and gas from a lease or property in the state and the denominator of which is all such property of the consolidated business. A corporation may rebut this presumption by satisfactorily demonstrating its actual expenses in Alaska are greater.

The net income of oil and gas pipeline transportation, basically, is the net operating income that is reported to the Federal Energy Regulatory Commission (FERC) or that would be reported to that commission in the case of pipelines that are not regulated by FERC. That method is modified by adding back taxes on or measured by net income. There are also limitations on interest and overhead expenses that may be deducted.

Income from activities other than the production of oil and gas from a lease or property in the state or pipeline transportation of oil or gas in the state is apportioned to the state. The determination starts with the total taxable income and then adding, if appropriate, income of member(s) of the worldwide consolidated business not required to file under the U.S. Internal Revenue Code less that portion of the entire income attributable to production and pipeline transportation of oil and gas worldwide. The apportionment formula is modified so that the numerator and denominator of the property, payroll, and sales factors are each calculated without reference to that portion of property, payroll, or sales directly related to the production of oil or gas or the pipeline transportation of oil or gas in the state.

IMPACT OF 1981 SLA, ch. 116 (SB 524)

Chapter 116 of the 1981 Session Laws of Alaska amended the oil and gas corporate income tax and the oil and gas severance tax in the following manner:

1. Prior to the amendments, AS 43.55 provided for a tax on oil production amounting to 12.25 percent of the gross value at the point of production modified by the economic limit factor (ELF) set forth in AS 43.55.013. The ELF factor on Prudhoe Bay production during FY 1982 was approximately .9249 which led to an effective rate of 11.33 percent. The ELF on Cook Inlet production in FY 1982 averaged approximately .2864 which led to an effective rate of 3.51 percent. The tax rate on gas was 10 percent of the gross value at the point of production modified by an ELF factor.

2. The new law increased the nominal tax rate to 15 percent on oil production (except that for fields commencing commercial production after June 30, 1981, the rate would be 12.25 percent for the first five years). The ELF was also modified so that if the actual calculation resulted in an ELF greater than 0.7 a factor

of 1 would be used. See AS 43.55.011(b) and AS 43.55.013(b)(4). Thus the actual tax rate on Prudhoe Bay production became equal to the nominal rate ($15\% \times 1 = 15\%$), the Kuparak rate became 12.25% ($12.25\% \times 1 = 12.25\%$) and Cook Inlet during FY 82 was approximately 4.3% ($15\% \times .2864 = 4.3\%$). The gas severance tax rate was unchanged although the gas ELF factor calculation was modified. See AS 43.55.013(g). The increased severance tax rates were made effective July 1, 1981, the beginning of FY 82.

3. The oil and gas corporate income tax method set forth in AS 43.21, known as separate accounting, was repealed and a new modified apportionment scheme was enacted effective January 1, 1982. These provisions can be found in AS 43.20.072. The new method for attributing oil and gas income to the state combined with the introduction of a graduated rate structure set forth in AS 43.20.011(e) decreased revenues from the overall corporate income tax.

REPRESENTATIVE
SAM COTTEN
DISTRICT 15



P.O. BOX 296, EAGLE RIVER, AK 99577
POUCH V, JUNEAU, AK 99811

ALASKA STATE LEGISLATURE
HOUSE OF REPRESENTATIVES

March 4, 1988

Mr. Leon Hess
Chairman
Amerada Hess Corporation
1185 Avenue of the Americas
New York, NY 10036

Dear Mr. Hess:

I have just seen a copy of your March 2 letter to Senator Coghill about the proposed legislation to provide relief for Seal Island development.

My reaction to your letter was 100% positive. It is a pleasure, after years of working in the Legislature, to read the words of a corporate chairman who also recognizes and wants to protect the interests of the people of Alaska.

I agree with you that there could be enormous benefits from the development of marginal fields in Alaska. Last year, the House of Representatives passed a bill (HB 164) that would have decreased the severance tax on marginal fields around the state. It also would have repealed the scheduled tax break for Prudhoe Bay and Kuparuk producers, and was therefore opposed by the major lessees in these two units. The only industry support that the bill ended up receiving was from Conoco, which might have been able to keep producing at Milne Point. For now the bill appears to have died in the Senate, but I have asked the Department of Revenue to indicate what kind of severance tax benefits the bill might have produced for Seal Island development. I might add that this bill had the Governor's full support.

At any rate, I appreciate your letter and look forward to meeting you someday when you are in Alaska, or I am in New York, if that would be possible. And we will continue looking for ways to enhance marginal field production for the benefit of the industry and Alaska's citizens.

Sincerely,

A handwritten signature in cursive script that reads "Sam Cotten".

Rep. Sam Cotten, Co-Chair
House Resources Committee

Original sponsor: Rules/Governor

1 IN THE HOUSE BY THE FINANCE COMMITTEE
2 CS FOR HOUSE BILL NO. 164 (Finance) am
3 IN THE LEGISLATURE OF THE STATE OF ALASKA
4 FIFTEENTH LEGISLATURE - FIRST SESSION

5 A BILL

6 For an Act entitled: "An Act relating to the oil and gas properties pro-
7 duction tax; and providing for an effective date."

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

9 * Section 1. AS 43.55.013(b) is repealed and reenacted to read:

10 (b) The economic limit factor for oil production of a lease or
11 property shall be computed according to the following formula:

12
$$(1 - [PEL/TP]) \exp ([55,000,000 \times WD] / [PEL \times TP / \text{Days}])$$

13 where: PEL = the monthly production rate at the economic limit;

14 TP = the total production during the month for which the tax
15 is to be paid;

16 WD = the total number of well days in the month for which
17 the tax is to be paid;

18 Days = the number of days in the month for which the tax is to
19 be paid; and

20 where "exp" indicates that the expression following it is an exponent.

21 * Sec. 2. AS 43.55.013(d) is amended to read:

22 (d) The monthly production rate at the economic limit for a
23 lease or property is presumed to be 300 barrels times the number of
24 well days for the lease or property during the month for which the tax
25 is to be paid. The taxpayer or the department may rebut this pre-
26 sumption at a formal hearing under AS 43.05.240 by providing clear and
27 convincing evidence of a different monthly production rate at the
28 economic limit for the lease or property. The hearing shall be held
29 before February 15 of the year or within six months after commencement

Hess loses its effort for tax, royalty relief

By PATTI EPLER
Daily News reporter

A "personal and confidential" proposal by oil magnate Leon Hess to Gov. Steve Cowper, aimed at cutting costs on a Beaufort Sea project Hess' company is pursuing, has been turned down by the governor as being a bad deal for the state.

So Hess, chairman of Amerada Hess Corp., now says his company will suspend drilling at Northstar/Seal Island, a pair of gravel islands near Prudhoe Bay a few miles off the coast of the North Slope.

Amerada Hess and other oil companies have announced discoveries of commercial quantities of oil at the site. However, the companies never have revealed how much oil they think the reservoir might hold. The state estimates the field contains about 300 million barrels of recoverable crude, a small

field by North Slope standards.

The 73-year-old Hess was in Anchorage last month hoping to convince Cowper to support legislation that would free Amerada Hess from paying royalties and taxes on Northstar production. Hess wants the state to waive the payments until an estimated \$1.8 billion spent to develop the field and build a subsea pipeline has been made up.

Hess pointed out the company bought the Beaufort Sea leases when oil prices were \$35 a barrel. At today's prices — around \$20 a barrel — Northstar development "is not economic and will not occur" without tax relief, he said.

In exchange for a waiver of royalties and taxes, Amerada Hess would give the state the buried pipeline, once the pipeline was paid off, Hess said. That way, the state could collect tariffs on oil shipped through

the line, and an infrastructure would be in place to encourage other offshore projects to go ahead, he said.

Additionally, Northstar development would create construction jobs as well as permanent employment once production began, Hess said.

The company has spent \$80 million exploring the Northstar prospect and had planned to spend another \$50 million this winter to drill more wells, he said.

But state officials don't think the Hess proposal is such a great deal. Especially, they say, because Hess would not disclose how much oil the company has found and give specific cost and financing estimates.

Without knowing how much oil might be produced and at what cost, the state has no

See Page C-8, HESS

Continued from Page C-1

way of accurately judging what it stands to gain or lose, officials said.

Neither Hess nor other company officials returned phone calls this week to talk about the state's concerns.

In memos to Cowper, state oil and gas and revenue officials advised the governor to reject the proposal.

"The Hess proposal offers some new construction activity — much of which would probably be for modules constructed elsewhere — and an unspecified number of new jobs in return for what, conservatively, is likely to be hundreds of millions of dollars in state revenue," wrote James Eason, state oil and gas director.

"If it served as the precedent for similar state participation in additional North Slope oil and gas developments, this cost could quickly grow to billions of dollars," Eason told the governor.

The Northstar leases carry a 20 percent royalty and a 15 percent severance tax. They also are "net profit" leases, which means the company paid less for the leases at a 1979 sale but agreed to pay the state 91 percent to 93 percent of the profits from the leases, after exploration and production expenses are subtracted.

The Hess proposal "essentially translates to a request

for the state to pay approximately 35 percent of Hess' development costs ... through suspension of its royalty and taxes," Eason said. "Meanwhile Hess ... would recover full construction and operating costs plus interest and overhead."

Despite misgivings about the Hess proposal, Eason said, his office has started reviewing incentives and assistance other states are coming up with to help oil companies that want to develop economically marginal fields. He hopes to have some ideas to help Alaska's oil companies formalized in a couple months, he said.

"Hess" North Star Proposal

ACD 1340145

Anchorage Daily News

Sept. 11, 1987

Mr. James Eason
Director
Alaska Division of Oil and Gas
PO Box 107034
Anchorage, Alaska 99510

Dear Mr. Eason:

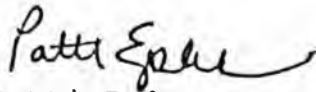
This is a formal request for information pursuant to Alaska's freedom of information and open records laws.

In August, Mr. Leon Hess of Amerada Hess oil company made a proposal to the state having to do with leases and an oil prospect the company owns in the Beaufort Sea. It is my understanding Mr. Hess presented the state with a written proposal/presentation. Further, I understand there has been some correspondence between the state, Governor Cowper and Mr. Hess on the matter.

I would like copies of, or access to, any written or visual material presented to the state by Mr. Hess or his representatives, including details of the proposal. Additionally, I would like copies of any correspondence between state officials and Hess regarding the proposal or other issues related to the company's Beaufort Sea and North Slope leases. I also would like copies of any memos or other communications between state officials on the Hess proposal or issues regarding Amerada Hess leases.

Thank you for your consideration of this request. I look forward to hearing from you within the 10 days required by statute.

Sincerely,



Patti Epler
Staff writer

RECEIVED

SEP 16 1987

DIVISION OF OIL & GAS
ANCHORAGE, ALASKA

MEMORANDUM
DEPARTMENT OF NATURAL RESOURCES

copy file
State of Alaska
DIVISION OF OIL AND GAS

TO: Rod Swope, Special Staff Assistant
Office of the Governor

DATE: September 15, 1987

FILE NO:

TELEPHONE NO: 762-2547

FROM: *James E. Eason*
James E. Eason
Director

SUBJECT: Release of Material in
North Star/Leon Hess
Proposal File

These are the materials in my North Star/Leon Hess proposal file. Materials which are clearly not confidential include the original letter from Leon Hess to Governor Cowper, as well as a copy of the bound Hess Proposal document which Mr. Hess delivered to Governor Cowper at our last meeting. Materials for which you may or may not want to raise the executive privilege argument include all of the documents which I am transmitting by telecopy. I look forward to our discussion.

Enclosure

1067E

DELIVER TO: <i>Rod Swope</i>	LOCATION: <i>Governor's Office</i>
FROM: <i>James Eason</i>	LOCATION: <i>Oil + Gas</i>
TELEPHONE/TELECOPIER # <i>465-3585</i>	TO: NUMBER OF PAGES <i>16</i>
TRANSMITTING CN/SPEED _____	DATE <i>9/15/87</i> TIME <i>2:30</i>
PHONE FOR PROBLEMS-NAME/NUMBER _____	<i>Robert Keith 762-2547</i>
COMMENTS _____	

400 1340148

The Hess proposal literally invalidates the competitive leasing process. Other sale participants submitted bids based upon the expectation that lease terms, including the payment of royalties and taxes, would be required.

Hess' claim of non-economic development cannot be substantiated until the field limits have been fully delineated. By Hess' own admission, additional delineation wells are required. Until recoverable reserves are known and development costs are calculated, it is entirely premature to assume that the field cannot be developed. While oil prices have risen more than 100 percent in the last twelve months, operating costs, including rig rentals and labor have remained low. If this trend continues, Hess' expectations must change. A good example of the dangers of accepting Hess' assumptions is provided by the experience of Sohio and its partners at Endicott. That development was budgeted at more than \$3.2 billion, yet it came in ahead of schedule and for only \$1.2 billion!

The proposal essentially translates to a request for the state to pay approximately 35 percent of Hess' development costs (including pipeline costs) through suspension of its royalty and taxes. Meanwhile Hess (through both its operating company and its transportation affiliates--both pipeline and marine vessels) would recover full construction and operating costs plus interest and overhead. It is important to note that this is not a temporary waiver with future repayment of foregone royalties and taxes after project payout; it is suspension of all state revenues which would otherwise ordinarily accrue until payout with no retroactive recovery. Only prospective payment of royalties and taxes would occur on the then remaining production. If the project is truly as marginal as Hess claims, there could be very few reserves remaining.

The proposal provides every incentive for Hess, through each its affiliates, to pad costs and delay payout. Every dollar spent on operation transportation, construction and overhead would defer payout, and thus the time when royalties and taxes would be payable. To make matters worse, the state would be in no position to effectively monitor or control project costs. The precedent of the Hess proposal would invite requests from similarly situated lessees at nearby fields, including Pt. Thomson, Tern Island, and Milne Point, which is currently shut-in.

In the final analysis, the Hess proposal offers some new construction activity (much of which would probably be for modules constructed elsewhere) and an unspecified number of new jobs in return for what, conservatively, is likely to be hundreds of millions of dollars in state revenue. If it served as the precedent for similar state participation in additional North Slope oil and gas developments, this cost could quickly grow to billions of dollars.

If the state decides to pursue some sort of marginal field assistance, there are numerous options to consider which, unlike the Hess proposal, would treat all lessees equally, and which could be tailored both to quantify beforehand and to minimize the state's revenue loss--both features which the Hess proposal does not offer. The state could agree to undertake a review of industry proposals, as well as recent legislation from other states, to determine if there are options the governor could agree to support. Copies of two recent articles from the Oil and Gas Journal, as well as a News Release from the government of Canada describing the approaches of other energy producing states and Canada are attached.

Buddy
Malone

AMERADA HESS CORPORATION

LEON HESS
Chairman of the Board

RECEIVED

SEP 11 1987

1185 AVENUE OF THE AMERICAS,
NEW YORK, NEW YORK 10038
(212) 997-8400

HAND DELIVERED
GOVERNOR'S OFFICE

September 9, 1987

Personal and Confidential

Honorable Steve Cowper
Governor
State of Alaska
Pouch A
Juneau, AK 99811-0101

Dear Governor Cowper:

I appreciate your courtesy in giving me the opportunity to meet with you, Deputy Commissioner Gorsuch and Mr. Basch concerning our Northstar/Seal Island Prospect in the Beaufort Sea. I wanted you to know that, regretfully, we have made the decision to suspend drilling operations at Northstar/Seal Island. Amerada Hess will not proceed with its delineation drilling program at Northstar/Seal Island in this coming winter season. We have released the Glomar Beaufort Sea I, the vessel which was to perform this work.

I am committed to working with you and your staff with the aim of seeing this project ultimately go forward to development. Based on what we know to date, Northstar/Seal Island is a valuable asset of our Company and, we believe, of the people of Alaska. But I must be plain in stating that we will not be able to bring Northstar/Seal Island to production under current and foreseeable world oil prices without relief from Alaska royalty and severance tax burdens. Without such relief, the project's cash flows will never be sufficient to pay out development costs, and without the assurance of payout of development costs, Amerada Hess will not be successful in obtaining the project financing necessary to undertake a project of this magnitude.

I want to review several very important points we touched on during our meeting.

1. Amerada Hess is not seeking special relief. We are suggesting that incentives, in the form of tax and severance forgiveness for a period of time, be adopted to encourage the development of smaller Alaskan oil fields. Northstar/Seal Island, based on current reserve estimates, is such a smaller field and deserving of such relief. Without this incentive, development of Northstar/Seal Island, as well as other, smaller prospective oil fields, is not economic and will not occur. This would be a great loss for all concerned.

2. The State of Alaska loses nothing by adopting such legislation. It seems obvious to me that Alaska's revenues will in fact be enhanced over time, rather than diminished. Without relief these smaller fields will not be brought into production. If Alaska does nothing to encourage development, it is unlikely that Alaska will ever receive any revenue from these potentially productive fields. There is no cost to providing relief from severance taxes and royalty -- only the potential for future gain through net profits and royalty and severance taxes paid in full on oil produced after the project pays out.

It was mentioned in our discussions that Alaska has spent two billion dollars in less than a decade on the development of energy programs. Our proposal is both cost and risk-free to the State, with long term, beneficial economic and social consequences.

3. The incentives Amerada Hess believes Alaska must adopt are not novel. A number of oil-producing states, notably among them Louisiana, Mississippi, Montana, New Mexico, North Dakota and Oklahoma, have already acted to suspend or reduce severance tax and/or royalty payments to encourage drilling activities. Internationally, Canada has been very aggressive in the reduction of tax and royalty burdens to promote exploratory drilling, including a five-year royalty free period for new wells. The United Kingdom has for some time encouraged the development of smaller fields through effective life-of-the-field relief from the U.K. Petroleum Revenue Tax. Norway is considering similar legislation. We can provide you with details on what other oil-producing states and countries are doing, but the point I want to make is that Alaska would not be alone in seeking to encourage, through royalty and severance tax relief, the development of otherwise uneconomic fields such as Northstar/Seal Island. Indeed, many other oil producing states and countries have already recognized the need for and long-term benefit of adopting such legislation.

4. We are not wedded to the proposal to contribute the project's subsea pipeline to the State, or to any particular form of that proposal. Our proposal to build and contribute to Alaska the subsea pipeline serving Northstar/Seal Island is intended to provide a positive, long-term benefit to Alaska, in recognition of the State's cooperation in promoting development of the field through royalty and severance tax relief. Tariffs will be paid by all users, including Northstar/Seal Island and other nearby prospective fields. Experience dictates these nearby fields will be oil productive, and development of these fields will be encouraged if pipeline transportation is already in place. I reiterate, as stated in my July 10 letter, that Amerada Hess does not seek to involve in any way the credit of the State, or any State authority, in the financing of the Northstar/Seal Island Project through this proposal. Most importantly, we recognize that the proposal, as well as any alternatives, require substantial discussion and further definition.

As I flew home after our meeting, I was much discouraged with my obvious failure to explain adequately our Company's proposals. Amerada Hess cannot go forward without your support. We had no choice but to take the disappointing step of halting further exploratory work at Northstar/Seal Island. My hope is that over time we will be able to demonstrate to you and your staff the great benefits to Alaska, not only in jobs but in future revenues, of providing incentives for small field development, and so gain your support for the required legislative program to secure such relief. I look forward to working with you and your staff towards this goal.

Sincerely,

Frank Hess



STATE OF ALASKA
OFFICE OF THE GOVERNOR
JUNEAU

cy to Eason pls -
L
RECEIVED

AUG 31 1987


DIV. OF OIL & GAS
DIRECTOR'S OFFICE

MEMORANDUM

TO: Garrey Poska
Chief of Staff

DATE: August 26, 1987

PHONE: 465-3500

FROM: 
Rod Scope
Special Staff Assistant
to the Governor

SUBJECT: Request for
Briefing Meeting
with the Governor

This morning I held a conference call/meeting with Commissioner Malone (in my office) and Lennie Gorsuch (on the phone in Anchorage) to debrief on the Governor's meeting that occurred with Mr. Leon Hess earlier this week.

Issues Summary

Per our discussion, we collectively agreed that the Governor should be briefed as soon as possible on two issues that were raised at the meeting with Leon Hess. Specifically, (1) a desire by the Governor to know more about the background and credentials of a person named Kurt Wulff. (as a person who is reported to be knowledgeable about the oil industry), and (2) the need for additional information about Leon Hess' proposal.

Laura has tentatively scheduled a briefing for 9:00-9:30 a.m. in the morning for the Governor.

Need for Briefing

To brief the Governor on his requests and to let him know who is following up on his concerns/frustrations. He also needs to know about some very recent discussions with petroleum companies that occurred with Lennie and Jim Eason (the discussions are relevant to Amerada Hess) before he takes any independent actions or has further discussions with anyone relative to this issue.

Finally, the Governor needs to know about efforts underway by DNR to examine special state incentives as they relate to the health and well-being of the oil industry at both a national and local level.

Current Agency Involvement

DNR staff was able to brief the Governor before the meeting with Leon Hess. The Department of Revenue also provided input and has been involved in this exercise. The issues involve state oil and gas leases and state royalty, interest from these leases which in turn directly affects the Department of Revenue and their various projections.

State Policies

The principal state policies involved are (1) the policy of adhering to standard conditions of our state leases, and (2) allocation of state royalty oil, interest and taxes. Obviously, these policies indirectly affect others that are being developed based on amount of revenue being received by the state from oil and gas development.

Next Step

The Governor may be going to Washington, D.C. the first week in October. At that time he may want to meet with Kurt Wulff, Leon Hess, etc. Therefore, our follow-up should be completed by then.

Resources Required

None

Recommendation

None

**DNR Briefing
Governor Steve Cowper
August 24, 1987**

Leon Hess Meeting

--State permits for delineation drilling on North Star Prospect

--Hess Proposal

- *Pipeline to TAPS
- *Royalty deferral
- *Severance tax deferral

Takeda/ Hiraki Meeting

--Alaska Pacific Refinery

--Fox Energy

--Gas Reserves Tax

Incentives/relief for industries in Alaska

Rod Swope
Special Staff Assistant
to the Governor

August 21, 1987

Seal Island Proposal

Hugh Malone, Commissioner
Department of Revenue

I agree completely with the Department of Natural Resources reserve on the Seal Island Project proposal as set set out in document 0998E. There will be plenty of time after completion of delineation drilling to evaluate the need of any subsidies to the lessee.

I would also point out that our present severance tax ELF provides reduction in the tax rate for marginal cost production. The lessee's claim that a 15 percent severance tax is too high ignores this fact. In addition the lessee can apply for exploration credits and royalty reduction on meeting certain conditions under AS 38.05.180, which is also ignored by the lessee.

The proposal by the lessee should be reviewed after the delineation drilling is completed.

MEMORANDUM
DEPARTMENT OF NATURAL RESOURCES

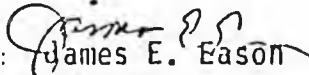
State of Alaska
DIVISION OF OIL AND GAS

TO: Lennie Gorsuch
Deputy Commissioner

DATE: August 21, 1987

FILE NO: C O N F I D E N T I A L

TELEPHONE NO: 762-2547

FROM: 
James E. Eason
Director

SUBJECT: Preliminary Thoughts on
the Hess Proposal for
Royalty and Tax Relief

This letter responds to your request for my preliminary thoughts on the Leon Hess proposal for Northstar royalty and tax relief. Because these are only preliminary thoughts, I will simply list them, without extensive analysis or careful organization.

* In addition to policy concerns, the extent of the legal constraints on legislative power to grant royalty and tax waivers are uncertain at this time. First, there may be a legal question whether a legislature has the authority to bind future legislatures on a tax matter. That is, a tax waiver may not be possible as a matter of law. Second, section 6(i) of the Alaska Statehood Act, the Alaska Constitution or the common law public trust doctrine may be interpreted to prohibit the waiver of royalties. In the 6(i) suit, Trustees for Alaska convinced the Alaska Supreme Court that section 6(i) of the Alaska Statehood Act requires rents or royalties for hardrock mining rights. The same ruling would apply to oil and gas rights in state "mineral lands" acquired under section 6 of the Statehood Act. Notably, the Alaska Supreme Court did not reach the issue as to whether the state constitution and the common law public trust doctrine require rental or royalty income. The case is still active (the state has petitioned the United States Supreme Court) and the Alaska Court could still reach the state law issues.

* Hess proposes to "contribute" the pipeline as a "bonus" to the state, and asserts that his proposal would not "involve in any way the credit of the state in the financing." (emphasis in original.) This rhetoric obscures the reality that the state could potentially pay much more, and have many fewer protections under the Hess proposal than if it were directly involved in the financing.

If directly involved in extending or guaranteeing credit, the state would have some control over the terms and extent of the project and could insist upon significant protections. These could include fixed loan limits, a definite loan term, fixed payments, a security interest and other protections. Instead, under the Hess proposal, the state is, at best, "buying" the pipeline (even that is not guaranteed, since there may never be any payout) for delivery at some unknown time in the future (when the useful life of the pipeline or field could be nearly over). The "price" to the state is substantial; 35 percent of the lease revenues (20 percent royalty waiver plus 15 percent tax waiver). The total amount paid would guarantee recoupment of capital costs and interest to the leaseholders for both the pipeline and the field development.

However, the state would gain title only to the pipeline. To be sure, the lessees would be contributing some of their share of lease revenues to project cost recoupment. However, some of their share of revenues would go to operating costs -- costs which they would have to cover out of their share before taxes and royalties are determined. This makes it extremely difficult (impossible??) to calculate how much of the pipeline (and field development) the state would be paying for, but it clearly would be a lot. Any characterization of the contingent conveyance of the pipeline as a "bonus" or "contribution" is entirely disingenuous.

- * If the state entertained this proposal, it will have no principled way of refusing other resource developers the opportunity to subordinate state tax and royalty income to full recoupment of the development costs. It would reverse a long tradition here, as well as in other mineral-producing states, of requiring that the royalty be free of costs and risks of development. For these reasons, this extraordinary proposal should probably be considered, if at all, in the context of general legislation which treats all state oil and gas (and coal and gold and ???) lessees in the same manner.
- * Hess has clearly not revealed all the relevant information he currently possesses, and even the data which he has revealed are clearly insufficient to provide the basis for informed decision-making. Missing, but essential elements would include the reserve estimates, cost estimates, price estimates, payout estimates and much more are essential pre-decisional background. Hess characterizes his offer as involving "short-term relief" to the oil companies in return for "long-term benefits" to the state. However, there is no basis for concluding the relief will be short or limited in any way (especially monetarily), or that there will be benefits, let alone long-term ones. Unless Hess can predict the future with absolute certainty, he cannot defend these claims.
- * Even if the state were predisposed to some sort of "relief", this particular proposal cannot be properly considered until more details are known. The interaction between this proposal and the unit agreement which would presumably govern development and cost-sharing with other lessees needs to be clarified. For instance, how would operating costs be determined and paid? The interaction between this proposal and its impacts on federal royalty and taxes would have to be clarified. Will Hess ask for a similar waiver of federal royalties and taxes for those reserves underlying federal acreage? Many accounting details could have tremendous impact. How would overhead be treated? What rate of return should Hess be allowed for its capital contribution? How would the tax value of depreciation of the field development facilities and pipeline be factored? Would the pipeline be a common carrier from the inception? How would tariff payments, designed to recoup pipeline development and overhead costs and provide profit, be treated under the Hess proposal?

As you know, pipeline tariffs are typically deductions from gross revenues for purposes of determining the net amount on which the royalty or tax percentage is taken. Here, presumably, tariff revenues would be applied at least partly to project cost recovery. Would the APUC's or FERC's cost recovery schedule for tariff purposes control when the state might gain title to the pipeline and commence to receive royalties and taxes? Or, would some oil revenues be used to supplement tariffs to accelerate pipeline cost recoupment? Would the state's tariff on the pipeline (after it gets it) be limited to operating costs and profit because of the fact that the state would not get title until after all capital costs are recouped? Doesn't sound like much of a deal to me, particularly if the state is saddled with dismantling and removing the structure.

- * At the time of the lease sale, Hess won the leases by outbidding rivals and paying the bonus. The bidding was based upon the understanding that the bonus and rents only entitled a lessee to hold and explore the lease; production would carry a 20 percent cost-free royalty burden, a tax burden and a net profit burden. Hess is proposing that the two major burdens, royalty and tax, be eliminated for a potentially unlimited time--conceivably for the life of the field if prices were to fall sufficiently. Before this unprecedented post facto change is made to the state's leasing program, the impact on the integrity of the leasing process should be carefully evaluated. I guess this could be characterized as a polite way of saying..."I can't imagine what the worth of any of our oil and gas leases might be after the first step was taken."
- * Hess proposes that the waivers terminate after payout on all capital expenses, with interest. How would this proposal interact with reimbursement of operating costs, which presumably would be paid on a current basis from production income? Would overhead and profits be allowed as part of the capital costs? As part of the operating costs?
- * What safeguard or control would the state have on the amount of capital costs and the rate of interest?
- * What safeguards would the state have against imprudent or manipulative establishment of the amount of "lease revenues"? Under the lease, the state has protections to ensure proper royalty value. For instance, the royalty value of production sold under a non-arm's-length contract would be valued at market value or contract price, whichever was higher. When there is no royalty due, some equivalent protection would be appropriate.
- * The proposed legislation would be special legislation, restricted by Alaska Constitution, Article 11, Section 19. The last oil and gas-related special legislation, Conoco's SB 430 (1986), to lessen royalty obligation for Milne Point, did not pass the legislature. What, if anything, is needed is a comprehensive marginal field statute, which addresses royalty

Lennie Gorsuch
August 21, 1987
Page 4

and/or tax relief for all the state's marginal fields, with definition of marginality and limits on relief, rather than ad hoc "fixes". Royalty reduction restriction in AS 38.05.180(j) would be superseded by the new legislation (new legislation controls old legislation), but the exemption should be expressly stated to avoid litigation.

- * The proposal to suspend royalty and tax until "payout" raises all the horrors of administering NPSLs without the protections. There would be no regulations or base provisions to say which expenses (out-of-state expenses, overhead, etc.) went towards payout. Litigation would be likely no matter how the standards were expressed. Similarly, there would be no safeguards against "gold-plating", where Hess builds large fancy facilities to transfer to a construction area or subsidiary to delay "payout".

As I said, these thoughts are not very well organized--my apology--but given the momentum this proposal seems to be gathering and the overwhelming downsides (in my parochial view), I thought it best to get some talking points on paper. I see the value of creating jobs--but not a few jobs for a short period of time in exchange for the evisceration of the state's leases and the potentially gigantic revenue losses which would follow. The state would literally need a new division to entertain all the proposals. Don't forget Exxon's shut-in "marginal field" at Pt. Thomson.....

0989E

(CW)
cc: JMB
Jim Cowper
LO

Please review
Rod Swope asked
LNR & Revenue
to develop a position
on this ASAP
(Tom Koester was
in cell but is out
of town)

August 5, 1987

DEPARTMENT OF
NATURAL RESOURCES

AUG 04 1987

COMMISSIONER'S OFFICE
JUNEAU

Please send up
time to discuss
this with
Commissioner
next week
JMB

Mr. Leon Hess
Chairman of the Board
Amerada Hess Corporation
1185 Avenue of the Americas
New York, NY 10036

Dear Mr. Hess:

I enjoyed the opportunity to meet with you in June to discuss your proposed activities in Alaska.

Your letter regarding the need for legislative initiatives to relieve the Northstar project of state royalty and severance tax burdens just arrived. I have asked some of my professional and technical staff in the Departments of Natural Resources and Revenue to review the proposal and suggestions contained in your letter. I will contact you once I have had an opportunity to confer with my staff.

I am hopeful that we will be able to work with you to develop a mutually acceptable and beneficial plan.

Sincerely,

Steve Cowper
Governor

bcc: Commissioner Judith M. Brady
Department of Natural Resources
Commissioner Hugh Malone
Department of Revenue
Tom Koester, Assistant Attorney General
Department of Law

RECEIVED

AUG 06 1987

DIVISION OF OIL & GAS
ANCHORAGE, ALASKA

SC/RS/mw

AMERADIA HESS CORPORATION

1185 AVENUE OF THE AMERICAS,
NEW YORK, NEW YORK 10036
(212) 997-8400

LEON HESS
Chairman of the Board

July 10, 1987

Personal and Confidential

Honorable Steve Cowper
Governor
State of Alaska
P.O. Box A
Juneau, AK 99311-0101

Dear Governor Cowper:

I appreciate your taking time from your busy schedule to meet with us to hear an update on Amerada Hess' Northstar Prospect in the Beaufort Sea. We believe the Northstar Prospect has significant potential for economic benefit both to our company and to the people of the State of Alaska.

Sadly, this project can never be brought to development, given the collapse in world crude oil prices that occurred in 1986 and the changed economic realities of the oil business, unless the legislature of the State of Alaska recognizes the need for and implements realistic development incentives. As you know, other oil producing states have recently undertaken actions to revitalize exploration and production programs within their borders.

In 1979, when bids were submitted for the Federal/State Beaufort Sea Oil and Gas Lease Sale in which the Northstar Prospect leases were awarded, the world price of crude oil was \$35.00 per barrel. Projections were for steadily increasing prices over the years ahead. Today, although some stability has returned to world oil markets, the economics of the market are completely different. In the aftermath of the OPEC-inspired price war, world oil prices stand in the \$20.00 per barrel range. No one reasonably anticipates a return to world crude oil prices of \$35.00 per barrel until at least after 1995.

That is why under current reserve assumptions development of the Northstar Prospect is not economic and will not occur. Simply put, with a 20% royalty burden and a 15% severance tax, the project will never pay out.

To make development even marginally viable, we need your support of legislative initiatives to relieve the project of Alaska State royalty and severance tax burdens. Without such relief, no company can proceed.

AGO 1340162

Page 2
Governor Cowper
July 10, 1987

I want to assure you that this is not a matter that is within our company's discretion. The development of the Northstar/Seal Island Project is an enormous financial undertaking. Preliminary design estimates over a year ago indicated a total cost of approximately \$1.5 billion. A project of this magnitude cannot be financed from internal cash flow and will require substantial borrowing from outside sources on a project finance basis. Project financing will not be obtainable unless it can be demonstrated to the lenders that the project will pay out within a reasonable period of time and that cash flows from the project will be sufficient to service principal and interest payments on the debt.

I know you are aware of the substantial benefits to the State of Alaska if this project proceeds. Many jobs will be provided by development work, the construction of production facilities and ongoing field operations during production. Additional jobs will be created by the construction of the subsea pipeline, as well as by ongoing pipeline operations once production commences at the Northstar/Seal Island field, and future fields served by the pipeline. The Alaska State leases involved are substantial net profit leases, ranging from 91% to 93%, and, even with royalty and severance tax relief, production after payout will generate significant royalty and severance tax revenues. Over the life of the Northstar/Seal Island field these leases will be a source of substantial revenue to the State of Alaska.

All this will obviously be lost if development never proceeds.

During our meeting, you requested an outline of our proposals. I emphasize that what is set out below represents only our preliminary thinking, our suggestions as to a possible approach. It is a basis for discussion, and you and your staff will undoubtedly have your own thoughts and ideas, which we welcome. Moreover, none of us will want to go forward to initiate these legislative proposals until our delineation drilling program of this coming winter season is completed and our company has a better feel for the developable reserves in the Northstar/Seal Island Project. In addition, the Northstar/Seal Island Project will ultimately be unitized and the participation of our partners, holding both Federal and Alaska State Leases, is necessary for any final position.

Our proposal is this:

AGO 1340163

1. The Alaska State Legislature must adopt legislation providing the Northstar/Seal Island Project relief from royalty and severance tax obligations for a period of time until full

development costs including interest are paid back. This legislation should provide:

°Waiver of the 20% royalty accruing to the State of Alaska on all production in the period prior to payout of project development costs. Payout would be defined as full recovery of total capital investment in the project, which would include principal and actual interest paid on project financing. Royalties on production should commence at the time payout is achieved, and all production thereafter should bear royalty at the full 20% rate.

°Waiver of the 15% state severance tax on all production in the period prior to payout, as above. As with the royalty obligation, severance taxes should become payable at the full 15% rate with respect to all production after payout.

2. The legislation we suggest should condition waiver of the royalty and severance tax on an agreement to contribute the subsea pipeline serving the Northstar/Seal Island Project to the State of Alaska, or to an appropriate Alaska State authority, upon payout of the Northstar/Seal Island Project. The proposed route of the subsea pipeline is shown on the map we left with you during our visit.

To facilitate the pipeline contribution:

°The pipeline would be constructed with sufficient capacity so that it could operate as a common carrier providing transportation for future production from neighboring prospective oil fields to Pump Station No. 1.

°The pipeline would be established as a separate entity. Financing of pipeline construction, estimated at approximately \$300 million, would be undertaken at the same time as the financing for the Northstar/Seal Island Project production facilities, but would be treated as an entirely separate, independently based financing package. The State of Alaska would bear no credit risk or take on any obligation with respect to this financing.

°Amerada Hess would be the owner of the pipeline prior to payout of development costs for the Northstar/Seal Island Project. Amerada Hess would agree to contribute the pipeline to the State of Alaska at the time payout was achieved, and would enter into an agreement to operate the pipeline after its contribution to the State of Alaska.

Page 4
Governor Cowper
July 10, 1987

*Tariffs would be established, applicable to all users including the Northstar/Seal Island Project and future field developments. These tariffs would provide a reasonable profit to the State after providing for the costs of pipeline operation and maintenance.

Our proposal to contribute the Northstar subsea pipeline to the State of Alaska is intended to provide a bonus to the State once payout of the Northstar/Seal Island Project is accomplished. The direct and immediate benefit would be through the tariffs received by the State. Long term, the existence of the pipeline would offer and be available as an economic incentive for the development of other nearby blocks, both Federal and State, whose development might otherwise be uneconomic without the benefit of existing, nearby Alaska State pipeline transportation to Pump Station No. 1.

This part of our legislative proposal obviously requires a good deal of further definition, but whatever its final form our sole aim and objective would be to provide an ongoing economic benefit to Alaska through the permanent contribution of the pipeline and its revenues to the State. I want to stress to you that we are not looking to involve in any way the credit of the State in the financing of the Northstar/Seal Island Project or the subsea pipeline. Contribution of the pipeline to the State would occur only after all Northstar/Seal Island Project debt and subsea pipeline debt was fully repaid.

Our Northstar leases have 1990 expiration dates. Amerada Hess has already expended over \$80 million on exploration at Northstar. Amerada Hess must act now in the 1987-88 winter season to do the additional drilling required to delineate the Northstar Prospect's crude oil reserves. Amerada Hess will spend \$40 to \$50 million on this delineation drilling program.

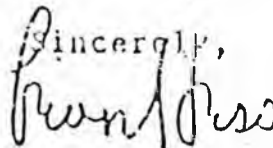
We need your Administration's cooperation in expediting the permitting process for this drilling activity. However, if after completion of our company's delineation drilling program, legislative relief along the lines proposed is not initiated and successfully implemented, our company would be much better off if the permits were never issued.

Amerada Hess believes that the crude oil reserves at Northstar are a substantial asset of the State of Alaska that should be developed. The long term benefits of bringing the field into production should not be lost by a failure of the State of Alaska to provide the short term relief from royalty and severance taxes required for the project to proceed.

Page 5
Governor Cowper
July 10, 1987

Unless you are convinced a world crude oil price of \$35 a barrel is around the corner, a legislative initiative along the lines we have proposed is essential, the crucial ingredient being a sufficient economic incentive to permit the Northstar/Seal Island Project to pay out. Without payout at a reasonable date the project cannot be financed and will not be undertaken. The State of Alaska will not have the benefit of the jobs and future revenues from royalties, severance taxes and net profits accruing to it after payout of a successful oil field.

We hope, after completion of our delineation wells, the results will be encouraging, and that you will then agree to sponsor the initiatives required to bring this important project to production. We stand ready to work with your Administration in formulating a plan which you can endorse.

Sincerely,


Leon Hess

jE



AMERADA HESS CORPORATION

NORTHSTAR PROSPECT

PRESENTATION FOR GOVERNOR COWPER

AUGUST 1987

CONFIDENTIAL

AGD 1340167

AMERADA HESS CORPORATION
NORTHSTAR PROSPECT
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<u>PAGE NO.</u>	<u>ITEM</u>
1	PROSPECT MAP
2	PROSPECT BACKGROUND
3	"CIDS" PHOTOGRAPH
4	DRILLING OUTLINE
5	PROSPECT PIPELINE MAP
6	ECONOMICS
7	PROPOSAL

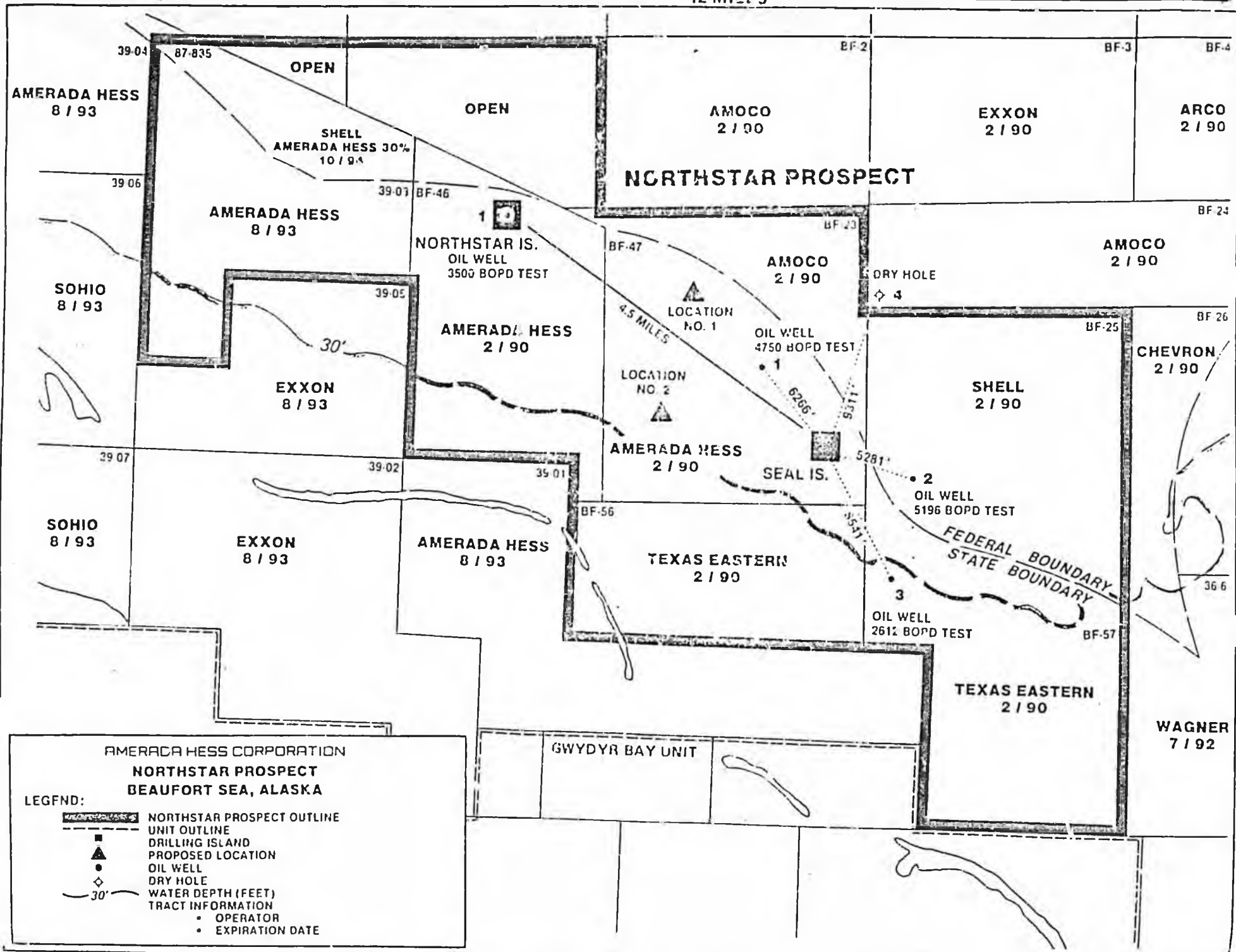
SUPPLEMENTAL ITEMS

PROPOSAL LETTER
RESPONSE LETTER
NOTICE

12 MILES

7 MILES

AGD 1340169



AMERADA HESS CORPORATION
NORTHSTAR PROSPECT
BEAUFORT SEA, ALASKA

LEGEND:

- NORTHSTAR PROSPECT OUTLINE
- UNIT OUTLINE
- DRILLING ISLAND
- PROPOSED LOCATION
- OIL WELL
- DRY HOLE
- WATER DEPTH (FEET)
- TRACT INFORMATION
- OPERATOR
 - EXPIRATION DATE

AMERADA HESS CORPORATION
NORTHSTAR PROSPECT
BACKGROUND

- LOCATED 20 MILES NORTHWEST OF PUMP STATION NO. 1 IN 40 - 45' OF WATER.
 - SITUATED ON STATE LEASES OWNED BY AMERADA HESS CORPORATION AND TEXAS EASTERN AND ON FEDERAL LEASES OWNED BY SHELL, MURPHY OIL AND AMOCO.
 - SEAL ISLAND CONSTRUCTED IN 1982 ON AMERADA HESS STATE LEASE BF-47.
 - SEAL NO. 1 DRILLED ON AMERADA HESS STATE LEASE BF-47 IN 1983 TESTED 4,750 BOPD FROM 11,000 ± FEET.
 - CONFIRMATION WELLS COMPLETED ON SHELL / MURPHY FEDERAL TRACT BF-25 IN 1984 AND TEXAS EASTERN STATE LEASE BF-57 IN 1985.
 - NORTHSTAR ISLAND WAS BUILT IN 1985 ON AMERADA HESS STATE LEASE BF-46 AND A CONFIRMATION WELL WAS COMPLETED ON THIS BLOCK IN 1986.
 - OPERATIONS WERE SUSPENDED IN EARLY 1986 WHEN WORLD OIL PRICES DECLINED AND AT THAT TIME AMERADA HESS HAD INVESTED \$83,000,000.
- TWO ADDITIONAL WELLS ARE REQUIRED AT A COST OF APPROXIMATELY \$40,000,000 TO DELINEATE THE RESERVES.

ASD 1340170

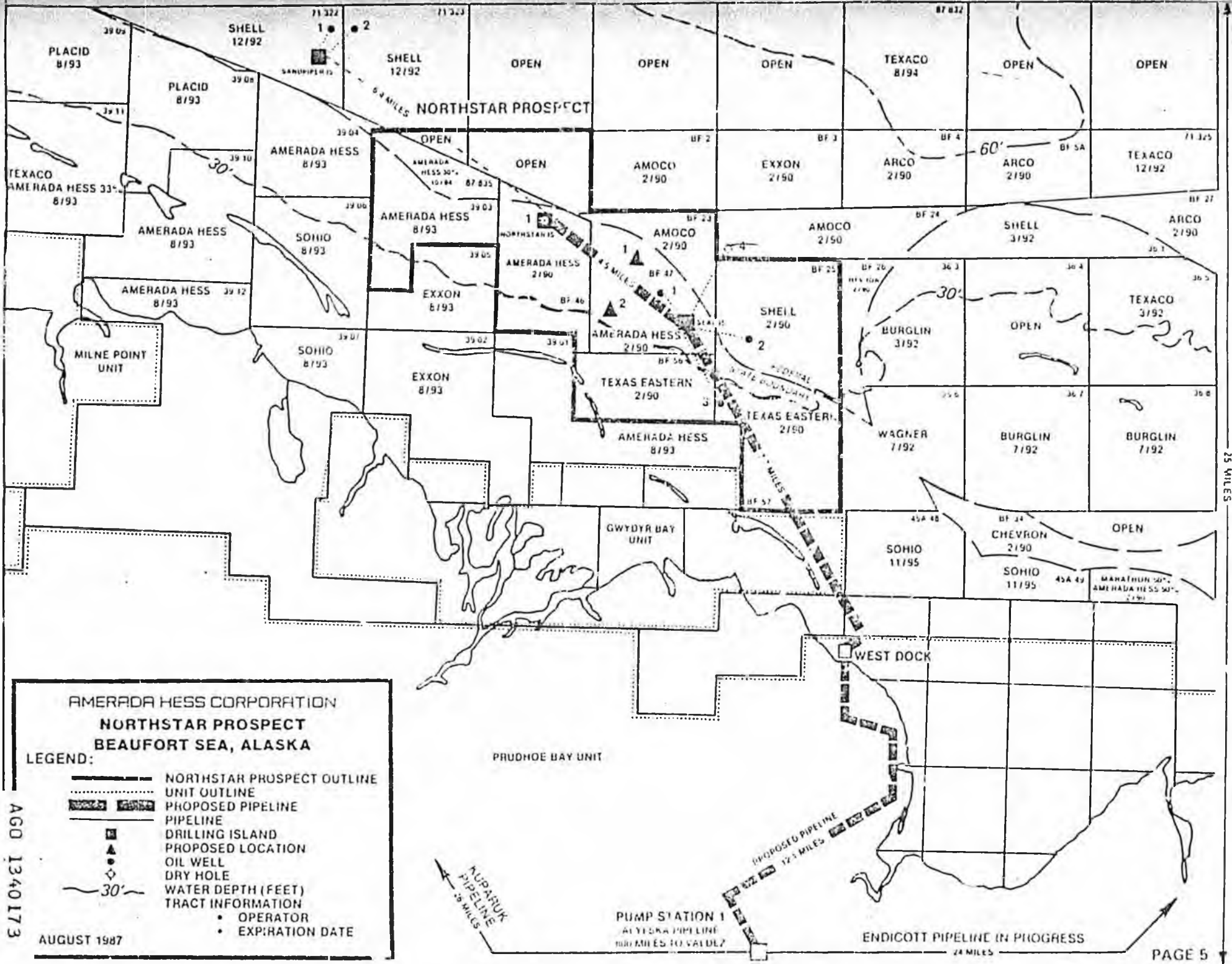


AGO 1340171

AMERADA HESS CORPORATION
NORTHSTAR PROSPECT
DRILLING




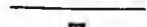



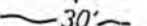


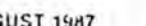

- AMERADA HESS HAS CONTRACTED TO EMPLOY A CONCRETE ISLAND DRILLING SYSTEM, THE GLOMAR BEAUFORT SEA I, DURING THE 1987 - 1988 WINTER DRILLING SEASON.
- THE GLOMAR BEAUFORT SEA I MUST BE MOVED ON LOCATION TO DRILL THE FIRST WELL BY OCEAN GOING TUGS PRIOR TO ICE IN.
- THE DRILLING COMPANY HAS NOTIFIED AMERADA HESS THAT THE LAST PRACTICABLE DATE TO COMMENCE THE MOVE IS AUGUST 30, 1987. LETTER ATTACHED.
- DEADLINE FOR AMERADA HESS TO AUTHORIZE DRILLING COMPANY TO PROCEED IS MONDAY, AUGUST 24, 1987.
- AMERADA HESS CANNOT PROCEED WITHOUT ASSURANCE OF INITIATION AND SUPPORT OF LEGISLATIVE RELIEF FROM ROYALTY AND SEVERANCE TAX.
- DRILLING COMPANY MAY TERMINATE CONTRACT IF AMERADA HESS DOES NOT MEET MONDAY DEADLINE, AND REQUIRE AMERADA HESS TO PAY \$1,000,000 IN DAMAGES.

AGO 1340172



AMERADA HESS CORPORATION
NORTHSTAR PROSPECT
BEAUFORT SEA, ALASKA

LEGEND:

-  NORTHSTAR PROSPECT OUTLINE
-  UNIT OUTLINE
-  PROPOSED PIPELINE
-  PIPELINE
-  DRILLING ISLAND
-  PROPOSED LOCATION
-  OIL WELL
-  DRY HOLE
-  WATER DEPTH (FEET)
-  TRACT INFORMATION
-  OPERATOR
-  EXPIRATION DATE

AGD 1340173

AUGUST 1987

PUMP STATION 1
 ALASKA PIPELINE
 100 MILES TO VALDEZ

ENDICOTT PIPELINE IN PROGRESS
 24 MILES

AMERADA HESS CORPORATION
NORTHSTAR PROSPECT
ECONOMICS

- DEVELOPMENT COSTS CURRENTLY ESTIMATED TO BE \$1,200,000,000.
- PIPELINE CONSTRUCTION COSTS CURRENTLY ESTIMATED TO BE \$300,000,000.
- DEVELOPMENT WILL REQUIRE PROJECT FINANCING FROM OUTSIDE SOURCES.
- LENDERS WILL REQUIRE PROJECT CASH FLOWS SUFFICIENT TO SERVICE DEBT AND INTEREST AND TO PAY OUT CAPITAL INVESTMENT WITHIN A REASONABLE PERIOD OF TIME.
- WHEN O.I.L WAS \$35.00 PER BARREL, STATE LEASES CALLED FOR 20% ROYALTY BURDEN AND 15% SEVERANCE TAX, PLUS NET PROFIT SHARE TO THE STATE. AMERADA HESS STATE LEASES PROVIDE NET PROFIT SHARE RANGING FROM 91% TO 93%.
- UNDER CURRENT RESERVE ASSUMPTIONS, PROJECT WILL NEVER PAY OUT, WITHOUT ROYALTY AND SEVERANCE TAX RELIEF.

AGD 1340174

AMERADP HESS CORPORATION
NORT STAR PROSPECT
PROPOSAL

- STATE RELIEF FROM ROYALTY AND SEVERANCE TAX BURDENS UNTIL RECOVERY OF TOTAL CAPITAL INVESTMENT, INCLUDING PRINCIPAL AND INTEREST PAID ON PROJECT FINANCING.
- AMERADA HESS WILL CONTRIBUTE SUBSEA PIPELINE SERVING THE PROJECT TO THE STATE AT PROJECT PAY OUT.
- PAST EXPERIENCE HAS PROVEN THAT CONTIGUOUS ACREAGE WILL BE OIL PRODUCTIVE.
- PIPELINE WILL HAVE SUFFICIENT CAPACITY TO SERVE AS A COMMON CARRIER FOR FUTURE PRODUCTION FROM THESE OIL FIELDS.
- TARIFFS WILL BE PAID BY ALL USERS, INCLUDING NORTHSTAR PROJECT, PROVIDING NET PROFIT TO THE STATE AFTER COSTS OF PIPELINE OPERATION.

AGO 1340175

AMERADA HESS CORPORATION

LEON HESS
Chairman of the Board

1185 AVENUE OF THE AMERICAS
NEW YORK, NEW YORK 10036
(212) 997-8400

July 10, 1987

Personal and Confidential

Honorable Steve Cowper
Governor
State of Alaska
P.O. Box A
Juneau, AK 99811-0101

Dear Governor Cowper:

I appreciate your taking time from your busy schedule to meet with us to hear an update on Amerada Hess' Northstar Prospect in the Beaufort Sea. We believe the Northstar Prospect has significant potential for economic benefit both to our company and to the people of the State of Alaska.

Sadly, this project can never be brought to development, given the collapse in world crude oil prices that occurred in 1986 and the changed economic realities of the oil business, unless the legislature of the State of Alaska recognizes the need for and implements realistic development incentives. As you know, other oil producing states have recently undertaken actions to revitalize exploration and production programs within their borders.

In 1979, when bids were submitted for the Federal/State Beaufort Sea Oil and Gas Lease Sale in which the Northstar Prospect leases were awarded, the world price of crude oil was \$35.00 per barrel. Projections were for steadily increasing prices over the years ahead. Today, although some stability has returned to world oil markets, the economics of the market are completely different. In the aftermath of the OPEC-inspired price war, world oil prices stand in the \$20.00 per barrel range. No one reasonably anticipates a return to world crude oil prices of \$35.00 per barrel until at least after 1995.

That is why under current reserve assumptions development of the Northstar Prospect is not economic and will not occur. Simply put, with a 20% royalty burden and a 15% severance tax, the project will never pay out.

To make development even marginally viable, we need your support of legislative initiatives to relieve the project of Alaska State royalty and severance tax burdens. Without such relief, no company can proceed.

AGO 1340176

Page 2
Governor Cowper
July 10, 1987

I want to assure you that this is not a matter that is within our company's discretion. The development of the Northstar/Seal Island Project is an enormous financial undertaking. Preliminary design estimates over a year ago indicated a total cost of approximately \$1.5 billion. A project of this magnitude cannot be financed from internal cash flow and will require substantial borrowing from outside sources on a project finance basis. Project financing will not be obtainable unless it can be demonstrated to the lenders that the project will pay out within a reasonable period of time and that cash flows from the project will be sufficient to service principal and interest payments on the debt.

I know you are aware of the substantial benefits to the State of Alaska if this project proceeds. Many jobs will be provided by development work, the construction of production facilities and ongoing field operations during production. Additional jobs will be created by the construction of the subsea pipeline, as well as by ongoing pipeline operations once production commences at the Northstar/Seal Island field, and future fields served by the pipeline. The Alaska State leases involved are substantial net profit leases, ranging from 91% to 93%, and, even with royalty and severance tax relief, production after payout will generate significant royalty and severance tax revenues. Over the life of the Northstar/Seal Island field these leases will be a source of substantial revenue to the State of Alaska.

All this will obviously be lost if development never proceeds.

During our meeting, you requested an outline of our proposals. I emphasize that what is set out below represents only our preliminary thinking, our suggestions as to a possible approach. It is a basis for discussion, and you and your staff will undoubtedly have your own thoughts and ideas, which we welcome. Moreover, none of us will want to go forward to initiate these legislative proposals until our delineation drilling program of this coming winter season is completed and our company has a better feel for the developable reserves in the Northstar/Seal Island Project. In addition, the Northstar/Seal Island Project will ultimately be unitized and the participation of our partners, holding both Federal and Alaska State Leases, is necessary for any final position.

Our proposal is this:

1. The Alaska State Legislature must adopt legislation providing the Northstar/Seal Island Project relief from royalty and severance tax obligations for a period of time until full

AGO 1340177

Page 3
Governor Cowper
July 10, 1987

development costs including interest are paid back. This legislation should provide:

°Waiver of the 20% royalty accruing to the State of Alaska on all production in the period prior to payout of project development costs. Payout would be defined as full recovery of total capital investment in the project, which would include principal and actual interest paid on project financing. Royalties on production should commence at the time payout is achieved, and all production thereafter should bear royalty at the full 20% rate.

°Waiver of the 15% state severance tax on all production in the period prior to payout, as above. As with the royalty obligation, severance taxes should become payable at the full 15% rate with respect to all production after payout.

2. The legislation we suggest should condition waiver of the royalty and severance tax on an agreement to contribute the subsea pipeline serving the Northstar/Seal Island Project to the State of Alaska, or to an appropriate Alaska State authority, upon payout of the Northstar/Seal Island Project. The proposed route of the subsea pipeline is shown on the map we left with you during our visit.

To facilitate the pipeline contribution:

°The pipeline would be constructed with sufficient capacity so that it could operate as a common carrier providing transportation for future production from neighboring prospective oil fields to Pump Station No. 1.

°The pipeline would be established as a separate entity. Financing of pipeline construction, estimated at approximately \$300 million, would be undertaken at the same time as the financing for the Northstar/Seal Island Project production facilities, but would be treated as an entirely separate, independently based financing package. The State of Alaska would bear no credit risk or take on any obligation with respect to this financing.

°Amerada Hess would be the owner of the pipeline prior to payout of development costs for the Northstar/Seal Island Project. Amerada Hess would agree to contribute the pipeline to the State of Alaska at the time payout was achieved, and would enter into an agreement to operate the pipeline after its contribution to the State of Alaska.

Page 4
Governor Cowper
July 10, 1987

*Tariffs would be established, applicable to all users including the Northstar/Seal Island Project and future field developments. These tariffs would provide a reasonable profit to the State after providing for the costs of pipeline operation and maintenance.

Our proposal to contribute the Northstar subsea pipeline to the State of Alaska is intended to provide a bonus to the State once payout of the Northstar/Seal Island Project is accomplished. The direct and immediate benefit would be through the tariffs received by the State. Long term, the existence of the pipeline would offer and be available as an economic incentive for the development of other nearby blocks, both Federal and State, whose development might otherwise be uneconomic without the benefit of existing, nearby Alaska State pipeline transportation to Pump Station No. 1.

This part of our legislative proposal obviously requires a good deal of further definition, but whatever its final form our sole aim and objective would be to provide an ongoing economic benefit to Alaska through the permanent contribution of the pipeline and its revenues to the State. I want to stress to you that we are not looking to involve in any way the credit of the State in the financing of the Northstar/Seal Island Project or the subsea pipeline. Contribution of the pipeline to the State would occur only after all Northstar/Seal Island Project debt and subsea pipeline debt was fully repaid.

Our Northstar leases have 1990 expiration dates. Amerada Hess has already expended over \$80 million on exploration at Northstar. Amerada Hess must act now in the 1987-88 winter season to do the additional drilling required to delineate the Northstar Prospect's crude oil reserves. Amerada Hess will spend \$40 to \$50 million on this delineation drilling program.

We need your Administration's cooperation in expediting the permitting process for this drilling activity. However, if after completion of our company's delineation drilling program, legislative relief along the lines proposed is not initiated and successfully implemented, our company would be much better off if the permits were never issued.

Amerada Hess believes that the crude oil reserves at Northstar are a substantial asset of the State of Alaska that should be developed. The long term benefits of bringing the field into production should not be lost by a failure of the State of Alaska to provide the short term relief from royalty and severance taxes required for the project to proceed.

AGO 1340179

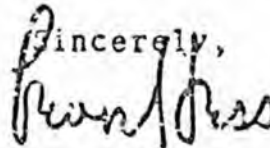
NOTICE

RESPONSE LETTER

Page 5
Governor Cowper
July 10, 1987

Unless you are convinced a world crude oil price of \$35 a barrel is around the corner, a legislative initiative along the lines we have proposed is essential, the crucial ingredient being a sufficient economic incentive to permit the Northstar/Seal Island Project to pay out. Without payout at a reasonable date the project cannot be financed and will not be undertaken. The State of Alaska will not have the benefit of the jobs and future revenues from royalties, severance taxes and net profits accruing to it after payout of a successful oil field.

We hope, after completion of our delineation wells, the results will be encouraging, and that you will then agree to sponsor the initiatives required to bring this important project to production. We stand ready to work with your Administration in formulating a plan which you can endorse.

Sincerely,


Leon Hess

jf



STATE OF ALASKA
OFFICE OF THE GOVERNOR
JUNEAU

August 11, 1987

Mr. Leon Hess
Chairman of the Board
Amerada Hess Corporation
1185 Avenue of the Americas
New York, NY 10036

Dear Leon,

My staff is in the process of evaluating the proposal which you sent to me recently. I expect to get back to you as soon as we've discussed the matter in depth. Except for a few selected Commissioners and staffers, this proposal is confidential.

I hope you're having a good summer, and that the Jets are getting into shape.

Sincerely,

A handwritten signature in cursive script, appearing to read "Steve Cowper".

Steve Cowper
Governor

cc: Ron Birch, Washington, DC

NOTICE

Applied Drilling Technology Inc.

10777 Westheimer, Suite 700 • P.O. Box 4509

Houston, Texas 77210 • (713) 266-4001

August 19, 1987



Thomas E. Short
President

Mr. P. A. Dysert
Amerada Hess Corporation
1185 Avenue of the Americas
New York, New York 10036

Re: Glomar Beaufort Sea I
Turnkey Drilling Contract
Dated 10 July 1987

Gentlemen:

Since we have been unable to reach agreement as to the date by which Applied Drilling Technology Inc. ("ADTI") shall commence deballasting operations of the Glomar Beaufort Sea I for purposes of mobilizing the drilling unit to your drilling location, we hereby respectfully give notice pursuant to Section 4.9 of the above subject Contract that the last practical date for commencement of such deballasting operations, taking into consideration weather conditions and availability of suitable tugs, is 30 August 1987. May we please have your concurrence to proceed with such mobilization.

Your cooperation in this regard is greatly appreciated.

Respectfully,

T. E. Short
President

TES/RNP/kec

c: Mr. C. R. Richard
Amerada Hess Corporation
P. O. Box 2040
Tulsa, Oklahoma 74102

We Concur:

Amerada Hess Corporation

By: _____

AGO 1340182

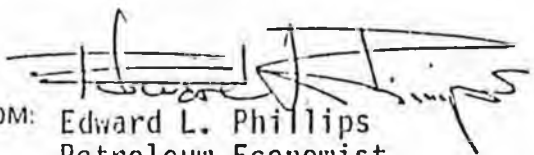
MEMORANDUM
DEPARTMENT OF NATURAL RESOURCES

State of Alaska
DIVISION OF OIL AND GAS

TO: James E. Eason
Director

DATE: January 8, 1988

FILE NO:


FROM: Edward L. Phillips
Petroleum Economist

TELEPHONE NO: 762-2589

SUBJECT:

One point overlooked in the Amerada Hess discussion is the "savings" already transferred to Amerada Hess by the state as a result of the net profit bidding system employed in Sale 30. At the date of the sale (12/12/79), price expectations were extremely bullish. The Iraq/Iran war had been underway for a few weeks and spot oil prices, reflecting the uncertain outlook of the war, were in the \$35.00 to \$40.00 a barrel range. Market contract prices were moving up, and many price forecasters saw no end in sight. For example, the March 1980 Department of Revenue forecast projected the price of Saudi Marker Crude at \$46.43 in 1985, \$57.91 in 1990, and \$143.17 in 1996 (a perfect example of the power of compounding). Parenthetically, yesterday's (7 January 88) Saudi spot price was \$16.40. Markets have little tolerance for the compounding process. This forecast was not, by any means, off the wall--but represented a "middle of the pack" estimate.

The petroleum potential of the Beaufort Sea looked extremely attractive (profitable) with the price expectations of the period. Against this background, the winning bidders at Seal Island paid a total of \$19.2 million in bonus payments for the state tracts overlying the prospects. Amerada Hess paid \$6.9 million for its two tracts. In addition, the net profit share (NPS) bids ranged from 85.26% to 93.2%.

At that time, our analysis indicated that the same tracts, if sold on a bonus bid basis with a 20% royalty, were worth an estimated \$333 million, and possibly much more. The state/federal price assumptions used for the presale analysis were relatively conservative.

One could argue that the NPS bidding system permitted "savings" to the winning bidders of approximately \$314 million. Specifically, Amerada Hess paid \$6.9 million for tracts the state estimated to be worth about \$120 million. Thus, NPS bidding saved Amerada Hess over \$113 million, and possibly much more. In fact, it is not clear that Amerada Hess possessed the financial resources to win the tracts under a conventional leasing system. The major North Slope operators (ARCO, Sohio, Exxon) had deeper pockets, and were clearly better positioned to bid higher cash bonuses had the cash bonus been the bidding variable for the state tracts, as it was for the adjacent federal tracts overlying the Seal Island structures.

As a conceptual exercise, one can compute the true savings to Amerada Hess by looking at what the \$113 million could have earned them over the eight year time period since the sale. At a 10% rate of return (ROR), Amerada Hess would have earned almost \$129 million since the sale. If their ROR was 15%, their earnings would approach \$233 million.

James E. Eason
January 8, 1988
Page 2

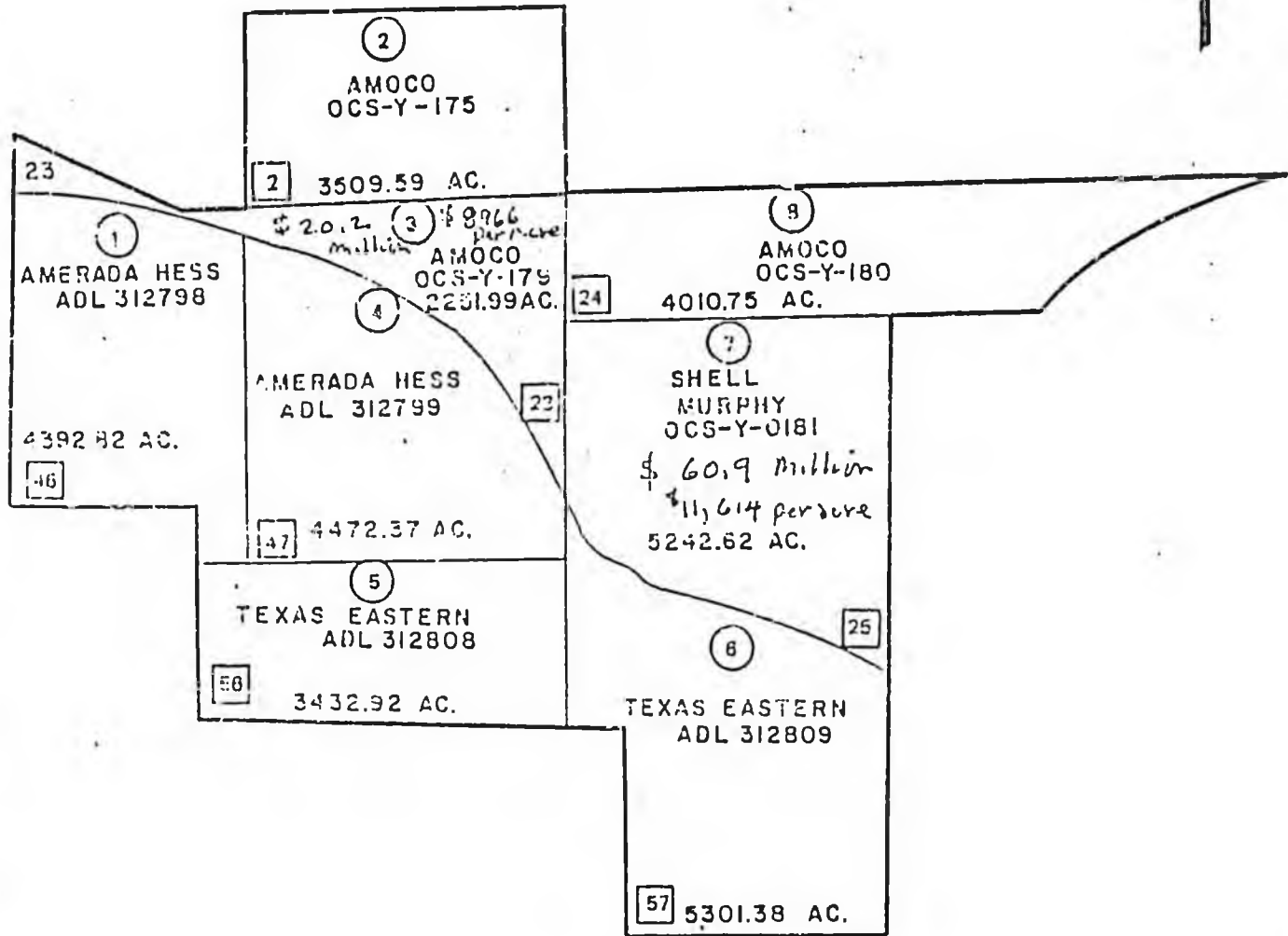
Thus, to this point in time the major sacrifice has been by the state in foregone bonuses and Permanent Fund contributions, including potential interest earnings. The Permanent Fund share of the estimated foregone bonuses would be \$78.5 million. This amount would have accrued to \$219.53 million by January of this year.

The current proposal appears to extend the state's sacrifice to a "foregone" conclusion.

Attachment

!269E

State Leases Bonus Bid = \$875.00 per acre
 Federal Leases Bonus Bid = \$10,808 per Acre
 Fed Royalty 16 $\frac{2}{3}$ % + Sliding Scale Royalty to
 Max of 65%



LEGEND
 UNIT OUTLINE ———
 LEASE BOUNDARY ———
 UNIT TRACT NO. (1)
 LEASE SALE BF (2)
 TRACT NO. (16)

NO SCALE

EXHIBIT B
 SEAL UNIT
 BEAUFORT SEA, ALASKA

MEMORANDUM

State of Alaska

DEPARTMENT OF NATURAL RESOURCES
DIVISION OF OIL AND GAS

TO: James E. Eason
Director

DATE: February 19, 1988

FILE NO:

TELEPHONE NO: 762-2589

FROM: Ed Phillips
Petroleum Economist

SUBJECT:

HB 471 introduced by Representative Gruenberg appears to be a clone of an earlier proposal offered to the state by Leon Hless for royalty and tax relief at Seal Island. HB 471 would generalize the applicability of royalty and tax relief to other North Slope "reserves" particularly Pt. Thomson and West Sak. In an earlier memo the Hless Proposal and its cost in barrels of oil for the Seal Island prospect only was specifically analyzed. With minor changes that analysis is produced below. The issues raised in the analysis are still valid. The fiscal cost of applying the proposed statute could be substantial and the gains possibly chimerical.

As is often the case, the potential "costs" of the proposal are more easily discernible than the potential benefits. The potential "costs" of the proposal are the foregone royalties and taxes. These would amount to about 25 to 30% of the gross production for the period before capital recovery or December 31, 1999, whichever is less. These revenues would be forgiven during the peak production phase of the typical field. The potential benefits result from transforming fields from submarginal status to profitable. This transformation in itself does not assure that benefits equal or exceed costs. In some cases, the forgiveness may only shift forward by a year or two a particular field's development. In this case it's hard to argue the wisdom of the forgiveness. In other cases the forward shifting of development and production may be much more dramatic. Until we have more evidence of which phenomenon is more likely it will be exceedingly difficult to assess the potential benefits of this proposed legislation.

Assumptions

1. Recoverable reserves at North Star/Seal Island are estimated to be 350 million barrels. State leases have an estimated 80% of recoverable reserves. The remaining reserves are on federal leases.
2. Project must earn after tax 10% real rate of return to be feasible.
3. All state leases have 20% royalty rate.
4. Peak production at 100,000 barrels a day through first four years, then production declines at 15% per year. Total field life is 16 years.
5. Time value of production is evaluated at three interest rates, 5%, 10% and 15%.
6. Price assumed to be constant so that analysis is done in terms of barrels of oil. This is the index number for measuring costs.

Methodology

1. Compute the present value of production as of time zero. Then lag time zero for various delays that apply discount factors to the delays. The present value is stated in terms of "discounted" barrels. For example, the present value of 350 million barrels of oil produced over a sixteen year period at 5% discount equals approximately 217 million barrels of oil as a present value equivalent. At 10% this value drops to 192 million barrels, and at 15% 171 million barrels. (The method used for these calculations is readily found in Newendorp, Paul D. "Decision Analysis for Petroleum Exploration," Petroleum Publishing Company, Tulsa, Oklahoma, 1974, Appendix I, pp: 651-659.)
2. Payback (recovery of invested capital) was estimated by two methods. First, the "Rule of 72" was used. This "rule" allows one to estimate payback by dividing the rate of return into the number 72. For example, if a particular investment earns 10% per year, it will payback in approximately 7.2 years. The "Rule of 72" is a quick and dirty way to compute doubling times for compound interest rates. The other method used was to divide the rate of return into 100. This works reasonably well for uniform cash flows. (This method is illustrated in Megill, Robert E., "Exploration Economics," Petroleum Publishing Co., Tulsa, Oklahoma, 2nd Ed., 1979, pp. 85-84.) Finally, doubling times for compound interest were computed directly. These techniques will yield estimates of undiscounted payback on original investment, thus they represent minimal estimates of payback periods. Capital recovery calculations permit payback with imputed interest and represent a maximum estimate of payback.

This analysis does not forecast a rate of return for Seal Island. It only examines the conditional statement that if Seal Island earns X rate of return, then payback will take approximately Y years. This proposition is evaluated for 10 and 15 percent rates of return (ROR). This methodology can be used for any ROR.

3. "Cost" to the state is measured in terms of undiscounted oil as well as the present value of royalty barrels foregone during payback period under the North Star (Seal Island) proposal. This simple methodology can easily be extended to include severance taxes. The inclusion of these taxes adds about 50% to the annual cost estimates, but shortens the payback period. Another potential "cost" to the state is from the delay in development and production at Seal Island due to submarginal economics attributable to state's royalty and severance taxes. This delay cost is measured for 5, 10, 15 and 20 year delays, at 0, 5, 10 and 15% discount rates.
4. Caveat: This methodology is admittedly crude, but very little data are available to justify a more sophisticated, yet questionably more accurate approach. This approach will, at least, frame the discussion in more analytical terms.

Results

1. Given an assumed 350 million barrels of recoverable reserves, the state's 20% royalty share would be 56 million barrels of undiscounted oil. (This total could be as high as 84 million barrels with the inclusion of the severance tax.) In discounted barrels this claim drops to 34.6 million barrels at 5%, 30.7 million at 10% and 27.4 million at 15% if the field could start producing as of today.

Table I
Present Value Barrels
Royalty Share

Discount Rates	Delay Times				
	0 Years (millions of BBls)	5 Years (millions of BBls)	10 Years (millions of BBls)	15 Years (millions of BBls)	20 Years (millions of BBls)
0	56	56	56	56	56
5	34.6	27.1	21.2	16.7	13.1
10	30.7	19.1	11.8	7.4	4.6
15	27.4	13.6	6.8	3.4	1.7

2. The reality of Seal Island economics and construction schedules vitiate columns one and two as possibilities. The maximum gain to the state if the delay is reduced by 10 years, is equivalent to 8.1 million royalty barrels of oil (Column 3 minus Column 5 at a 5% discount rate). At discount rates of 10 and 15 percent the gain associated with expedited development is less.
3. What is the royalty "cost" to the state of waiting until payback in order to capture this "gain"? The cost depends upon the rate of return on investment. If the rate of return is 10%, simple payback can take from 7.2 years by the "Rule of 72" or 11.5 years if operators are allowed a 10% rate of return on their investment before payback is complete. This would imply a minimum of 76% of recoverable reserves or about 16.1 million present value royalty barrels (42 million actual barrels) would be produced at no royalty value to the state. The maximum estimate would be about 17.4 million royalty barrels (46 million actual barrels). This means that about 82% of the field's recoverable reserves would be produced before the state would begin to receive its royalty share. The "actual" barrel estimates were derived from the field's estimated production profile as stated in Assumption 4.

At higher rates of return, simple (interest free) payback is less onerous. Payback can be achieved in five years if the project earns 15%. With this ROR payback even with imputed interest of 10% is achieved in about eight years. The cost is between 12.5 to 15.6 million present value royalty barrels (28.6 million to 41 million actual barrels).

Including a severance tax forgiveness does not change the actual barrel sacrifice by the state, but it does increase the present value barrel cost. This result follows directly from the greater "upfront" sacrifice by the state at peak production rates. The implied gain is faster payback, hence earlier reimposition of the royalty and severance tax.

Thus, for the present value equivalent of approximately 16 to 17 million barrels, (42 to 46 million actual barrels) one could argue that production would be hastened by 10 years. But that would be giving the operator benefit of all of the best assumptions. What if, in reality, the state was only purchasing a year or two in expedited development? The cost is still the same, but the benefits decline considerably. Whereas costs were only double the benefits where production was hastened by 10 years (16 million cost, 8 million benefits), the benefits approach zero as the delay difference declines. Suppose allowing payback only reduced delay by 5 years from 15 to 10 years, then the gain is only 4.5 million present value bbls at most. (Column 3 minus Column 4.) If production was only affected by one year, the benefit is reduced to 1 million barrels. The cost is still 16 million barrels.

Some caveats are important. The preliminary results outlined here may be sensitive to assumptions about field size and decline rates. Given economics of scale and concomitant longer, peak production periods, it is likely that payback would occur earlier for a significantly larger field. (This effect would follow from a higher ROR associated with the larger field.) A rapid real increase in oil prices would also change this result by increasing the ROR. The relationship between the ROR and payback would not change.

Conclusion

1. For a minimum royalty oil cost of 28.6 to 46 million barrels the state may get something.
2. Unless real oil prices substantially increase, the state will receive no royalty payments from the proposed development in this century.

MEMORANDUM

State of Alaska

TO: Jim Eason
Director

DATE: February 26, 1988

FILE NO:

TELEPHONE NO: (907) 762-2546

FROM: Mike Kotowski *MOK*
Petroleum Engineer

SUBJECT: Potential Hydrocarbon
Areas Subject
to HB 471

The following are areas of the state where hydrocarbon discoveries have been made, but have not produced in commercial quantities to date. These are known areas that have the potential of being subject to the criteria set forth in HB 471, Fifteenth Legislature - Second Session.

<u>Area</u>	<u>Estimated Recoverable Hydrocarbons (Millions of Barrels)</u>	<u>Royalty Interest</u>
Seal Island/North Star	300	20% with Net Profit Share
Cwydyr Bay	10	12.5%
Hiakuk	57	12.5%
Point Thomson	350 (oil and gas condensate)	12.5%
West Sak Sands	3000	12.5%
Colville Delta	Unknown	12.5%

It should be noted that under a strict interpretation of parts of HB 471 Sec. 3., two areas, the West Sak Sands and Point Thomson, may not qualify for the proposed royalty and severance tax relief. HB 471 Sec. 3. states in part

" (cc) Upon application by a lessee of a lease covered by this section, the commissioner shall temporarily waive the royalty requirement of a lease, if the lessee demonstrates that

(2) commercial production from the lease has not yet begun;

(4) exploration of the lease has delineated oil reserves."

Some of the Kuparuk River Unit leases are producing commercially from the Kuparuk formation. As these leases are also underlain by the West Sak Sands and the West Sak is not presently in commercial production, would the future royalty production from the West Sak on these leases be waived by this bill?

Jim Eason
Page 2

Also, item (4) specifically addresses delineated oil reserves. The present central area development plans for the Point Thomson Unit call for possible gas cycling that permits gas liquid production prior to major gas sales. Does the specific reference to delineated oil reserves in this section of the bill preclude the gas cycling with gas liquid production development option? In other words, would leases with gas and gas liquid production qualify for HB 471 relief?

Finally, under the most liberal interpretation of the criteria in Sec. 3., up to 487 million barrels of royalty hydrocarbons would be waived by HB 471.

3511A

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December 10, 1987

The Honorable Steve Cowper
Governor of the State of Alaska
P.O. Box A
Juneau, Alaska 99811-0101

VIA FEDERAL EXPRESS

Dear Governor Cowper:

At your request, and on behalf of Amerada Hess, I am pleased to forward draft legislation that would give your administration the power to encourage development of Alaska's smaller, offshore oil fields. Without that relief, development of these fields will be uneconomic, and will not occur.

It is conservative legislation. Many other oil producing jurisdictions have encouraged new oil development by forgiving royalties and severance taxes without regard to project economics and for the life of the field. The enclosed bill takes a more cautious approach, designed to foster development where it would not otherwise occur. Under the bill, if a company purchased its leases prior to January 1, 1986 -- in other words, at a time of radically different oil price expectations -- and the company can demonstrate that it cannot develop its field under current economic conditions, it can receive royalty and production tax relief, but only until recovery of initial development costs. Once those costs are recovered, the relief automatically ends, and the state will have in return: (1) a revenue-producing field that would not otherwise have been developed; (2) a net profit share of production, if the lease is not already a net profit share lease; (3) particularized local hire requirements developed on a constitutionally-defensible case-by-case basis by the Commissioner of Labor; and (4) if it desires, ownership of any affiliated common carrier pipeline.

Relief is available only to those oil fields where the costs of development are so high in relation to foreseeable production revenues as to make development uneconomic. As you have recognized, these are Alaska's smaller offshore fields that face

The Honorable Steve Cowper
December 10, 1987
Page 2

particular hurdles such as distance from existing pipeline transportation, relatively deep water, sea ice, seasonal drilling restrictions, and high construction and operating costs. However, those constraints make a field uneconomic only if their associated costs exceed likely field production revenues. There is no fixed formula to determine what level of reserves will overcome any particular mix of cost impediments. By defining "uneconomic" fields as ones where development costs exceed production revenues, the bill necessarily takes account of all the engineering and operational difficulties that make development of small offshore fields so uniquely difficult.

The bill has been carefully tailored to limit relief to those instances where it is necessary and appropriate. Three particular aspects of the bill guarantee its limited scope:

(1) After relief is granted, your commissioners of Revenue and Natural Resources will keep a close watch on field revenues. Once the company has realized revenue sufficient to pay for development costs, they will terminate the relief. In this way, the state is assured that the moment a company begins to realize any profit from its investment, the company will have to pay royalty and production tax at the normal rate;

(2) The company must meet four distinct requirements to obtain any relief: One, relief is available only to those who bought their leases before the unanticipated collapse of oil prices in 1986; Two, the company must have explored its properties and delineated reserves; Three, relief is available only for fields that have never had commercial production; and Four, most fundamentally, the company must meet its burden of showing that unless relief is granted, it cannot recover its development costs in a commercially reasonable time; and

(3) Companies can apply for relief only during the next six years. The bill is thus an emergency measure, intended only to provide an immediate, short-term stimulus to Alaska's moribund economy and not to signal a permanent shift in Alaska's leasing policy. For this reason, the immediate economic benefit of this legislation to the State of Alaska will be substantial. Under the bill, a company must delineate its reserves before application is made. Lessees will thus have a strong incentive to accelerate their exploration plans in order to meet the application deadline.

The Honorable Steve Cowper
December 10, 1987
Page 3

As you and your staff know, other states, and oil producing countries, have recognized the need to adjust royalties and severance taxes in order to stimulate new investment and employment. In 1983, for example, the United Kingdom acted swiftly in response to a downturn in new oil development. That year, Parliament provided that:

(1) Any new field north of the Southern Gas Basin approved for development after April 1, 1982 would be excused from the government's 12 1/2 percent royalty over the life of the field; and

(2) To encourage small field development, 20,000 barrels per day of production from all fields would be exempt from the petroleum revenue tax, up to a 75 million barrel field limit.

In the same vein, the province of Alberta has provided that any exploratory well drilled between November, 1986 and October, 1987 will be free of royalties for a period of five years, while wells drilled in the subsequent two years will enjoy three and one year royalty holidays, respectively. Alberta has also cut royalty rates across the board for existing production by 2-3 percent in order to improve companies' cash flow. At the same time, the federal government has instituted the Canadian Exploration and Development Incentive Program, which provides cash grants of up to \$2.5 million (U.S.) for new exploration and development.

Finally, a number of producing states have provided for severance tax exemptions of varying duration for new wells. In Louisiana, for example, new wildcat wells are exempt from the severance tax until 1990, while all new oil production in Montana is exempt for two years. Other exemption "windows" to encourage new or enhanced production have been enacted by Mississippi, North Dakota, Oklahoma and Wyoming.

I would like to touch on one other component of the legislation. The bill allows the state to acquire the lessee's related pipeline interest as a condition of granting relief. We previously offered this option believing that it would substantially increase our proposal's benefits to the state. Since then, members of your administration have voiced particular concern over this aspect. We continue to believe it would be of substantial benefit to the state to own this pipeline, not only in terms of tariff revenues, but also to encourage development of nearby, prospective fields. However, we do not want this

The Honorable Steve Cowper
December 10, 1987
Page 4

particular provision to in any way complicate the bill's progress or jeopardize your ability to support it. If you feel the provision would do either, we would concur that it be deleted.

I am confident that Amerada Hess can meet the strict standards of this legislation for the Northstar/Seal Island project. I also believe that your sponsorship and active support of this legislation will signal strong and positive commitment to Alaska's economic future and will receive overwhelming public support. It will help break the current economic logjam in Alaska oil development. It will clearly demonstrate that your administration is committed to taking the forceful steps necessary to turn Alaska's economy around.

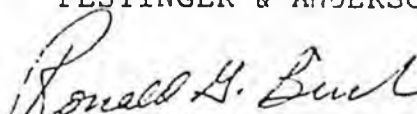
Legislation of this kind serves Alaska and the nation, and there should not be any opposition to it. It will advance development by at least a decade at the very time Alaska most needs that development.

Thank you for the interest you have shown on this issue. From this point, as we all have recognized, time is of the essence. Legislation removing the current barriers to Northstar/Seal Island development is critically important this session, and with one month remaining before the session convenes, we must find a sponsor who is anxious to make this bill a legislative priority. Your personal leadership in setting the agenda before Alaska's legislators return to Juneau would set this matter on the proper course.

With your permission, I will call next week, and I will be anxious to hear your reaction to our proposal.

Sincerely,

BIRCH, HORTON, BITTNER
PESTINGER & ANDERSON


Ronald G. Birch

RGB/kf
09RGB2
Enclosure

bcc copies:
John Tillinghast
Barclay Collins
John Katz

IN THE _____

By: _____

_____ BILL NO. _____

IN THE LEGISLATURE OF THE STATE OF ALASKA
FIFTEENTH LEGISLATURE -- SECOND SESSION
A BILL

For an Act entitled:

"An Act allowing the development of otherwise uneconomic state oil and gas leases not in commercial production by authorizing temporary changes in royalty and production tax rates prior to recovery of development costs, and providing for an effective date."

Sec. 1. The legislature finds and declares that:

(1) Since 1985, world oil prices have dropped precipitously;

(2) The sharp decline in world oil prices has had a dramatic effect on new oil and gas exploration and development in Alaska. In 1987, three exploratory wells were drilled in the state, compared to 22 in 1985;

(3) Future oil and gas development in Alaska is dependent upon the productivity of smaller fields in the state. Many smaller fields lie in remote offshore areas of the state, and face severe and unique constraints including distance from pipelines and supply systems, sea ice, seasonal drilling restrictions and high construction and operation costs. Under current economic conditions, these fields will not recoup the costs of development, and therefore will not be developed absent encouragement from the state; and

(4) Because of the long lead time necessary to bring remote fields into commercial production, and because of the severity of Alaska's current economic difficulties, it is in the public interest to encourage the immediate development of these fields.

Sec. 2. AS 38.05.180 is amended by adding new subsections to read:

(cc) Upon application of a lessee, the commissioner shall temporarily waive the royalty requirement of the lease, if the lessee demonstrates that:

(1) the lease was issued prior to January 1, 1986;

(2) commercial production from the lease has not yet commenced;

(3) projected production revenues from the lease would be insufficient to permit recovery of projected initial development costs within 10 years of commencement of commercial production, or any lesser period that may be commercially reasonable under the circumstances; and

(4) exploration of the lease has delineated oil reserves

(dd) An application under (cc) at this section must be filed with the commissioner by July 1, 1994. The lessee must pay the cost of processing the application.

(ee) A royalty change granted under (cc) of this section expires when the commissioner certifies that production revenues have been received sufficient to recover initial development costs. If the lease is a net profit share lease, certification under this subsection may not precede the first credit balance in the lessee's development account.

(ff) The commissioner may attach the following conditions to any royalty change granted under (cc) of this section:

(1) If the lease is not a net profit share lease, the commissioner may require a net profit share to the state upon recovery of initial development costs;

(2) The commissioner may require that the lessee employ qualified and available Alaskans on activities on or directly supporting development of and production from the lease. A condition imposed under this paragraph shall be developed by the commissioner on a case-by-case basis, in consultation with the commissioner of the Department of Labor, after considering the economy and employment patterns of the affected area, and the degree to which non-residents may cause unemployment or underemployment among qualified and available Alaska residents in the absence of the condition;

(3) If the lessee, or an affiliate of the lessee, intends to construct a pipeline to transport oil or gas from the point of production, the commissioner may require conveyance to the state of the lessee's or affiliate's interest in the pipeline upon recovery of initial development costs from the lease. The commissioner may further require that the lessee or affiliate:

(A) operate the pipeline as a common carrier; and

(B) finance construction of the pipeline in a manner that will allow subsequent conveyance to the state free of any debt obligation to the state.

(4) The commissioner may impose reasonable reporting requirements for the purpose of certifying recovery of initial development costs under (ee) of this section.

(gg) The commissioner may not attach any condition under (ff) of this section that would deny the lessee a commercially reasonable rate of return from the lease after recovery of initial development costs.

(hh) If a lessee files an application under AS 43.55.018 within 60 days before or after filing an application under (cc) of this section, the commissioner and the commissioner of the Department of Revenue shall hear and decide the applications jointly.

(ii) Any person aggrieved by a decision of the commissioner under (cc) of this section may appeal that decision only by filing a notice of appeal with the Superior Court under AS 44.62.560 within 30 days of the decision, and this requirement is jurisdictional. Any appeal under this subsection shall be heard as an appeal based upon the record compiled by the department and, to the extent consistent with the rules of the Alaska Supreme Court, the appeal shall be expedited.

(jj) As used in subsections (cc)-(ii) of this section:

(1) "projected initial development costs" include all expenses projected to accrue from issuance of the lease to the commencement of commercial production in support or as a result of lease development, together with interest on those costs from the date of accrual equal to: (A) the rate of interest allowed on the company's development account in the case of net profit share leases; and (B) for all other leases, the then-prevailing commercial rate for projects of like risk and magnitude, but in either case not less than the then-prevailing prime rate plus two percent. If the lease is a net profit share lease, the term includes any expenditure includable as a debit in the lessee's development account;

(2) "projected production revenues" must be determined based upon the Department of Revenue's then-current 30 percent case price projections at the point of production, less:

(A) projected direct operating costs;

(B) the projected federal windfall profits tax;

(C) projected subsequent development costs on an accrual basis; and

(D) the projected royalty that would be due on the lease, and the projected production tax that would be due under AS 43.55, absent a change in either obligation under subsection (cc) of this section or AS 43.55.018; and

(3) "projected subsequent development costs" means all development costs that are accrued after commencement of commercial production.

Sec. 3. AS 43.55 is amended by adding a new section to read:

Sec. 43.55.018. TEMPORARY PRODUCTION TAX CHANGE. (a) Upon application of an owner of a lease or property, the commissioner shall temporarily waive the production tax for the lease or property if the applicant demonstrates that:

(1) the lease or property was conveyed by, or derived in chain of title from, a lease issued by the Commissioner of the Department of Natural Resources under AS 38.05.180 prior to January 1, 1986;

(2) commercial production from the lease or property has not yet commenced;

(3) projected production revenues from the lease or property would be insufficient to permit recovery of projected initial development costs within 10 years of commencement of commercial production, or any lesser period that may be commercially reasonable under the circumstances; and

(4) the commissioner of the Department of Natural Resources has certified that exploration of the lease has delineated oil reserves.

(b) An application under (a) of this section must be filed with the commissioner by July 1, 1994. The taxpayer must pay the cost of processing the application.

(c) A rate change granted under (a) of this section expires when the commissioner certifies that production revenues have been received sufficient to recover initial development costs. If the lease is a net profit share lease, certification under this subsection may not precede the first credit balance in the lessee's development account.

(d) The commissioner may attach the following conditions to any rate change granted under (a) of this section:

(1) If the lease or property is not a net profit share lease, the commissioner may require conveyance to the commissioner of the Department of Natural Resources of a net profit share to the state upon recovery of initial development costs;

(2) The commissioner may require that the applicant employ qualified and available Alaskans on activities on or directly supporting development of and production from the lease or property. A condition imposed under this paragraph shall be developed by the commissioner on a case-by-case basis, in consultation with the commissioner of the Department of Labor, after considering the economy and employment patterns of the affected area, and the degree to which non-residents may cause unemployment or underemployment among qualified and available Alaska residents in the absence of the condition;

(3) If the applicant, or an affiliate of the applicant, intends to construct a pipeline to transport oil or

gas from the point of production, the commissioner may require conveyance to the commissioner of the Department of Natural Resources of the applicant's or affiliate's interest in the pipeline upon recovery of initial development costs from the lease or property. The commissioner may further require that the applicant or affiliate:

(A) operate the pipeline as a common carrier; and

(B) finance construction of the pipeline in a manner that will allow subsequent conveyance to the state free of any debt obligation to the state; and

(4) The commissioner may impose reasonable reporting requirements for the purpose of certifying recovery of initial development costs under (b) of this section.

(e) The commissioner may not attach any condition under (d) of this section that would deny the applicant a commercially reasonable rate of return from the lease or property after recovery of initial development costs.

(f) If an applicant files an application under AS 38.05.180(cc) within 60 days before or after filing an application under (a) of this section, the commissioner and the commissioner of the Department of Natural Resources shall hear and decide the applications jointly.

(g) Any person aggrieved by a decision of the commissioner under (a) of this section may appeal that decision only by filing a notice of appeal with the Superior Court under AS 44.62.560 within 30 days of the decision, and this requirement is jurisdictional. Any appeal under this subsection shall be heard as an appeal based upon the record compiled by the department and, to the extent consistent with the rules of the Alaska Supreme Court, the appeal shall be expedited.

(h) As used in subsections (a)-(g) of this section:

(1) "projected initial development costs" includes all expenses projected to accrue from issuance of the lease to commencement of commercial production in support or as a result of lease development, together with interest on those costs from the date of accrual equal to: (A) the rate of interest allowed on the company's development account in the case of net profit share leases; and (B) for all other leases, the then-prevailing commercial rate for projects of like risk and magnitude, but in either case not less than the then-prevailing prime rate plus two percent. If the lease or property is a net profit share lease, the term includes any expenditure includable as a debit in the lessee's development account;

(2) "projected production revenues" must be determined based upon the department's then-current 30 percent case price projections at the point of production, less:

(A) projected direct operating costs;

(B) the projected federal windfall profits tax;

(C) projected subsequent development costs on an accrual basis; and

(D) the projected royalty that would be due on the lease or property, and the projected production tax that would be due under AS 43.55, absent a change in either obligation under subsection (a) of this section or AS 38.05.180 (cc); and

(3) "projected subsequent development costs" means all development costs that are accrued after commencement of commercial production.

Sec. 4. AS 38.05.180(j) is amended to read:

(j) To prolong the economic life of an oil and gas field, the commissioner shall adopt regulations for all bidding methods to allow reduction of royalty on leases within the field to compensate for increasing costs in the later stages of production decline. Except as provided in subsection (cc) of this section, [T]the commissioner may not grant a reduction of royalty until two years' initial production from the field has occurred and each lessee requesting the reduction has made a clear showing that the revenue from all hydrocarbons produced from the field is insufficient to produce a reasonable rate of return with respect to that lessee's total investment in the field.

Sec. 5. AS 43.55.011(a) is amended to read:

Sec. 43.55.011. OIL PRODUCTION TAX. (a) There is levied upon the producer of oil a tax for all oil produced from each lease or property in the state, less any oil the ownership or right to which is exempt from taxation. Except as provided in AS 43.55.018, [T]the tax is equal to either the percentage-of-the value amount calculated under (b) of this section or the cents-per-barrel amount calculated under (c) of this section, whichever is greater, multiplied by the economic limit factor determined for the oil production of the lease or property under AS 43.55.013. If the amounts calculated under (b) of (c) of this section are equal, the amount calculated under (b) of this section shall be treated as if it were the greater for purposes of this section.

Sec. 6. AS 43.55.015(a) is amended to read:

Sec. 43.55.016. GAS PRODUCTION TAX. (a) There is levied upon the producer of gas a tax for all gas produced from each lease or property in the state, less any gas the ownership or right to which is exempt from taxation. Except as provided in AS 43.55.018, [T]he tax is equal to either the percentage-of-value amount calculated under (b) of this section or the cents-per-Mcf amount calculated under (c) of this section, whichever is greater, multiplied by the economic limit factor determined for gas production of the lease or property under AS 43.55.013. If the amounts calculated under (b) and (c) of this section are equal, the amount calculated under (b) of this section shall be treated as if it were the greater for purposes of this section.

Sec. 7. This Act takes effect immediately in accordance with AS 01.10.070(c).

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TO: Ned Farquhar (Rep. Sam Cotten's Office)

FR: Cindy Bailey

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Over the 2 and 1/2 year construction phase of Endicott, beginning in Spring of 1985, approximately 1020 men and women worked directly on the project here in Alaska mostly in construction. Using a conservative Department of Labor multiplier of 1.5, Endicott created about 2,250 jobs in Alaska.

A workforce of 300 will be required in 1993. Of these, 250 will be ongoing operating and training positions.

In 1993, 43% of the workforce will be in the oil and gas industry and operating positions.

The overall impact of the project on the local economy is expected to be significant. The project will provide a major source of income for the local community and will create a large number of jobs for the local population.

Endicott is a major project in the state of Alaska and will have a significant impact on the local economy.

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Northern Region Oil & Gas Employment 1980-1987
 SIC 13 Oil & Gas Extraction

	Jan	Feb	Mar	Apr	May	June	July	Aug	Sept	Oct	Nov	Dec	Annual Average
1980	2,609	2,593	2,665	2,697	2,707	2,686	2,397	2,348	2,406	3,353	3,361	3,520	2,779
1981	3,922	4,080	4,079	3,785	3,819	3,605	3,751	3,904	3,867	3,994	4,127	3,985	3,910
1982	3,993	3,869	3,760	3,778	3,663	3,523	3,727	3,578	3,454	3,186	3,166	3,185	3,574
1983	3,604	3,614	3,543	3,347	3,111	3,199	3,378	3,302	3,206	3,139	3,253	3,258	3,330
1984	3,541	3,564	3,713	3,704	3,662	3,523	3,806	3,660	3,731	3,504	3,416	3,440	3,605
1985	3,719	3,895	3,947	3,894	3,834	3,758	4,151	4,291	4,150	3,883	3,801	3,798	3,927
1986	4,307	4,413	4,297	3,623	3,527	3,585	4,048	4,253	4,236	4,328	4,181	3,840	4,053
1987	3,792	3,765	3,702	3,819	3,825	4,193	4,062	4,102	4,138	4,068	3,964	3,950	3,948

	1st Qtr	2nd Qtr	3rd Qtr	4th Qtr
1980	2,622	2,697	2,384	3,411
1981	4,027	3,736	3,841	4,035
1982	3,874	3,655	3,586	3,179
1983	3,587	3,219	3,295	3,217
1984	3,606	3,630	3,732	3,453
1985	3,854	3,829	4,197	3,827
1986	4,339	3,578	4,179	4,116
1987	3,753	3,946	4,101	3,994

State loss from ELF may double

By PATTI EPLER
Daily News reporter

A controversial oil tax program will cost the state about \$100 million more than first estimated, according to state petroleum economist Chuck Logsdon.

The Economic Limit Factor (ELF), designed as an incentive to encourage oil production as fields begin to decline, will cost the state about \$305 million in reduced severance taxes in fiscal years 1988 and 1989, about \$108 million more than state officials had figured on when they were factoring the tax reduction into the state revenue picture.

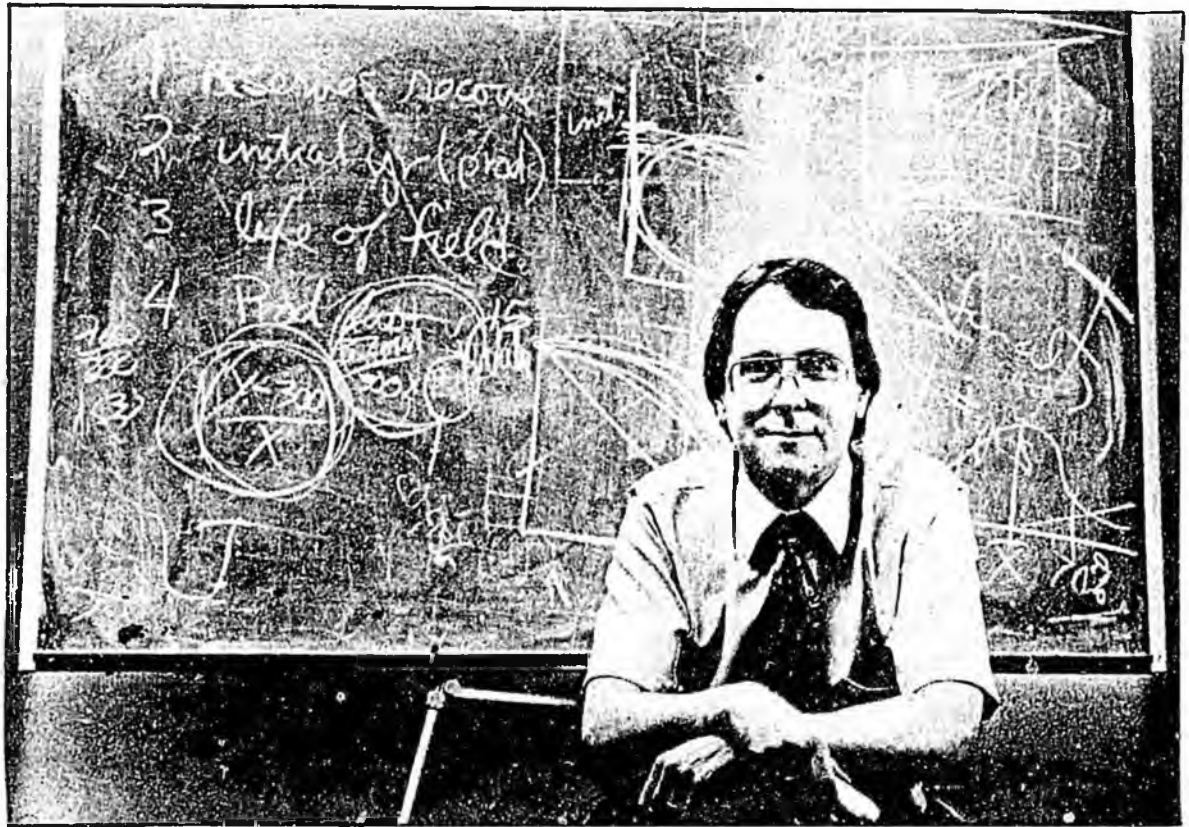
Logsdon said officials had underestimated the number of wells that North Slope producers planned to drill in those years.

Also, oil prices are higher than projected and production rates will be higher than expected, he said in a Feb. 19 memo to state Revenue Commissioner Hugh Malone.

However, state officials also have said that increased royalties to the state because of greater production in large part will offset bigger losses in severance tax revenue from a reduced ELF.

Since July, the ELF has been factored into tax computations on production from Prudhoe Bay, the largest oil field in North America and the source of most of the state's income.

The ELF is based on how much oil is produced from each well. Taxes drop as the number of barrels per well drop, which usually happens when a field declines.



Daily News file photo/Michael Penn

State oil price expert Chuck Logsdon

Logsdon said in the memo that "an aggressive drilling program such as that announced by the Prudhoe producers will keep production at the 1.54 million-barrel-per-day level but will do it with more wells than are currently required. For this reason, the severance tax rate will fall even though Prudhoe production will not."

Based on current assumptions about oil prices, production rates and number of wells for Prudhoe Bay, Logsdon said, his office now is projecting that the cost to the state of the ELF will be \$147 million in FY 1988 and \$158 million in 1989.

"These estimates are considerably higher than those made last spring when the legislature was considering ELF legislation," he wrote. "The reason is a combination of higher assumed prices, production in FY 1989, and a greater number of wells."

In June, petroleum economists had estimated the cost to the state to be \$101 million in FY 1988 and \$96 million in FY 1989.

Logsdon said in an interview his staff had underestimated the number of wells to be drilled by about 100. They also used lower oil

place



after rally
YORK — The market shed little ground Tuesday after a bounce trying to extend its recent rally. "The market is a time out," Alfred E. Loman, a senior analyst for Edwards & Kelcey Inc. in St. Louis, said. The Dow Jones average of industrial stocks on Monday slipped as the market's decline had risen more

ELF: State losses from tax program double

Continued from Page B-4

prices in their calculations, he said.

The memo to Malone updates the revenue projections, he said.

It was written partly because of recent announcements by North Slope producers of increased spending and drilling plans and

partly because there has been renewed interest by legislators in a House bill that would change the ELF tax program, he said.

"It became apparent we were going to have to explain to somebody a drop in our severance tax estimates for reasons other than our usual price drop," Logsdon said.

AHFC director to speak

Dr. Ron Lehr, executive director of the Alaska Housing Finance Corp., will be the guest speaker at a Thursday meeting

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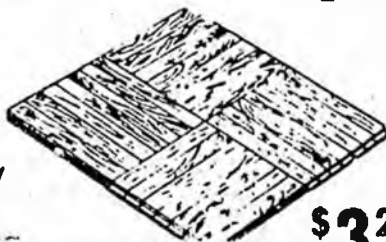


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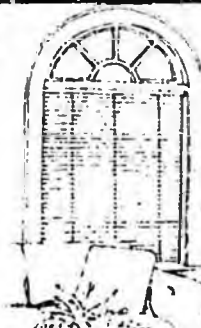
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9:00 - 11:30 AM

Bob Coe, President,

Duty Free Shoppers, Alaska Division

Bob Poe, Deputy Commissioner,

Department of Transportation, State of Alaska

Hugh Gellert, Director,

Division of Tourism, State of Alaska

Keith Fernandez, Marketing Director,

Anchorage Convention and Visitors Bureau

2/9/88

Sam -

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Ned



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January 18, 1988

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To: RDC's Oil and Gas Division
 From: Becky L. Gay
 Executive Director *Becky Gay*
 Re: Oil and gas incentives

The Resource Development Council's Executive Committee endorsed the following position on December 30, 1987. On behalf of RDC, I want to thank all of you that participated in the Division's activities that led to our support for this policy.

Incentives to be added:

- * **Discovery royalty incentives:** Draft legislation was prepared by RDC last year, but has not been introduced legislatively.
- * **Exploration incentive credits:** Exploration incentives should be added to all future state lease sales, especially to encourage drilling.
- * **Non-competitive leasing:** Certain tracts should be allowed to be filed for and awarded through this over-the-counter or lottery process as was done until 1978. This measure would encourage "grass-roots" interest in oil and gas issues, give opportunities to risk-takers and potentially create a positive, pervasive attitude change in the public favorable to development.
- * **Increase DNR's flexibility to add acreage to scheduled lease sales:** Contiguous or adjacent acreage, for which there has been a best interest finding made within the last three years, should be available for addition to programmed lease sales.

*AKISS
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Disincentives to be removed:

- * **Abolish DGC coordination of permitting:** Instead, institute lead agency permitting as introduced as SB280 and HB212 last year.
- * **Change the SEEA process:** Develop a legislative resolution and/or gain administrative consent to support lead resource agency supervision of the Social, Economic and Environmental Analysis (SEEA).
- * **Worker Compensation insurance premiums:** Support reform which can demonstrably reduce premiums in order to make Alaskans more competitive in labor markets.

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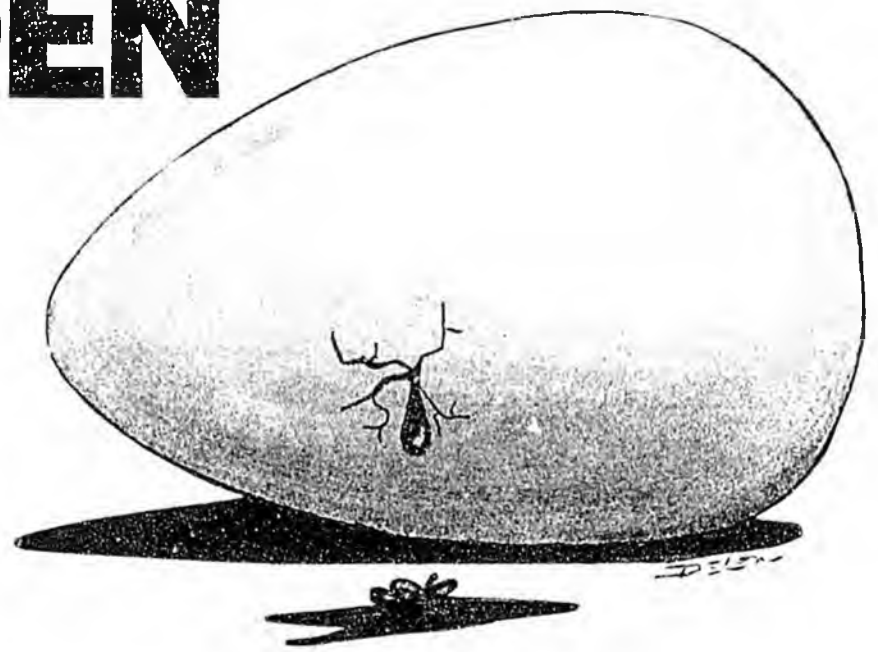
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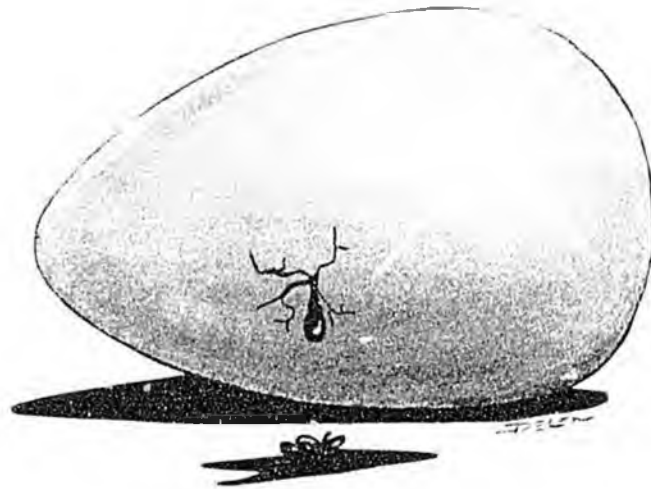
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'You Have To Feed The Goose That Lays The *Golden Egg*'

10 IDEAS FOR REJUVENATING ALASKA'S OIL INDUSTRY
REGARDLESS OF PRICES
AND MAXIMIZING ALASKA'S RETURN ON THE INVESTMENT

By Paul Laird

1

Continue and strengthen the state's oil and gas leasing program.

Most industry executives are satisfied with the current pace of oil and gas lease sales by the state, even though the number reportedly has slipped from the target of three sales a year to two because of manpower shortages in the leasing section of Alaska Department of Natural Resources' Division of Oil & Gas.

Once is not enough for parcels that don't

receive bids the first time around. Add them to future lease sales or try noncompetitive ("over-the-counter") leasing by making them available to anyone for a nominal, set fee.

Says Becky Gay, executive director of Resource Development Council for Alaska, "(Over-the-counter leasing) would give more Alaskans a stake in the process and generate additional interest in the program. At very least, it would promote more of a development attitude in the state."

2

Reinstate the discovery royalty bonus on state leases.

Designed to encourage exploratory drilling in frontier areas, the bonus reduced royalties on production from a discovery well in a new geologic structure. It was repealed in 1969 after the discovery of Prudhoe Bay.

The program reduced the normal 12½ percent royalty to 5 percent for 10 years, and it spawned additional development in areas around discovery wells.

A total of 10 discovery wells had been

approved for reduced royalties by late 1987, and Standard Alaska Production Co. has applied for the reduction on discovery wells at Endicott and Niakuk.

Says O.K. "Easy" Gilbreth, assistant executive director and manager of exploration and production affairs for the Alaska Oil & Gas Association, "I remember one time when 14 exploratory wells were being drilled at once in Cook Inlet; the different companies were in a race to make a discovery and eligible for the bonus. Some companies said the royalty bonus was the final incentive to drill."

3

Expand use of exploration incentive credits.

The commissioner of Natural Resources can credit a percentage of exploratory and geophysical expenditures toward companies' royalties, rents and taxes.

Companies can accelerate recovery of their investments and improve cash flow. Through October, more than \$36 million in credits had been granted on nine wells.

In the past, use of exploration incentive credits was limited to "net profit share leases"

in which companies bid a percentage of their profits from the tracts. Higher royalty rates (20 percent) were involved as well.

Kuparuk Uplands Sale 54 scheduled for January was the first time exploration incentive credits were offered on non-net profit share leases.

At a time when cash flow has slowed to a trickle for many oil companies, anything Alaska can do to improve it should enhance the state's competitive position for oil investments.

4

Develop a comprehensive state policy toward development incentives and offer additional exploration incentives.

Early last year, Amerada Hess Corp. Chairman Leon Hess flew into Juneau and proposed

this to Gov. Steve Cowper:

Amerada would develop its Northstar/Seal Island prospect in the Beaufort Sea and turn the pipeline linking it with existing North Slope pipeline infrastructure over to the state after project payback so the state could collect tariffs. In return, the state would have to suspend royalties and severance taxes on the project during the payoff period.

With state guidelines on development incentives, the plan may or may not have gone further. Without such a policy, it would have set its own precedent and didn't have a chance. An opportunity lost?

A number of states and provinces—and the Canadian government as well—have adopted incentive packages that include severance tax and royalty holidays and other inducements to speedy exploration and development.

Common features: time limits on eligibility for the benefits, greater benefits for earlier drilling and production, restrictions limiting benefits to activity in new fields, a trigger price for oil at which benefits are suspended (as low as \$19 per barrel, as high as \$33). Another strategy for quicker payback: accelerated depreciation.

"Peers in the (Canadian oil) industry say the incentives have had a big impact," says Tom Reinhart, vice president of finance and administration for Conoco Canada Limited. "There are definitely projects we've gone forward with that we wouldn't have without incentives."

But there's a catch. Cautions Hans Maciej, vice president of the Canadian Petroleum Association, "We're not in love with incentives; we'd prefer lower royalties on a permanent basis. (Royalties in Canada range from 25½ to 34 percent.) The incentives are temporary, and they distort normal business planning. Before the deadline for five-year holidays, there was a rush to drill. After that, activity dropped off dramatically.

"Who knows what would happen if we had 12½ percent royalties all the time? That's not an unreasonable rate over the life of a project, but it may be a good idea to look at a lower rate during payout and a higher rate after that so it averages out at 12½ percent."

Louisiana adopted a severance and royalty holiday program in 1986, and it's considering dropping lease bonus payments on state leases in exchange for development commitments. A preliminary analysis indicated no appreciable impact on drilling activity in the state, but neighboring states have adopted similar programs to keep up with the Cajuns.

"It's not just a matter of the state giving away revenues," says Jim Porter, secretary of the Louisiana Department of Natural Resources. "Our goal has been to keep the industry alive and to keep people working."

There's no consensus—in the industry or out of it—what impact such incentives would have in Alaska. There's even disagreement between

Prudhoe Bay's "haves" and "have nots" whether to seek tax breaks.

Says a spokesman for one of the majors, "We certainly aren't going to be at the forefront asking for incentives that may be interpreted as us asking for special treatment."

Some, like Natural Resources Commissioner Judith Brady, contend that because oil fields in Alaska are so large and lead times are so long, incentives won't sway companies' development decisions. Adds William Wade, president of ARCO Alaska, "You don't want to create an industry that relies on subsidy for survival."

Biggest challenge in tailoring an incentive program is identifying measures that will encourage new activity that wouldn't occur without incentives while minimizing the impact on state revenues. Let's not forget, however, that today's "giveaways" could be the fodder for tomorrow's investments.

"Incentives wouldn't be necessary if every field were a Prudhoe Bay," says economist Scott Hawkins, president and CEO of the Anchorage Economic Development Corp. "But when you start talking about the smaller marginal fields, those credits matter. The only time the state loses is if an oil company was ready to proceed with a project without incentives, and even then, incentives induce other private activity."

Alaska's willingness to renegotiate the 20 percent royalty forced on Conoco at Milne Point will be pivotal in determining when production resumes.

Oil & Gas's Michael Kotowski, who participated in a state study of oil industry incentives last year, notes: Milne could have applied for a reduced tax burden under terms of the Economic Limit Factor (ELF) after two years of production (late 1987). The two-year provision discourages companies from winning leases with unrealistic bids then applying for immediate relief.

The oil price collapse of 1986 has posed extraordinary circumstances for the industry and the state alike. The industry has adjusted, other states and provinces have adjusted, and now it's Alaska's turn. Since Milne Point production was suspended early in 1986, the state has reaped 20 percent of nothing from the lease.

A program to lower taxes and royalties on wells drilled within a specified time will push up the timetable for work already planned and provide a quicker infusion of new

jobs for Alaska—fueling “work flow” in the private sector instead of cash flow for state government.

Deadlines for any program designed to speed up activity in Alaska still would have to reflect the long lead times for planning and development in the state.

Says Wade, “Alaska could count on that kind of acceleration of work. Projects are evaluated on the basis of economics, and it just makes sense that anything like that would improve

the economics. And remember, Alaska is competing for oil company funds with other areas throughout the country and the world.”

“When you ask if the tax and royalty breaks are too small to make a difference, you also have to ask if they’re just enough to get things done,” says Conoco Canada’s Reinhart. That question is particularly compelling for the smaller North Slope oil prospects likely to chart the region’s oil future.

5

Offer enhanced oil recovery incentives.

Enhanced recovery projects are more capital- and labor-intensive than primary development work, and they yield greater benefits to the Alaskan economy as a result. Strategies for encouraging them: broader use of investment tax credits and severance tax exemptions for a specified period.

Enhanced recovery tax breaks and research credits could be the key to unlocking some of

the billions of barrels of Alaska’s proven yet unrecoverable reserves: West Sak Sands, half of Prudhoe Bay, Ugnu and the list goes on.

“When we talk about incentives, we need to consider the three ‘R’s.’” State Sen. Jan Faiks told an Alaska State Chamber of Commerce gathering in early December. “You start with a resource in the ground. It doesn’t become a reserve until someone drills and discovers it. The state gets the royalty after production begins.”

6

Reinvest a portion of the state’s oil wealth in an institute for petroleum research.

“Alaska hasn’t acted like the owner of its oil,” says G.D. Sharma, director of the Petroleum Development Lab at the University of Alaska in Fairbanks. “It’s acted like an administrator for collecting and disbursing taxes and royalties.”

Investing a small percentage of the state’s oil-related revenues in a research agency would enable Alaska to maximize recovery of known reserves, assist the industry *and* the state in evaluating prospects and provide an independent center for petroleum research.

Funds would be used to inventory oil and gas resources, to determine and address technological needs and to provide an independent clearinghouse for Alaskan petroleum data and other information.

Says Sharma, whose lab’s activities within

UAF’s School of Minerals and Engineering have been restricted by limited (and dwindling) budgets since it was established in 1984. “There would be an immediate return for Alaska in additional industry and federal interest if we had such a database.”

Such an institute also could develop equipment and technology to overcome barriers to oil activity or make it more efficient . . . and spawn their own global markets. Look at what’s happened with offshore equipment and technology developed by England and Norway for North Sea drilling and production.

Cowper’s proposed Alaska Science & Technology Foundation may be one avenue toward taking an oil and gas research initiative.

“Compared to other states and Alberta, state government in Alaska reaps a lot more revenues from petroleum and is a lot more dependent on oil activity,” Sharma says. “Yet they assist the industry and we don’t plow anything back in. You have to feed the goose that lays the golden egg.”

7

Designate the Department of Natural Resources as the lead agency for resource development proposals and give it ultimate authority in setting stipulations.

Industry figures this is one of the keys to improving operating efficiency in Alaska, and it's not hard to see why. One company estimates stipulations and environmental requirements add 20-25 percent to the overhead cost of drilling a well; another says permitting adds 50 percent to the time required to bring a new field into production.

"These days it doesn't take much to kill a project," says Thomas Cook, Alaska exploration representative for Chevron USA. "We face a lot of redundant reviews whenever we want to do anything."

Do your dentist, your minister and your babysitter have equal say with your mechanic when you want a tuneup for your car . . . only to have your marriage counselor draw up the final terms? Of course not.

So why do the Departments of Fish & Game, Environmental Conservation and occasionally Commerce & Economic Development have the same input on resource development issues as the Department of Natural Resources . . . so the final decision can be made by the governor's Office of Governmental Coordination?

8

Adopt incentives to encourage local hire and to improve Alaska's competitive position for oilfield fabrication work.

Tax credits and state investments in infrastructure could be used to help offset higher labor, freight and cost-of-living expenses in Alaska.

Punitive local hire legislation might be politically expedient, but it's failed miserably. The stick hasn't worked; time to try the carrot. By subsidizing infrastructure development and labor in the early stages, the state can lower costs and make Alaskan workers and companies more competitive.

Says Pete Leathard, president of Veco Inc., "Costs will go down as infrastructure develops. But in the early stages, we need incentives for things to be built here. The state needs to be willing to give on the front end to get it back later."

Veco's contract with ARCO Alaska to fabri-

Says Resource Development Council's Gay, "It just makes sense that the agency that knows the most about the resource should lead the show. Other agencies should comment and make suggestions, but Natural Resources should have the power to overrule inconsistencies and unreasonable stipulations from the others."

Designating Natural Resources lead agency would minimize duplication and unnecessary delays. Quicker, more reasonable reviews would result in faster returns to both the industry and the state. Stipulations shouldn't become "wish lists" for various agencies.

Maybe Alaska's state bureaucracy needs a bit of attitude adjustment, too. A lot of bureaucrats figure antagonism between regulators and the industry is natural. Oddly, other states have found it possible to work *with* the industry.

How about approaching the industry with: "What can the state do to help make the project work?" instead of: "Here's what you'll have to do to satisfy us before you start work . . ."

cate a pair of North Slope production modules in Wasilla will generate 50 jobs. It will be the first time production modules have been fabricated in Alaska.

"The oil industry is a place for Alaska to create jobs," says ARCO's Wade. "For a number of reasons, we prefer doing the work in Alaska to doing it in the Lower 48. But the work has to be done competitively if it's going to be done here."

One reason the modules will be fabricated in Wasilla instead of Anchorage: a low overpass on the Glenn Highway between the two cities that would have forced trucks transporting the units to the North Slope to use a detour. Says Veco V.P. Bert Hartley, "In a lot of cases, Alaska has failed to take commercial uses into consideration when it's designed things."

9

Get tough with the federal government on oil and gas development issues.

Admittedly, developments where the feds are involved are out of the state's control. But it would have to count for something if the state were to take an aggressive pro-development stance and protest unreasonable delays and requirements heaped on by federal agencies. (Do the fish really need lighted tunnels to swim

under the Endicott causeway?)

Who'd like to explain why several other states went on record last year supporting oil exploration on the Coastal Plain of the Arctic National Wildlife Refuge while the Alaska House was playing political games and failed to pass its own resolution supporting exploration during the '87 session?

If Alaska's policy makers can't speak with a united voice on oil and gas development, how can the state expect anyone else to listen?

10

Do nothing.

It's not paranoia if people are really out to get you. With all the times Alaska lawmakers have changed the tax rules on Prudhoe Bay and all the other times they've tried, it's little wonder Prudhoe operators in particular suffer heart palpitations whenever anyone so much as whispers the words "oil taxes" in Juneau.

Companies with big stakes in Prudhoe Bay and Kuparuk have too much to lose if "quid pro quo" becomes the rule of the day for new exploration and development incentives.

"Three of the companies have told us they want to stay completely away from the issue of taxes and tax incentives," says Natural Resources' Brady. "They're afraid it would be like opening Pandora's Box."

Alaska's historically unstable oil tax climate forces corporate decision makers to include "fudge factors" in project cost estimates. Al-

lowances for the possibility of higher taxes in the future damage the economics of every project and could result in low-margin project not being built.

"Our No. 1 priority is a stable tax policy," says ARCO's Wade. "We've only drilled about half of the development wells we're going to need on the North Slope, and there's still a lot of exploration and enhanced recovery potential, too."

ARCO sees billions of dollars it would like to invest in Alaska over the next 10 years, but we have to know what the rules are and be able to count on them."

Adds Veco's Leathard, "You can't recreate the traffic laws while someone is driving down the highway."

If lawmakers do adopt new incentives to encourage additional petroleum exploration and development in Alaska, they should aspire to disprove the maxim that for every action (new incentives for smaller fields) there's an equal and opposite reaction (new tax burdens for the giants). □



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The Missing Link

Four Small Steps Toward One Giant Economic Leap

Juneau entrepreneurs are carving business niches with fish incubator boxes, bottled spring water, beer and salmon skin accessories.

By Chuck Kleeschulte

WHEN GOV. STEVE Cowper spoke last year about the need for individual Alaskans to be inventive and open small businesses to lead Alaska out of its economic slump, some Alaskan entrepreneurs were listening. This is a look at several Juneau businessmen and women who took the plunge during the height of the downturn, survived and even have thrived.

HAROLD ZENGER
*North Pacific Aquaculture
Development Co. (NOPAD)*

It's been said that if you build a better mousetrap, the world will beat a path to your door. For Zenger, the saying's been true. Literally (almost).

The retired Alaska Department of Fish & Game technician who used to build salmon hatcheries for the state's Fisheries Rehabilitation Enhancement & Development Division was frustrated a decade ago by the design of the old boxes used to incubate fish eggs. Says he, "The old boxes were round. They used a lot of water and wasted a lot of space. I knew there had to be a better

design. I woke up all of a sudden at 2 o'clock one morning, and by 5 I had a new incubator box all sketched out. The problems were solved."

Zenger, who's 65, promptly patented his 4-foot-square, 14-inch-high box, which holds between 175,000 and 375,000 eggs. Its beauty: Incubator trays stack on top of each other, with water dripping from one box to another. In the process, the water reabsorbs oxygen and cuts the amount of water needed to raise fish. Now being used for steelhead as well as salmon, the boxes are non-toxic and easier to clean than the wooden boxes used previously.

Since launching the venture in his house, Zenger has expanded his aluminum fabricating business and patented his design in Canada and Japan. In October he became the first Alaskan to ink a contract inside the state's sister province in China, Heilongjiang. The Chinese will use 50 of the boxes in two new mainland salmon hatcheries. That contract could open the door to significant new business for Zenger's NOPAD.

"I could probably have a couple thousand boxes in use in the U.S. and a few other foreign countries," he says. "But if aquaculture in China grows like it looks

like it will, my business could really take off."

Zenger will travel to China in July to install the boxes in the 4- and 6-million-egg facilities. The hatcheries, which will raise pink and chum salmon, are several days' drive from Harbin, the provincial capital.

**JIM SATTERFIELD,
JIM STEVENS &
BILL SUMMER**
Alaska Pure Spring Water

When most people think about selling natural resources from Southeast, they think of peddling fish and trees. But the region's most plentiful resource by far is water. That's exactly what Satterfield's selling, and with considerable success.

For the past four years, 35-year-old Satterfield has been making his living selling bottled water to Juneau customers—water from a Mcendenhall Valley well. But last fall he sold Alaska

Zenger's incubator boxes are headed for China.



1988 Mark Kelley, Juneau Empire

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February 18, 1988

To: Rep. Adelheid Herrmann
Rep. Sam Cotton
Co Chairs
House Resources Committee

From: Max F. Gruenberg, Jr. *Max*

I would very much appreciate it if you would schedule a hearing on HB 471, relating to state royalty waivers, as soon as possible.

Thank you very much.

*March 8??
Thanks*

WSJ 1/26/88
 PF

Profit of Most Major Oil Firms Surged On Refining Upturn in Fourth Quarter

By JAMES TANNER

Staff Reporter of THE WALL STREET JOURNAL

Fourth-quarter profit of major oil companies generally surged on a year-end turnaround in the long-depressed refining business. Higher crude oil prices and strong chemical operations contributed to the gains.

Among the biggest oil companies reporting results, only Los Angeles-based Unocal Corp. showed a decline, mainly because of huge gains on asset sales a year earlier. Unocal's profit dropped 39%.

But Exxon Corp., Amoco Corp. and Atlantic Richfield Co. posted higher profit.

FOURTH-QUARTER NET INCOME

	1987		1986		% chg.
	in millions	per share	in millions	per share	
Exxon	1556.0	1.12	1480.0	1.03	+ 5
Arco	340.0	1.86	64.0	0.35	+ 431
Amoco	377.0	1.47	165.0	0.65	+ 129
Unocal	29.8	0.26	49.2	0.42	- 39
YEAR NET INCOME					
Exxon	4841.0	3.43	5360.0	3.71	- 10
Arco	1224.0	6.68	615.0	3.38	+ 59
Amoco	1360.0	5.31	747.0	2.91	+ 82
Unocal	181.4	1.56	175.8	1.51	+ 3

New York-based Exxon, the nation's biggest oil company, had the smallest percentage increase. Its net income climbed 5.1%, even though gains from asset sales contributed 34 cents a share to year-earlier profit.

Chicago-based Amoco's net more than doubled, while Arco's quintupled. For Los Angeles-based Arco, net included a gain of \$186 million from a public offering in October of Arco Chemical Co. shares, although that gain was offset by several charges.

The increase in refining margins was an important factor in each company's results—and was particularly evident at Ashland Oil Inc. of Ashland, Ky., which is chiefly a petroleum refiner. In its first quarter ended Dec. 31, net nearly tripled to \$71.1 million, or \$2.50 a share, after a \$31.1 million gain from an accounting change.

Stocks Surge

Analysts had generally expected refining profits to swell in the fourth quarter—and in some cases the results exceeded Wall Street expectations. In New York Stock Exchange composite trading yesterday, Arco surged \$2.75 to \$75.375, Amoco jumped \$2.625 to \$73.50, Exxon climbed \$1.125 to \$40.75, Unocal rose 50 cents to \$31.25 and Ashland fell \$1 to \$54.25.

For the first nine months of 1987, petroleum-refining margins were severely depressed because of the increasing costs of crude oil. But in late 1987 crude oil prices softened somewhat, thus firming refining margins. The decline in the value of the dollar also helped the foreign refining operations of international companies such as Exxon, whose fourth-quarter results reached their strongest level since the brisk 1986 first quarter.

"The combination of lower crude supply costs and relatively firm product prices led to an improvement in refining and marketing margins—in contrast to the situation earlier in the year when higher supply costs depressed margins," said Lawrence

G. Rawl, chairman of Exxon.

For 1987, however, Exxon's earnings fell despite higher revenue. Exxon's revenue rose 18% to \$22.59 billion in the quarter and 10% to \$84.12 billion for the year.

But for the quarter, Exxon's earnings from refining and marketing operations rose to \$376 million—their highest level of 1987. Earnings from worldwide exploration and production totaled \$993 million, or \$185 million higher than a year earlier.

Exxon sharply boosted capital and exploration expenditures in the quarter to \$2.98 billion from \$1.59 billion a year earlier. For all 1987, however, spending was flat at \$7.18 billion.

Petrochemical Demand

Although crude prices began tumbling in late 1987, average prices for the year climbed sharply from the severely depressed levels of 1986. Exxon, like several other oil companies, also cut operating expenses throughout 1987. Exxon's chemical profits reached a record level, reflecting stronger demand industrywide for certain petrochemicals and a sharp rise in petrochemical exports as the dollar tumbled.

At Amoco, Richard M. Morrow, chairman, cited a rise of \$3 to \$4 a barrel in the average price of crude, as well as improved refining margins and continued strong demand for chemical products. Revenue for the quarter rose 22% to \$5.92 billion.

For the year, Amoco's earnings jumped on a revenue increase of 11% to \$22.39 billion, reflecting, among other factors, the higher crude oil prices and lower exploration expenses. Capital and exploration expenditures for 1987 fell slightly to \$3.1 billion from \$3.2 billion in 1986, although Amoco previously has announced a spending budget of \$3.8 billion for this year.

At Arco, fourth-quarter earnings included gains totaling \$205 million. These were largely offset by \$193 million of charges, including a \$95 million charge for future environmental cleanup costs. Revenue increased 26% to \$4.59 billion. In 1987, revenue increased 12% to \$16.83 billion.

At Unocal, fourth-quarter earnings included a gain from asset sales of \$2 million, compared with a \$79 million gain in the 1986 quarter. Revenue for the quarter increased 13% to \$2.33 billion. For 1987, revenue increased 12% to \$9.39 billion.

Unocal continued its debt-reduction program in 1987, lowering debt by \$452 million to a total of just under \$5 billion. "We expect to continue to make significant debt reduction in 1988 and beyond," said Fred L. Hartley, chairman.

Microcom Acquires Meridian

NORWOOD, Mass.—Microcom Inc. said it acquired Meridian Technology Inc., an Irvine, Calif., marketer of communications software for personal computers.

Terms weren't disclosed.

Microcom makes computer communications equipment. Meridian markets the Carbon Copy line of software.

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Mark Abernathy, Pacific Coast Coal

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AT PRESS TIME

Valdez Refinery Planning Continues

Alaska Pacific Refining Inc. is moving ahead with permitting and construction plans for a 120,000-bpd refinery at Valdez despite pending legislation that could limit product export overseas to 33 percent of the plant's output.

An amendment to the Omnibus Trade Bill which would constrict product marketing in Pacific Rim nations is causing foreign investors to drag their feet on project financing. J. Timothy Campbell, APRI chairman, said the refinery is economically viable even if two-thirds of its potential exports are bottled up. He is counting on capturing West Coast and U.S. military markets in the Pacific Rim from foreign suppliers through efficient refinery operation and certain transportation concessions. Campbell reportedly has told the Seafarers Union that half of exported product would

be shipped on U.S. flagged Jones Act vessels.

As of late December, project management firm Bechtel Inc. of California was some 70 percent finished with a technical bid package to include project scope, site layout and project execution plan. Engineering firms working on permits include Dames & Moore, Santa Barbara, Calif.; North American Weather Consultants, Salt Lake City, Utah; Valdez Engineering, Valdez; and Environmental Services Ltd., Anchorage. UOP Inc. of Des Plaines, Ill., was reportedly 75 percent finished with its refinery facilities design at year-end.

OCS Lease Sale Update

The Minerals Management Service has rescheduled federal offshore oil and gas Lease Sale Number 97-Beaufort Sea for mid-March to give the state of Alaska time to review and respond to a study on drilling activity and bowhead whale movement.

On Dec. 24, the state commissioners of Natural Resources, and the Fish and Game and Environmental Conservation departments sent Secretary of In-

terior Donald Hodel a response outlining three main points.

First, the state agencies supported a lease sale alternative that would delete 201 blocks (412,354 hectares) around Point Barrow and west toward Point Franklin. Second, the state did not favor deleting 161 blocks (327,000 hectares) between Kaktovik and the Canadian Border but wants a whale feeding study done in the area. Third, the state wants seasonal drilling restrictions on exploratory activity during spring and fall whale migration periods.

The sale, originally consisting of 3,930 blocks in 21.2 million acres, has been set back from December 1986, July 1987 and January 1988.

Adjoining the sale 97 area to the southwest is Lease Sale Number 109-Chukchi Sea. The MMS reports the final environmental impact statement is available and this sale is on schedule for this May. The sale 109 area offers 5,450 blocks within about 29 million acres between 3 mi. and 239 mi. offshore extending from Point Franklin to Point Lay. No sales have been held in the Chukchi Sea planning area. Sale 85, scheduled for February 1985, was deleted from the leasing

schedule. Sale 109 was postponed from May 1987.

Copies of the final sale 109 EIS are available from the Minerals Management Service, 949 E. 36th Ave., Rm. 110, Anchorage, AK 99508-4302.

Denali Facilities To Expand

A new hotel and visitor access center are scheduled for construction at Denali National Park beginning this year.

The hotel will replace an existing facility, built as temporary lodging after a fire in 1972. It will feature 140 rooms, restaurant, snack bar, lounge, gift shop, post office, general store, laundry, showers and a rental outlet for camping and other recreational equipment.

It will be built on and adjacent to the existing hotel site. An auditorium and some other existing facilities will be incorporated into the new structure.

ARA Outdoor World, the current concessionaire managing the hotel, has first right to contract for the construction and management of the new hotel. The Park Service would solicit other bids if Outdoor World declines the contract.

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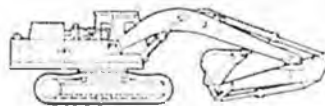
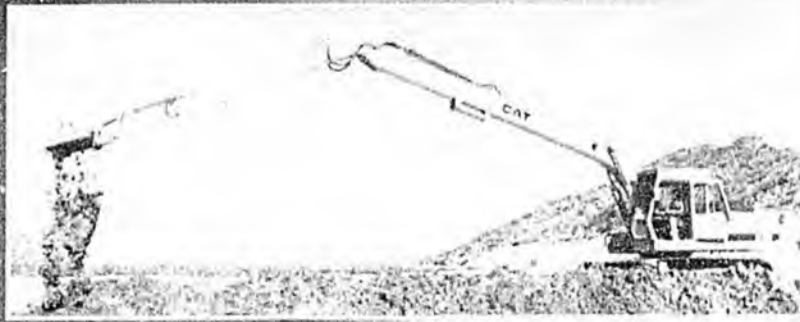
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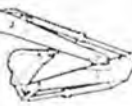


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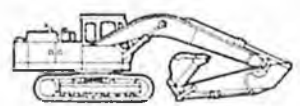
EL300



E240



EL240



E180



EL180

Power	137 FWHP	147 FWHP	148 FWHP	148 FWHP	118 FWHP	118 FWHP
Operating Weight	67,240 lb	69,665 lb	50,705 lb	52,030 lb	42,110 lb	43,650 lb
Maximum Ground Level Reach	38' 10"	32' 10"	33' 9"	34' 9"	31' 9"	31' 9"
Maximum Digging Depth	27' 4"	27' 4"	24' 4"	24' 4"	21' 6"	21' 6"
Lift Capacity - Ground Level, Over Front, 20' Reach	16,000 lb	22,600 lb	13,200 lb	16,000 lb	10,000 lb	12,050 lb

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FEATURES

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- 14 **ALASKA'S HIGHWAY AND ROAD SYSTEM IN CRISIS:** Current federal support for Alaska's highway construction programs expires in 1991. An in-state revenue stream to replace this cash flow would be equivalent to a new state gas tax of 40 to 80 cents per gallon. The alternative is a deteriorating transportation infrastructure.

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Alaska Construction Oil



FEBRUARY 1988 VOL 29, NO 2
At work on the road to the Red Dog Mine, a motor grader makes its way through the tundra. Photo by Judy Patrick.

The Road to Red Dog

Doing Battle with the Arctic

By MARK HARRIS

Building a road to what will become the world's largest zinc-lead mine located 100 mi. above the Arctic Circle can be compared to some of the amazing military construction projects accomplished during wartime.

Imagine a general addressing his construction battalion: "Your mission is to establish a beachhead and punch through 52 mi. of gravel road capable of withstanding 2,000-ton loads. You must rip, drill and blast every cubic yard of embankment material, erect nine major bridges and place 6.6 mi. of culvert at 450 more stream crossings.

"By the way, you cannot tear up one tussock of tundra outside of the road right-of-way in the process. You will work in summer, fighting hordes of mosquitoes and muck up to your knees. Then you will work in winter, fighting 30-degree-below-zero temperatures and winds of 25 knots. Good luck, gentlemen."

Such was the task facing Enserch Alaska Construction Inc. The Anchorage-based company was the low bidder last spring on the road to Red Dog mine at \$47.8 million. Other associated contracts brought the project's total cost to

about \$52 million — or \$1 million per mile for a dirt road with no intersections or stoplights.

The project is administered by the Alaska Industrial Development Export Authority and the Department of Transportation and Public Facilities. It is the key component of the DeLong Mountain Regional Transportation System. AIDA invested \$150 million in the road, ore conveyor system, fuel tank farm port and related facilities for development of a world class zinc-lead mine on land owned by the NANA Regional Corp. in 1982. NANA has signed an agreement with Cominco Alaska Inc., a subsidiary of Cominco Ltd. of Vancouver, B.C., to develop and operate the mine.

Wilson Hughes, president of Enserch Alaska Construction, said as road building began last summer, "We've talked about the project, examined the people, equipment, logistics and the schedule. The only thing that needs examining is the president of a company who would take on such a project and still sleep at night, and be able to spend some of his waking hours with a smile on his face."

As it turned out, everyone involved

has a lot to smile about. The contractor pushed through the pioneer road to the mine site 69 days ahead of the Feb. 1 deadline.

Much of the credit goes to a cadre of experienced construction professionals. Among them are Enserch's project manager Roger Blankenship, project engineer Dick Reed, spread foreman Harvey Powell and head mechanic Elmer Winquist. Winquist, credited with keeping all equipment operational, died in early December.

A team effort on the part of all of Enserch's management made for smooth going in the early stages of the project. Blankenship commented, "Harvey Powell always said he would have a road to the mine site by Dec. 1." All the skeptics were quieted when a drivable road extended from the port to the mine site by Nov. 24. Road building progressed at an amazing 100-ft.-per-hour average or about 2,000 ft. per day. They hauled an average 25,000 cu. yd. of material per day, Blankenship said, beginning about July 28. The quick work earned Enserch a \$2,500-per-day bonus for a total of \$172,500.

Between July and October, Foss Maritime Co. brought in 11 bargeloads



More than 1.1 million cu. yd. of geotextile was placed under the mine road, material site access roads and at bridge abutments. It was rolled out directly onto the tundra by ATVs in summer and with dozers after freeze-up. PN&D photo.

"... The only thing that needs examining is the president of a company who would take on such a project and still sleep at night, and be able to spend some of his waking hours with a smile on his face."
— Wilson Hughes



Crews quickly assembled 40-ft. by 30-ft. bridge sections in a large metal rib and fabric building at the project site. Eight prestressed concrete panels were grouted onto four I-beams for each 40-ft. section. Cutouts in the panels fit over Nelson studs welded to the girders. PN&D photo.

of equipment, supplies and fuel. The 269 pieces of equipment on site have a replacement value of \$30 million. The spare parts inventory is valued at \$4 million. That doesn't include the value of some 800 spare tires.

Four barges carried in 3.1 million gal. of arctic-grade diesel. Of this, 750,000 gal. will be used by Green Construction Co. of Anchorage, which has a \$20-million contract for mine site preparation work.

The contractor brought 280 major pieces of equipment on site. Some came from its Prudhoe Bay operations, from the Bradley Lake hydro project near Homer and some from Arizona. Equipment included 17 dozers, four graders, 12 loaders, three compactors, five cranes, 10 scrapers, 14 welders, 12 generator sets for 3,000 kW of power generation, 44 pit lights, 35 pickups and Suburbans and 53 hauling trucks, buses, service trucks, fuel trucks, mixer trucks and other vehicles.

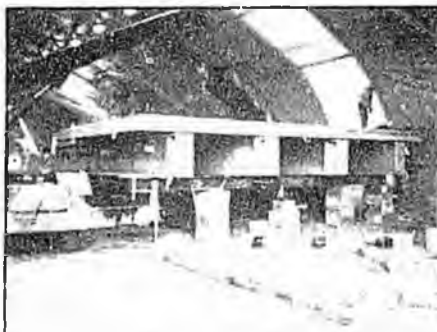
Shop buildings transported from Prudhoe Bay included a 100x300-ft. building and two 80x100-ft. buildings, all beluga-type structures with fabric stretched over metal ribs.

Getting to Work

The 2.64 million cu. yd. of embankment fill and 17,690 tons of riprap needed for the road and bridge abutments were to come from 17 material sites spaced along the project length. The challenge was getting to the pits. No construction equipment was allowed on the tundra until it was well frozen to prevent environmental scarring.

However, the contractor could begin road building under "summer conditions." That meant keeping equipment on existing fill and building road in tunnel-head fashion.

Enserch chose this option for reasons



The contractor will shop fabricate 22 40-ft. sections for nine bridges spanning a total of 898 ft. PN&D photo.

of worker efficiency, reduced equipment downtime and early jump-out for the project as a buffer against unforeseen delays later. This proved to be a wise decision.

"When we hit the beach in July, we just kept going," Blankenship said. Others may have chosen to get equipment on site, open a couple of beach material sites, set up camp, then leave the project until freeze-up when they could drive on the tundra.

"We kept going, kept our valuable people working and kept the project momentum high. Our schedule required building road at 100 ft. per hour, 20 hours a day for 132 days. This resulted in moving the road completion date up a year, enabling Cominco to push up its mine development schedule if desired."

Cominco plans to move heavy modules of milling and processing equipment on site in 1989 based on Enserch's road completion estimate.

Mile by Mile

Work progressed from the beach onward under "summer conditions" through an unseasonably mild October. The method involved dumping material onto existing fill. Then dozers spread the gravel onto geotextile laid on the tundra. This prevented fabric damage.

More than 2.1 million sq. yd. of woven geotextile was used on the main road, material site access roads and at bridge abutments. Crews on four-wheel, all-terrain vehicles unrolled 400-ft.-long rolls of fabric weighing 900 lb. Two 24-ft. widths overlaid with a 12-ft. width of Nicolon fabric were used under the roadbed the length of the project.

Not until early November was the tundra frozen enough for advance crews to race ahead and open up forward material sites. The contractor built some 23 mi. of road using the summer method. "This allowed us to lay off the project during January to March when the weather is miserable and productivity is very low," said Wilson Hughes.

Once equipment reached a material site, it took about two days to scrape the overburden, drill and shoot the first material. Blankenship said. "We tried to open up about a 150-ft. face of rock to work from. Meanwhile, we were building pit access roads with the Terex TS24 scrapers and Terex 40-ton offroad trucks.

"We would excavate enough material to lay down a 3-ft. road base at first. Scrapers were used to extend the base road 2 to 4 mi. on either side of a pit. Then the advance group would move on

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to the next material site and repeat the process.

"The Terex 40-ton haulers would extend the base road several more miles until the sections between pits were linked. Then the Kenworth tractors pulling 30-ton Maxhaul trailers would come in and build the roadbed up to subgrade levels. Subgrade depth averaged 6 ft., but some stream crossings with culverts required up to 50 ft. of fill."

In the typical pit situation, explosives crews would drill, fill and blast a section then ready another section for blasting. At some sites, the ripping power of Enserch's Caterpillar D11 dozer precluded the need for immediate blasting at material sites where it was used. "I think the D11 gave us about 3 ft. of material we couldn't have ripped otherwise off every material site," Blankenship said. "We ripped down about 20 ft. at MS 2 with the D11. A D9 may have gotten us down to 15 ft. there."

Enserch spent \$24,000 to bring its D11 dozer from a job site near Tucson, Ariz. It was disassembled into three main pieces, trucked to Seattle and barged to the Red Dog port site for reassembly.

For blasting, Enserch used \$1 million worth of ammonium nitrate, mixed with fuel oil at the site. The explosives shipment was so large, Enserch had to get permission from the Department of Defense to use a military munitions transfer facility in Puget Sound to load its barges.

The shipment of 3.2 million lb. of material was the largest commercial quantity ever to go across the Indian Island dock at Hadlock, Wash. The supplier was Alaska Explosives Co.

Load 'Em Up, Head 'Em Out

The load-haul-dump process for embankment material quickly became well-orchestrated under Blankenship's guidance. He would time the loadouts to keep a handle on time-cost factors.

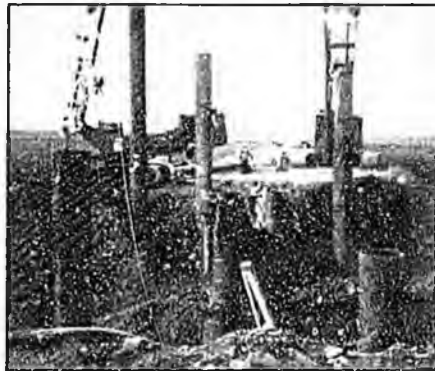
"Dozers would continually push material to the loading area," Blankenship said. "Two Cat 988 loaders would be positioned so a truck would pass one and receive a load then loop back between loaders and get bucketfuls from both sides to make a full load. The process generally took under 30 seconds per truck for the 30-ton units and 45 to 60 seconds for the 40-ton haulers."

"We tried to keep gravel hauls down to 30 minutes for a complete load-dump-load cycle. Most cycles took 20 minutes or under, depending on the distance between the pit and dump point," Blankenship said.

Material sites ranged from at road-side to 1.6 mi. away via access road. There could be up to 15 trucks between pit and dump site on the longest hauls.

Meanwhile, scrapers were making passes up and down the material site, getting dozer assists when needed. The loaders also kept clearing the traveling surface of sharp, angular rock, which proved hard on tires.

Prior to construction of the nine major bridges, the contractor kept road building on schedule by using detours.



Nine major bridges on the project will require the placement of 156 pipe pile supports and cell anchors, or up to 10,500 lin. ft. of pile. The contractor is using the drive-and-drill method at most locations. PN&D photo.

Crews had made several temporary bridges with 48-in. I-beams and 12-in. decking that could be moved and used where needed.

Complex Bridge Work

Peratrovich Nottingham & Drage Engineers of Anchorage designed the road and stream crossings. All design criteria revolved around the 1,500- to 2,000-ton modules Cominco must transport overland to the mine site.

A minimum 4-ft. depth of embankment fill was required to prevent permafrost thaw. Hills could be no more than 6-percent grade and curve radius could be no more than 600 ft. due to the module carriers' limitations on climbing and turning.

The one-lane road with 30-ft.-wide traffic surface features 300-ft.-long passing turnouts about every two miles. This design feature saved millions of tons of fill that would be specified for a two-lane road.

There are 646 drainage crossings including 13 major stream crossings. Nine bridges, 40 ft. to 200 ft. in length are needed. There are four major culvert crossings requiring 4-ft.- to 12-ft.-diameter pipe.

Four bridges feature sheet pile cells,

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or bulbs, extending 60 ft. back from the abutment backwalls. This PN&D design was used only on single-span bridges of 40 ft. where streambed shifts could threaten bridge integrity.

Also, it proved a sensible way to keep riprap from choking a stream on short crossings, a concern of the Alaska Department of Fish & Game. Twelve streams contain various anadromous species.

Alan Christopherson, PN&D project engineer, said these bulbs extend 270 degrees in an arc from the abutment wall. "This creates a diaphragm with shape retention provided by fill pres-

sure. We didn't make this a closed 360-degree cell because it is easier to place fill and do compaction with an open-end cell than to lift fill into a closed cell."

Sheet pile flange walls were placed on the upstream and downstream sides of cells as needed for scour protection and as deflectors should the stream channel shift. One single-span bridge and the four multi-span bridges are natural spill-through types with benched riprap slope protection.

Some 44,000 sq. ft. of sheet pile is to be driven 12 to 20 ft. depending on site characteristics. Six-in.-diameter pilot holes were drilled every 18 in. to facili-

tate driving with a vibratory hammer.

The project will use 10,500 lin. ft. of 24-in.-diameter pipe pile for bridge supports and sheet pile cell anchors. Pier piles were required to bear 240 tons each. Abutment piles must bear 120 tons.

Bridge design plans showed two alternative pipe pile placement methods. One involved drilling a 12-in. pilot hole before pile driving. The other called for grouting the pile into a larger auger hole. Both methods showed the use of a sleeve or casing if practical. Site conditions made both methods largely ineffective, so Christopherson recommended a drive-and-drill method used successfully elsewhere. The casing was eliminated and the 24-in. pile driven to resistance with a diesel impact hammer. Where driving alone ended up short of desired embedment, the pile was cut off and drilled out with a 16-in. auger. A pilot hole was drilled to desired depth, a new section welded to the pile as needed and the pile was driven to refusal.

The contractor established a smooth work flow of driving, drilling, cutting, welding and final driving that kept all equipment working efficiently.

A crane accident during pile driving slowed things temporarily but Blankenship refused to let it interfere with construction goals. As a Manitowoc 4100 crane was being moved on a low-boy, a temporary bridge settled on one side and the crane pitched off the low-boy onto its boom. The crane was not damaged but the boom and impact driving guide structure were destroyed.

Christopherson, who was on site at the time, said, "Enserch had some very fine welders on the project and they went to work to rebuild the structure that holds the drive hammer and guides the pile. Spare drive leads, as they are called, were not available."



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Up to 44,000 sq. ft. of sheet pile will be driven to form open-ended cells and flank walls at the abutments of four bridges. The design provides high load-bearing qualities while preventing fill encroachment into streams. PN&D photo.

Welders used air arc welding to disassemble all the steel frame members. Using heat and force, they realigned all the pieces and rewelded them. It took about four weeks to rebuild the leads and hydraulic spotter unit that keeps the leads plumb.

Meanwhile, Blankenship scoured the country for a new boom. Enserch flew in two mid-boom sections from its Prudhoe base but the butt and tip sections were not available. Enserch ended up having the Manitowoc factory deliver them. Promised in 10 days, the sections took three and a half weeks to arrive on site. This mishap did not stop the pile driving. A second 4100 was fitted with the pile driving hydraulics and repaired leads and work continued as before.

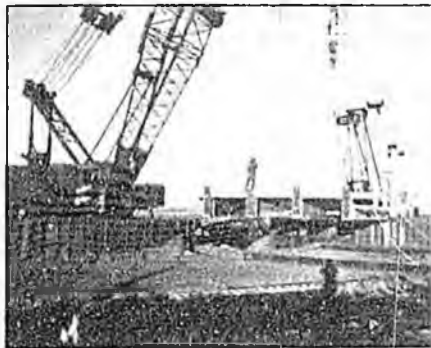
Bridge Building Factory

The contractor elected to assemble 40-ft. bridge sections on site in a heated shop building due to the amount of grouting involved that required cure time. Bridge crews soon got the process down to a science. They were able to assemble, form, grout and move out a 40-ft.-long by 30-ft.-wide section in five days, including three days' cure time for the grout.

The process began with four I-beam girders placed at 8-ft. centers on blocking high enough for a lowboy to be driven under.

Eight 4-ft., 11-in.-wide by 30-ft.-long prestressed concrete panels were placed across the girders. Preformed cutouts in the 1-ft.-deep panels matched up with patterns of Nelson studs welded in groups of three onto the girders.

Grout from 8-yd. mix trucks was pumped into the gaps between panels and into these "pockets" around the Nelson studs. Shims placed between the girders and deck panels left a void for grout to spread, creating a tight seal



Forty-ft. bridge sections, weighing 120 tons, are fabricated under cover at the Red Dog construction camp, trucked to bridge sites and lowered onto pipe pile supports with Manitowoc 4100 and P&H 5100 cranes. Twenty-two such sections are needed for nine bridges of one to five spans each. PN&D photo.

while adjusting for fabrication differences in the girders and panels. The grout, once vibrated into the pockets and into the void underneath, assures a strong, even bearing surface for the heavy loads these bridges must bear.

The grout was premixed and shipped to the site in 2-ton bags. The mix consists of type III cement, fine-aggregate sand and aluminum flake additive. This flake creates some expansion to offset shrinkage during grout drying.

Bridge sections are trucked to crossings and lifted onto pipe pile supports with two cranes. As of mid-December, one bridge was completed, piles were ready for bridge placement at two more and pile driving was under way at a fourth crossing. Detours and temporary bridges provided access at other stream crossings.

Calling a Halt

Altogether some 42 mi. of subgrade road has been completed from the port. Another 10 mi. of pioneer road is drivable to the mine site. Work halted on Dec. 17 due to mechanical considerations and impending storms. "We had been achieving about 80-percent equipment availability," Blankenship said. "That compares to about 90 percent on

a Lower 48 job of comparable scope, but the conditions are radically different at Red Dog.

"It was determined that productivity would slip below acceptable levels during the depths of winter." Some December days registered 30 degrees below zero with 25-knot winds. So, work was suspended for nearly three months.

Beginning in mid-March, Enserch crews will be back at it, drilling and shooting new roadbed material. They will bring the pioneer road up to subgrade level beginning in April, fabricate and install more bridges and place remaining culverts.

A major aspect will be the crushing and placement of some 770,000 tons of surface course for the top 12 in. of roadway. At press time, the state had yet to identify a source of rock to meet specifications. Rock tested in most material sites has not passed both hardness and composition specs. Failing to find an acceptable top-grade source, the state may have to revise the specifications, according to some sources.

But Blankenship and his crew aren't thinking about that now. They are off the front line and enjoying some R & R. The time to rejoin the battle will come soon enough. □

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The national Highway Users Federation and the Highway Users Federation of Alaska have prepared a report for the Alaska Legislature which brings to light some disturbing information about the state's highway and road system and the agency that oversees it.

Major findings and concerns in the report, entitled "Alaska Highway Program Review," can be summarized in six points:

1. Roadway maintenance and repair have been cut to the point where Alaska may not now be gaining the maximum service life from highway-improvement dollars.

2. The Alaska Department of Transportation & Public Facilities has cut manpower to the point where reduced snow and ice removal work sometimes creates hazardous conditions and inconvenience for motorists.

3. Alaska's State Highway Program lacks a dedicated fund source, making it difficult to set a long-range plan for system modernization, pavement upgrading and system expansion. (Editor's note: The Legislature is expected to take up a bill that would double the motor fuels tax to 16 cents. However, state law prohibits dedication of new tax revenue to specific highway or other uses.)

4. Boroughs and communities look to the state for road project financing. Meeting local road needs dilutes the effectiveness of the state's highway program in meeting maintenance and modernization needs of major urban and rural routes.

5. Alaska's transportation program is decentralized into three regions. This makes it more difficult than in other states for DOT/PF officials to develop and apply uniform policies. A relatively small headquarters technical staff further retards policy development and implementation monitoring.

6. A need exists to develop better information on the condition and performance of Alaska's transportation systems and the adequacy of funds to meet the needs.

Traditionally, Alaska has received a large portion of its transportation infrastructure funding from federal sources. Of \$525.4 million in DOT/PF expenditures in 1986, \$197.2 million was funded by federal sources.

Alaska is miles ahead of the other states in benefits from the Federal Highway Trust Fund. At \$150 million per year, this funding resource pays for most highway improvements in urban and rural Alaska.

Federal support remains vital to Alaska's highway development. Historically, Alaska has received up to eight times what Alaskans contribute in federal highway taxes on motor fuel and truck purchases. No other state comes close to this return. In spite of this relatively generous revenue, Alaska's highway needs continue to outstrip its financial resources.

Alaska's spending plan for these funds falls into four major categories. First, as pavements and the other highway elements wear out, they need to be re-

placed. Pavements are designed to last about 10 years, meaning that each year roughly one-tenth of Alaska's highway miles needs to be resurfaced. As new miles of pavement are added to the highway system, the need for rehabilitation increases.

Second, Alaska has a program to bring the highway network up to modern and safe standards. That means wide shoulders and gentle curves, such as on the Parks Highway between Anchorage and Fairbanks. At current funding levels, however, correcting these geometric, structural and safety problems on major highways, such as the Tok Cut-off, extend beyond the year 2000.

Third, there are major capacity problems in urban areas. Because of right-of-way costs and sophisticated urban design, these projects are extremely expensive and have to be staged over many years. Although traffic growth has stagnated across the state, traffic volumes remain at or near record levels, requiring continued investment in new urban facilities. Existing funding programs fall short of meeting the above three needs by some \$25 million annually.

Finally, demand continues for new rural roads: some for resource development and some for connecting existing communities to the state's contiguous highway system, such as the proposed Copper River Highway to Cordova.

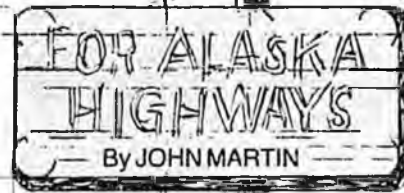
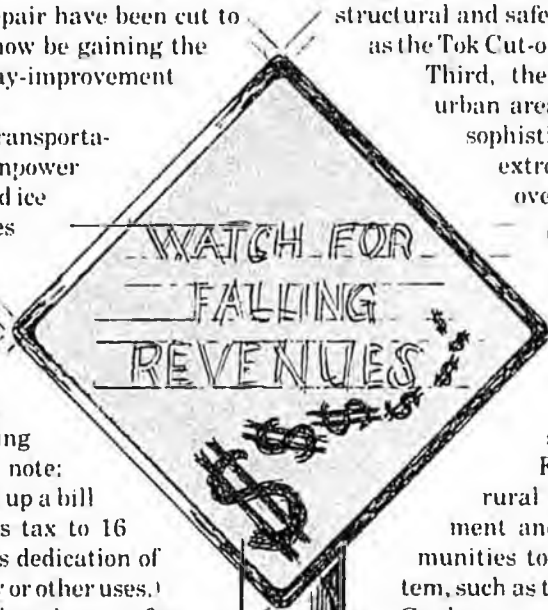
Future Funds Not Assured

The current federal support for Alaska's programs expires in 1991. Reauthorization will be debated in Congress over the next three years.

An in-state revenue stream to replace this cash flow would be equivalent to a new state gas tax of 40 to 80 cents per gallon. The alternative is a deteriorating transportation infrastructure which translates into direct economic cost for users, due to five factors: increased fuel consumption; increased wear and tear on vehicles and premature depreciation; increased labor costs, for commercial vehicles in congested traffic; increased accidents; and increased highway construction and repair costs. When the current highway bill was pending in Congress a year ago, the U.S. House of Representatives drafted legislation to make major cuts in federal aid to Alaska's highways. States contributing more to the highway trust fund feel that it is unfair to heavily subsidize Alaska's program. We have few, if any, strong allies in this battle.

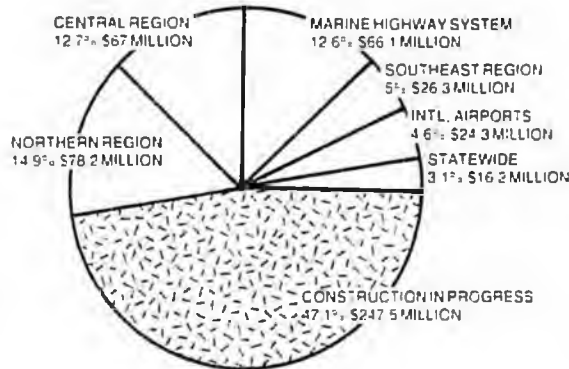
The American Association of State Highway and Transportation Officials (AASHTO), in conjunction with many other organizations including the Highway Users Federation, is spearheading a national effort to prepare a policy framework for enhancing America's surface transportation system in the 21st century. This framework is expected to form the backbone of a new national surface transportation act for the 1990s. Across the nation, state and local officials, private industry and public interest groups are working together to

- Assess the nation's surface transportation requirements through the year 2020.

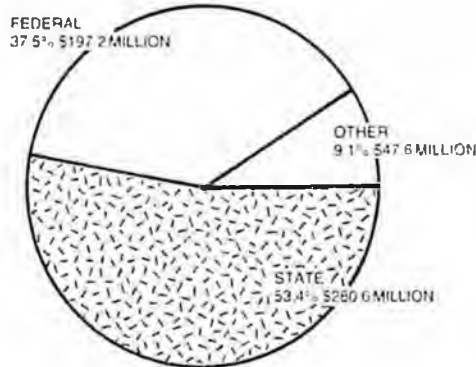


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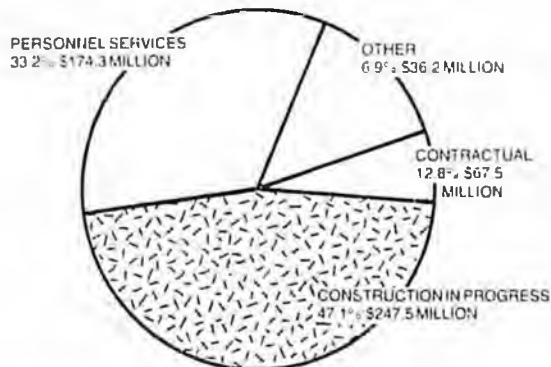
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EXPENDITURE OBJECT



TOTAL: \$525.4 MILLION

Source: 1987 Alaska Highway Program Review

- Develop alternative proposals for meeting those requirements at the federal, state and local levels.

- Achieve a consensus on the best means of doing the job.

The upcoming Alaska Transportation Forum is part of the information-gathering phase of this effort aimed at assessing the nation's surface transportation requirements through the year 2020. The Highway Users Federation, in conjunction with AASHTO, has asked each state to hold a public forum on the future needs of surface transportation in America.

This is a key step in forming a new national surface transportation policy. The focus for U.S. highway policy for the last three decades has been completion of the interstate system. It will be completely funded as the current legislation expires in 1991. With major national and state policy changes looming, now is the time to make Alaska's concerns known.

This fifth annual Alaska Transportation Forum in March not only will incorporate Alaska's input into the "Transportation 2020" process, but will also address Alaska's airport, rail, port and highway systems issues, as well as transportation research in Alaska. Because of the 2020 theme, this year's Transportation Forum is expected to tackle issues with long-term implications.

A Gathering of Support

At the Transportation Forum, we expect to hear from groups supportive of transportation programs. One such group is the Alaska Department of Transportation and Public Facilities, itself heavily dependent on federal programs for primary funding. Another group is the Associated General Contractors, some of whose Alaska chapter members depend primarily on construction work funded by DOT PF.

A third group is the Fairbanks Chamber of Commerce. Through its transportation committee and the annual publication of "Interior Transportation Needs Report," the chamber works to understand and influence improvement plans for the state transportation system.

Others with interests in transportation improvement programs are the trucking industry, local governments, the Alaska Municipal League and community chambers of commerce.

The Alaska Transportation Forum can help strengthen transportation constituencies and develop a better understanding of how current programs function and what they accomplish in Alaska. Further, this forum will look at prospects for change from an Alaskan perspective and discuss the uniqueness of transportation needs in Alaska and the relationship of those needs to national transportation policy.

We need to recognize that Alaska's aging roads, bridges, airports and other facilities need increasing rehabilitation and repair. We also know the strong correlation between a healthy transportation system and economic vitality. Greater competition for revenue is inevitable as financial needs in all areas increase.

Alaskans have a lot at stake and need to send a strong, clear message to Washington.

The University of Alaska Transportation Center's fifth annual Transportation Forum will be held at the University of Alaska, Fairbanks, March 4-5. For information, contact John Martin at (907) 451-5150. □

John D. Martin is the chief of planning and research for the Alaska Department of Transportation and Public Facilities. He is a registered engineer and is the DOT PF representative to the Advisory Board for the University of Alaska Transportation Center.

DRILL REPORT

A dozen land-based rigs were on the active list as of early January and drillers were preparing others for work as oil companies mobilized for increased North Slope development and exploratory drilling.

Arco Alaska Inc., Standard Alaska Production Co. and Texaco were all looking to tap additional reserves within or near the Prudhoe and Kuparuk River units.

Arco was building a 4-mi. ice road off the haul road and ice pad from which to drill its Prudhoe Pipeline State No. 1 well on one of 30 state tracts gained in the 1985 Kuparuk Uplands No. 47 sale. Doyon Drilling Co.'s No. 9 rig is drilling this test, targeted for below 12,000 ft.

Texaco was to begin drilling this year the first of up to three wells on three of 51 tracts gained in the 1986 state Kuparuk Uplands No. 48 sale. Texaco has proceeded with the permitting process while awaiting a financial commitment from 50-percent partner BP America, parent company of Standard Alaska Production Co. Should BP decline to participate this season, drilling would be bumped back to winter 1989.

Plans call for spudding the first well from an ice pad on ADL 368033, a tract about 26 mi. south of the Kuparuk field 2G pad. Access is via an ice road from the 2G pad.

The first well, designated Wolfbutton No. 1, has a target depth of 9,500 ft. Successive wells would be drilled from ADL 386044, 5 mi. to the northwest, and on ADL 368036, 3.3 mi. south of the first well site. A drilling contractor has yet to be announced.

Standard will use two Alaska United Drilling Co. rigs and one Nabors Alaska Drilling Inc. rig for developing the Eileen region at the western edge of the Prudhoe Bay unit. Nabors is modifying its No. 22-E rig for work to begin in April.

An undisclosed number of wells will tap an isolated section of the Sadlerochit formation. Standard estimates this development program could recover about 110 million bbl. of oil. Drill pads are in place. Plans to develop the Eileen area in early 1987 were postponed until oil prices recovered and showed some signs of stability.

Standard also is launching a \$120-million project to bring the Niakuk field into production by 1990. The company estimates that 12 production wells on a gravel island a mile offshore of the Sagavanirktok River could produce 19,000 bpd. Recovery of 58 million bbl. is expected from the reservoir, estimated to contain 150 million bbl.

Like Standard's Endicott field to the east, Niakuk development hinges on construction

of a gravel causeway linking the production island to the mainland. Should the Army Corps of Engineers require a full environmental impact study, project costs would jump and production would be pushed back to 1991.

In December, Amoco Corp. announced plans for a \$3.8-billion exploration budget. Alaska could see up to \$25 million in capital and exploration spending, said company officials in Denver.

Marathon Oil Co. is assessing the damage to the Steelhead platform in the Trader Bay Unit. (See *AC&O*, Nov. 1987, p. 22.) A Dec. 20 gas well blowout and eight days of fire caused destruction of the Parker Drilling Co. rig and damage to the helideck and crew quarters.

The rig had drilled the M-26 well to 2,265 ft. through the northwest platform leg and crews were cementing casing at 2,255 ft. when a gas leak developed. A diverter system failed to channel the gas to burnoff towers and crew members evacuated the platform in emergency pods. The pressurized gas plume ignited at the wellhead a few hours after the blowout. No serious injuries were reported. On Dec. 28 the well bridged over with debris and the fire went out. □

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Drill Report Continued

Area
Location
 Driller, Rig, Status, Well Site, Operator

North Slope

Prudhoe Bay

Alaska United, #2, (d), PBU DS E-25, S APC
 Alaska United, WSR #1, (w), PBU DS 5, Arco
 Nabors, 1-ES, (w), PBU-GC-1D, S APC
 Nabors, 18-E, (d), PBU DS C-30, S APC
 Pool Arctic Alaska, #102, (w), PBU DS 17, Arco

Kuparuk

Doyon Drilling, #14, (d), KRU DS 3H-12, Arco
 Roll 'n Well Servicing, Nordic #1, (w), KRU
 3M -, Arco

Lisburne

Nabors, #28E, (d), PBU L2-32, Arco

Endicott

Doyon Drilling, #15, (d), DIU 2-24 R12, S APC
 Pool Arctic Alaska, #7, (d), DIU 3-39 J39, S APC

Barrow Gas Field

Grace Drilling Co., #211, (i), NSB #7, NSB

Offshore

Beaufort Sea

Canmar, SSDC Mat, (d), *OCS Y-0943 Aurora
 #1, Tenneco

Cook Inlet (Offshore)

Granite Point Shoals

Amoco, Platform Anna, (c), GPS-36, Amoco

Middle Ground Shoals

Amoco, Platform Baker, (i), MGS 17-1, Amoco
 Amoco, Platform Dillon, (i), MGS 8-RD, Amoco
 Amoco, Platform Anna, (c), GP-1, Amoco
 Shell, Platform A, (i), MGS G-16, Shell
 Shell, Platform C, (d), MGS -, Shell

McArthur River Unit

Union, Greyling Platform, (w), MRU G-30, Union

Trader Bay Unit

Marathon, Dolly Varden Platform, (w), TBU D-6,
 Union Marathon
 Marathon, Steelhead, (i), *TBU M-25, Union
 Marathon
 Union, Monopod, (i), TBU-, Union

Cook Inlet (Onshore)

Cannery Loop

Grace Drilling Co., #154, (d), *Cannery Loop 3,
 Union

Kenai

Great Northern Drilling, #1, (s), *Mike Pelch #1,
 Far North

Swanson River

Roll 'n Well Servicing, #5, (i), -, Arco

Other

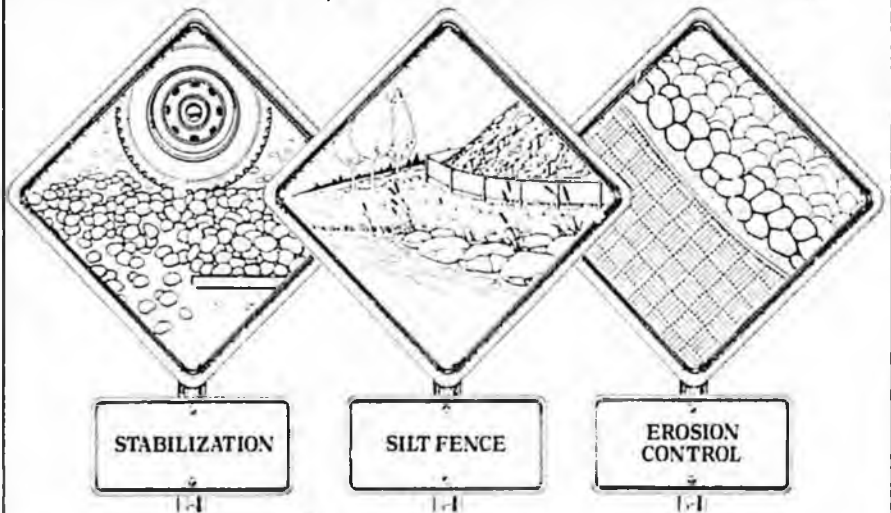
Katalla

NKG Drilling, NKG #1, (s), *Katalla KS-2,
 Alaskan Crude

KEY

- (c) — completing
- (d) — drilling
- (i) — idle
- (l) — logging
- (r) — rigging up
- (s) — standby
- (t) — testing
- (w) — workover
- *exploratory well

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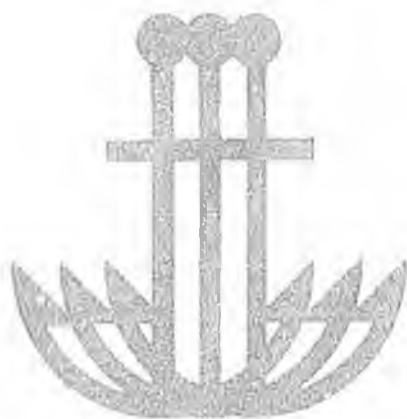
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Industry Feature

DOG Studies Incentive and Procedure Changes

By MARK HARRIS

The Alaska Division of Oil and Gas within the Department of Natural Resources has been reviewing possible drilling and production incentive legislation and leasing permit-procedure changes that could save the oil industry money and boost state royalty revenue.

Incentives under consideration are modeled on programs now in effect in several states and Canadian provinces. They include the following:

Severance Tax Exemptions and Royalty Holidays. This would encourage bringing new reserves on stream by offering limited time tax exemptions and royalty-free periods for new wells drilled in a specific period. Alberta collects no royalty for a year up to \$1 million on eligible wells and Saskatchewan has a three-year royalty or tax holiday on wells drilled through June 30, 1988, and a two-year holiday on wells drilled between July 1, 1988, and June 30, 1989. Louisiana exempts severance tax on certain wells through 1990 and levies no tax on development through 1989 for discoveries made after mid-1986. No production or monetary limits apply. Mississippi has enacted similar legislation.

Discovery Royalty. This would allow a royalty rate cut for a specified time for a producer who discovers and produces oil and gas on state leases in a specified period. The Alaska Legislature repealed such a law in 1969.

Exploration Incentive Credits. Alaska statutes allow use of such credits. The program could be expanded under existing law to include more leases. Alberta allows credits on 50 percent of well costs, applicable to royalty reduction or transferable to other operators.

Enhanced Oil Recovery. These capital and labor-intensive operations could be exempted from severance taxes for specified periods. Also, the current gas plant investment tax credit program could be expanded to increase feasibility of large projects under current oil prices. New EOR incentives could spur development of known reserves such as the West Sak and Ugnu Sands reservoirs on the North Slope, or help the economics of secondary and tertiary recovery programs for existing production.

New Tax Court. Legislation has been drafted to establish a new division within the superior court system. Appeals of disputed oil and gas tax assessments could go directly to that court, bypassing the current Department of Revenue appeals process. About \$1.5 billion in disputed tax assessments is now pending in Alaska.

In addition, proposed lease-operations permitting changes include the following:

Three-year Lease-Operations Permit Terms. This would replace the one-year-commence, two years-complete terms with a standard three-year construction-phase term with annual status reports required.

Six-year Lease-Operations Permit Terms. To be granted for projects expected to exceed the three-year term. Annual status reports required.

Ten-year Lease-Operations Permit Terms. This would fix the normally long-term use of abandoned or unused pads for storage purposes. Status reports to be required every other year.

Other possible operation-procedure changes would create a single status reports filing date for many operations and two dates for filing completion reports for summer and winter work, instead of 15 days after finishing the construction phase, as is currently required. Further changes would deal with past-due reports, as-built submissions, gravel accountings and unit representative requirements.

All contemplated changes would need approval from DNR, the governor's office and passage into law by the Legislature. □

BRIEFS

• R. Craig Taylor, former Alaska businessman and bank director, died of heart failure Nov. 18 in San Diego, Calif., at the age of 69. Taylor founded and served as president of Craig Taylor Equipment Co. He started the company in Anchorage in May 1954. The company later opened Alaska branches in Fairbanks, Soldotna, Delta Junction and Wasilla and another office in Seattle. The firm was appointed John Deere dealer for the state of Alaska in May 1959.

Born Aug. 5, 1918, in Boise, Idaho, Taylor came to Anchorage in 1953. In July 1967 he was elected to the 11-member board of directors of the Matanuska Valley Bank. Taylor was a lifetime member of the Anchorage Elks Lodge No. 1351 and a 35-year member of the Associated Equipment Distributors. He was a past member of the Anchorage Petroleum Club and an associate member of the Associated General Contractors.

Following a heart attack in 1967 Taylor semi-retired to his ranch in Dulzura, Calif., where he resided at the time of his death. He leaves his wife, Thelma, and a son, Michael, both of Dulzura.

The family suggests that memorial contributions be directed to the Anchorage Salvation Army, 742 Barrow St., Anchorage, 99501, or the charity of the donor's choice.

• Arthur J. "Jack" Sahlberg Sr., founder of the Jack Sahlberg Equipment Co., 300 Aurora Ave. N., Seattle, died Dec. 9 in Kirkland, Wash., at the age of 91.

Sahlberg, who was born to Swedish parents in Osage City, Kan., on Oct. 10, 1896, first learned to speak English in primary school. He served in the U.S. Navy during World War I, attending the University of Washington as part of his naval training, and joining the Sigma Nu fraternity. He received his commission as a naval officer in 1925 and later became commander of the destroyer USS McKenzie.

Sahlberg married Helen E. Morris in 1923 at Kettle Falls, Wash. He joined the staff of the Howard Cooper Co. in 1936 and in 1945 became the branch office manager of the company's Portland office. He and his son A.J. "Jack" Sahlberg Jr. founded the Jack Sahlberg Equipment Co. in 1950.

He is survived by his wife, Helen "Nellie" Sahlberg of Bellevue, Wash.; Jack Sahlberg Jr. and his wife Dulcie, who live in Seattle; his daughter and son-in-law, Judith and Richard L. Evans of Bellevue; 10 grandchildren and nine great-grandchildren.

The family requests remembrances in his name be sent to Bellevue Medic One, Northwest Harvest or favorite charities.

• Brent T. Drage, a partner in the Anchorage consulting engineering firm of Peratrovich, Nottingham & Drage, died Jan. 2 at the family cabin in Rainbow Valley, south of Anchorage.

Drage was born Sept. 26, 1944, in Salt Lake City, Utah. He had lived the past 20

years in Anchorage, Rainbow Valley and Fairbanks, where he received a master's degree in civil engineering from the University of Alaska in 1977.

His Alaska work experience dates back to 1967, when he was a surveyor for the Department of Highways, working summers while attending school. After receiving his bachelor's degree in civil engineering from Utah State University in 1969, he worked as a professional engineer during the exploratory stages of the Prudhoe Bay oil field.

In 1981, he joined Peratrovich & Notting-

ham Inc., which the following year became Peratrovich, Nottingham & Drage Inc.

He was a member of the American Society of Civil Engineers, the Project Management Institute and Sigma Chi fraternity.

He leaves his wife of 20 years, Kathleen, and his sons, Jeremiah and Joshua, all of Anchorage, his parents, Don and Dixie of Logan, Utah; and his brothers, Gary, of San Diego, and Jeffrey, of Monument, Colo.

Memorials may be sent to the Brent Drage Memorial Fund in care of Peratrovich, Nottingham & Drage Inc., 1506 W. 36th Ave., Anchorage, AK 99503.

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• Shareholders elected six directors to the Sealaska Corp. Board of Directors at the 14th annual meeting in Sitka on Sept. 19. Elected to the board of directors for three-year terms ending in 1990 were **Charles Carlson**, a commercial fisherman from Sitka; **Niles Cesar**, executive vice president of the Southeast Alaska Regional Health Corp., from Juneau; **Raymond Demmert**, retired construction manager from Ketchikan; **Jim Edenso**, financial management consultant, from Bellingham, Wash.; **Alan Williams**, vice president loans for the Community Enterprise Development Corp., from Anchorage; and **Rosita Worl**, special assistant to Alaska Governor Cowper, from Anchorage.

Immediately following the meeting, the board of directors met and re-elected all officers of the corporation. The officers re-elected are **Marlene A. Johnson**, chairman of the board; **Raymond Demmert**, vice chairman of the board; **Byron I. Mallott**, chief executive officer; **William M. Howe**, president and chief operating officer; **William F. Strafford**, vice president finance and treasurer; **Robert W. Loescher**, senior vice president resource management; **Chris E. McNeil Jr.**, senior vice president and general counsel; **Robert Martin Jr.**, vice president administration; **Richard P. Harris**, vice president resource planning and administration; **Maxine H. Richert**, corporate secretary; **Edith E. McHenry**, assistant corporate secretary/shareholder services;

and **Doris Stevens**, assistant corporate secretary/office manager.

• **Rod Garriott**, Anchorage operations manager for McDonald Industries Inc., recently announced three personnel changes. **Bill Bovee** has joined the service department and will concentrate on component rebuild. Bovee has worked on products by Komatsu, Terex, Detroit Diesel, Allison, Caterpillar and Cummins. Early this year **Darren Folkers** joined McDonald as shop foreman. He will continue those duties, but with more emphasis on general repair projects. **John Gallipeo** has moved to parts supervisor with responsibility for day-to-day parts sales activities. Gallipeo's experience covers 20 years of automotive and construction equipment parts in Alaska.



ENGLAND



NIDOWICZ

• **Harding Lawson Associates** recently implemented a management staff change in its Anchorage branch office. **Jay England**, vice president-in-charge of the Anchorage office

since 1969, has been named to the new position of regional manager of HLA's corporate headquarters in Novato, Calif. England's regional duties will include operations and marketing responsibility for HLA branch offices in Northern California, Nevada, Alaska and Hawaii. **Bernard Nidowicz**, P.E., has been promoted to managing principal of the Anchorage office. Nidowicz is a registered professional engineer in Alaska and has been with HLA's Anchorage office since 1980. He has a master of science degree in civil engineering from the University of Alaska and specializes in geotechnical and arctic engineering.

• **George Woodbury** and **Jess Cline** have been appointed as corporate officers to Alaska Pulp Corp. The appointments were announced by **Frank Roppel**, executive vice president for the Sitka-based mill. The two new officers were appointed after the January retirement of vice president **Ryner**, who had 15 years of service with Alaska Pulp. Woodbury, now vice president, timber operations, came to Alaska Pulp in October 1986 from Ketchikan Pulp Co., where he served as logging manager and in other capacities for nearly 20 years. His new responsibilities include ensuring that the Sitka mill has raw materials (chips and logs), administering long-term sales and contracts of logging sites, and finding markets for sawmill logs. Cline becomes vice president, industrial relations. Prior to coming to Alaska Pulp eight years ago, he worked in labor relations positions for companies in Nebraska, Missouri, Kansas and Oregon. Presently, he oversees all personnel matters, including employment, wages, benefits, motivation and safety, as well as handling labor relations issues for the company.

• **Paul Ramert**, a senior in the civil engineering department at the University of Alaska, Anchorage, has received a \$1,000 scholarship from Construction Machinery Inc. and Ingersoll-Rand Inc. Money to fund the scholarship was made available through a cooperative effort made by Construction Machinery, an Anchorage heavy equipment firm, and Ingersoll-Rand, a manufacturer of heavy power tools. Ramert was born and raised in Anchorage and plans to use the scholarship to pursue a master's degree.



Dr. Robert Miller, UAA, observes as Paul Ramert, engineering student, receives a \$1,000 scholarship award from Ken Gerondale, president of Construction Machinery Inc.

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ANNUAL MAPPING AND SURVEYING CONFERENCE — At the Captain Cook Hotel, Anchorage; (907) 563-1867. Feb. 8-12.

WINTER CITIES SHOWCASE '88 — Theme is "The Business of Winter." Edmonton, Alta.; (403) 428-1988. Feb. 13-19.

SOIL COMPACTION SEMINARS — One-day seminars for contractors, engineers, architects and others involved in the design, construction and testing of compacted fills. In Phoenix, AZ, Feb. 25; Los Angeles, CA, March 3; Denver, CO, April 7; Anchorage, April 27.

SOCIETY OF PETROLEUM ENGINEERS SPE/IADC DRILLING CONFERENCE — Dallas, TX; (214) 669-3377. Feb. 28-March 2.

ASME OPEN FORUM ON CERTIFICATION — The American Society of Mechanical Engineers presents an open forum to assess need for and scope of certification of gas and hazardous liquids pipeline operators and/or inspectors. At the Marroitt Hotel, Dallas Fort Worth Airport, Dallas, TX, March 4.

ANNUAL TRANSPORTATION FORUM — "Future of Transportation into the 21st Century." Contact: Department of Conferences and Continuing Education, University of Alaska, Fairbanks; (907) 474-7800. March 4-5.

SOCIETY OF AMERICAN MILITARY ENGINEERS NORTHWEST REGIONAL CONFERENCE — At the Four Seasons Olympic Hotel, Seattle, WA. March 6-8.

Erratum

An article in the September 1987 issue entitled "Nome Mining Operations Ripe for a New Bonanza" incorrectly identified Inspiration Gold Inc. as based in Vancouver, B.C. The company is headquartered in Scottsdale, Ariz., and is a wholly owned subsidiary of New York-based Inspiration Resources Corp.

Inspiration Gold operates the Bima offshore dredge on private and state sea-floor lease holdings a mile seaward and about 3 mi. west of Nome. This, the world's largest dredge, began test operations during open-water season in 1986 and overwintered in Seattle where modifications were made and worn buckets replaced. The dredge worked a full test production season in 1987 and is wintering at the Port of Nome in anticipation of further underwater gold mining this summer.

The Bima is kept in place with one 20-ton head anchor and two 20-ton storm anchors. Its giant bucket line dredges the ocean floor in an arc along a cable line attached to four 14-ton swing anchors.

Inspiration bought the Bima in Indonesia from Billiton B.V. for considerably less than the \$33 million quoted in the article, according to company officials.

ALASKA CONTRACTING SUMMARY

More than twice the dollar volume in awards was reported in December than in November — \$34 million in December as opposed to \$14 million in November.

Twenty and a half million dollars in highway awards was the major factor in this recovery and most of the \$20 million was contributed by two awards, one for \$12 million and another for \$6 million.

At the end of 1987, the category of highway construction was \$65 million ahead of 1986. It is the only category to show significant improvement from the previous year.

The category of industrial commercial buildings was up \$4 million over 1986 and the miscellaneous category was up \$10 million. All other categories were down significantly from the previous year.

We finished 1987 at \$291 million from 1986.

CATEGORIES	DECEMBER	1987 TO DATE	1986 TO DATE
Airports	—	\$13,763,322	\$46,613,136
Electric Power	—	1,091,343	46,776,318
Highways	20,554,572	170,862,879	105,050,829
Industrial Commercial Buildings	2,906,591	29,098,777	25,003,272
Marine	1,078,596	19,274,664	28,864,369
Military	30,952	105,379,881	165,619,782
Petroleum	—	—	20,250,000
Public Buildings	6,684,168	86,577,484	229,576,287
Sewer and Water	715,337	22,307,535	82,197,137
Miscellaneous	1,756,265	30,354,113	20,206,269
TOTAL	\$33,915,316	\$478,798,842	\$770,177,399

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NEW PRODUCTS

Peterbilt Announces Electronic Dash

Peterbilt Motors Co. has announced the availability of a new electronic dash option for the recently introduced conventional line and COE models. The electronic dash represents the latest technology and is compatible with other electronic equipment.

Consisting of a large liquid crystal display panel and a separate keypad, the dash replaces all standard dash functions. Features include fuel economy monitoring and self-diagnostic capability for dash functions. The keypad allows the operator to select alternate panel functions and to perform calibrations.



For ease of visibility, all dash components are grouped together directly in front of the driver. Readouts on the panel are a combination of amber bar graphs and digital displays.

Panel functions consist of speedometer, tachometer, cruise speed indicator/speed alarm, instantaneous and average miles per gallon, fuel economy trend indicator, outside air temperature, odometer, trip odometer, fuel level, voltmeter, hourmeter, average trip speed, clock elapsed time, oil pressure, oil temperature and coolant temperature. A dual air-pressure gauge and warning lights are also standard. Up to 10 more regular size gauges may be added to customize the dash for specialized functions.

A fuel economy trend indicator shows the comparison between the instantaneous miles per gallon and the average miles per gallon by displaying either a red, yellow or green light. The operator can immediately make driving adjustments for improved fuel economy.

For more information, contact: Peterbilt Motors Co., P.O. Box 404, Newark, CA 94560; (415) 790-4035. □

Small Loader Does Big Things

Kawasaki Loaders Inc. has introduced the 65ZII, a 2.3-cu.-yd. machine that delivers quick response and powerful performance not seen in other loaders of comparable size, according to the manufacturer.

The 65ZII features the optional interchangeable toolcarrier system with coupler and attachments for multipurpose applications. The Isuzu 6BG1 engine provides greater horsepower, higher torque, improved fuel consumption and lower operat-

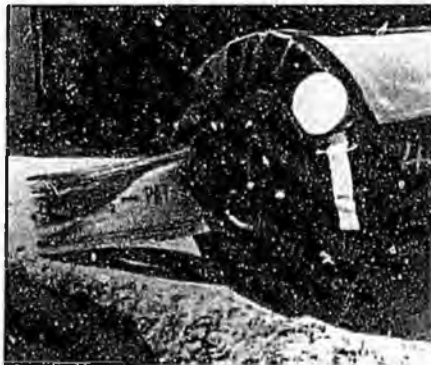


ing costs than previous Kawasaki loader engines.

The new ROPS cab offers excellent visibility, low sound levels and in-cab climate control system to maximize operator comfort and productivity. The hydraulic system has been made cleaner and cooler for increased reliability.

For more information, contact: Kawasaki Loaders Inc., 4041-E Kingston Ct., Marietta, GA 30067; (404) 953-0660. □

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Amoco Fabrics and Fibers Co. has introduced its Roll Handles as standard packaging on all woven and non-woven construction fabric rolls shipped to distributors and fabric end-users.

Roll Handles were designed to cut by half the time required to unload and handle construction fabric rolls on the job site. With these devices, contractors can handle fabric rolls much easier and unload them in the field without a forklift. Standard equipment on the job site can be used, cutting field unloading time by more than 50 percent and reducing equipment requirements.

Amoco offers a complete line of woven and non-woven construction fabrics that exceed all Task Force 25 standards. For more information, contact: Amoco Fabrics and Fibers Co., 900 Circle 75 Pkwy, Ste. 550, Atlanta, GA 30339; (404) 956-9025. □

New Dozer Blade from American Trencher

American Trencher Inc. has announced an eight-way Model 715 front dozer blade for the John Deere 755 and 855 compact hydrostatic tractors.

Designed for tough rental and contractor market duties, the dozer blade has hydraulic raise/lower, hydraulic angle, mechanical tilt and roll-out/roll-in capacities. The dozer blade is available with 52- or 60-in. moldboard widths and will mount with the JD underdeck mower, Bradco trencher and Bradco landscaper backhoes.

For more information, contact: American Trencher Inc., P.O. Box 266, Delhi, IA 52223; (319) 922-2981. □

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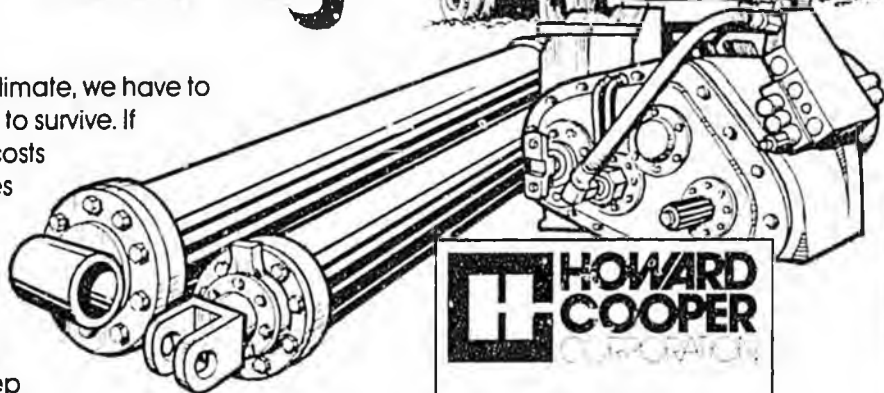
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ENROLLED

Regular Session, 1987

HOUSE BILL NO. 246

BY MR. M. HEBERT, MRS. BLANCO AND MR. GOMEZ AND SENATORS BAGERT,
CHABERT, KELLY AND LAURICELLA

ACT No. 895

AN ACT

To amend and reenact R.S. 30:148.2(1)(d) and R.S. 47:648.1(1)(d) and to enact R.S. 30:148.2(1)(e) and R.S. 47:648.1(1)(e) relative to the Louisiana Economic Acceleration Program, to provide for a spudding date of certified LEAP oil and natural gas well, to provide relative to certain set-asides and women-owned businesses, and to provide for related matters.

Be it enacted by the Legislature of Louisiana:

Section 1. R.S. 30:148.2(1)(d) is hereby amended and reenacted and R.S. 30:148.2(1)(e) is hereby enacted to read as follows:

§148.2. Definitions

Unless the context otherwise requires, the words defined in this Section have the following meaning when found in this Subpart:

(i) A "certified LEAP oil and natural gas well" is one so designated by the assistant secretary of conservation after a determination in accordance with rules promulgated under the Administrative Procedure Act that:

* * *

(d) The drilling operator has certified that, to the maximum extent possible, at least ten percent of the operator's service contracts related to the well have been made available to minority-owned businesses and that at least five percent have been made available to women-owned businesses.

(e) The well was spudded after January 1, 1986.

* * *

Section 2. R.S. 47:648.1(1)(d) is hereby amended and reenacted and R.S. 47:648.1(1)(e) is hereby enacted to read as follows:

§648.1. Definitions

Unless the context otherwise requires, the words defined in this Section have the following meaning when found in this Part:

(1) A "certified LEAP oil and natural gas well" is one designated as such by the assistant secretary of conservation after determining that:

* * *

(d) The drilling operator has certified that, to the maximum extent possible, at least ten percent of the operator's service contracts related to the well have been made available to minority-owned businesses and that at least five percent have been made available to women-owned businesses.

(e) The well was spudded after January 1, 1986.

* * *

SPEAKER OF THE HOUSE OF REPRESENTATIVES

PRESIDENT OF THE SENATE

GOVERNOR OF THE STATE OF LOUISIANA

APPROVED: _____

LOUISIANA DEPARTMENT OF NATURAL RESOURCES
OFFICE OF CONSERVATION
RULES OF PROCEDURE FOR THE ADMINISTRATION OF THE
LOUISIANA ECONOMIC ACCELERATION PROGRAM (LEAP)

December 1, 1986


The Assistant Secretary of the Office of Conservation, under the authority of Act 763 of the 1986 Regular Session of the Legislature, promulgates these rules of procedure for the administration of the Louisiana Economic Acceleration Program (LEAP).

1. A "Certified LEAP oil and natural gas well" (LEAP) well) is one designated as such by the Assistant Secretary of Conservation, Department of Natural Resources, following a public hearing and after determining that:
 - a) the well is a "discovery well" permitted as a "wildcat well" during the time period provided for herein, or a subsequent "developmental well" in the same field likewise during the time period provided for herein,
 - b) acceptance of a well by the Office of Conservation as a "wildcat well" for LEAP certification purposes shall not necessarily be determined by the field designation on the drilling permit issued by the Office of Conservation or the field name subsequently issued by the Office of Conservation, it being intended, however, to continue the same field name designations unless otherwise required under existing policy and regulations of the Office of Conservation.
2. A "wildcat well" is a well that is drilled, completed, and produced during the time period provided for herein from a pool which has not produced or known to have been capable of producing hydrocarbons in commercial quantities. A well drilled in a contiguous fault segment of a sand that was either producing or capable of production prior to July 1, 1986, or which is subsequently recompleted in a sand previously penetrated from a well that was drilled, completed, and/or produced prior to July 2, 1986, is not considered a wildcat well. Upon successful completion, the "wildcat well" is then recognized as a "discovery well."
3. A "developmental well" must be drilled and completed to a pool previously discovered by a "wildcat well."
4. The discovery well and subsequent developmental wells in the same field must be completed between July 1, 1986, and January 1, 1990, or the date on which the posted price of West Texas Intermediate of the United States bench mark crude equals or exceeds twenty-nine dollars and fifty cents per barrel, whichever occurs first.
5. The drilling operator must certify that Louisiana residents were employed to the maximum extent possible during exploration and production activities in connection with the well.
6. The drilling operator must certify that, to the maximum extent possible, at least ten per cent of the operator's service contracts related to the well have been made available to minority-owned businesses. A "minority-owned business" is one that is certified as such by the Governor's Office of Minority Business Development, P. O. Box 94095, Baton Rouge, Louisiana 70804-9095.

7. The application for LEAP well certification shall include:

- a) identification of the potential production zone, its depth, location, geology and engineering data. Such data must show that the production reservoir is geologically separated (structurally and/or stratigraphically) from the nearest reservoir that has produced, or known to have been capable of producing hydrocarbons,
 - b) in order to be geologically separated (structurally) and/or stratigraphically, submission of geological and engineering evidence supporting such classification and shall include electric logs, structure maps, isopachs, bottom hole pressure and production history. It is not intended to exclude from classification as wildcat wells those wells which are deepened and sidetracked in previously designated units, but recompleted in previously non-producing reservoirs located in such fields or units,
 - c) certification that, to the maximum extent possible, Louisiana residents were employed during the exploration and production activities undertaken in connection with the well,
 - c) certification that, to the maximum extent possible, at least ten (10%) per cent of the operator's service contracts related to the well were made available to minority-owned businesses.
- 8) If, after consideration of the application and the proceedings of a public hearing held to establish the well's status with regard to the LEAP well criteria, the assistant secretary determines the well qualifies as a LEAP well, he shall issue an order recognizing the well as a LEAP well.
- 9) Rules of Procedure shall be effective on or after December 20, 1986.

OFFICE OF CONSERVATION
OF THE STATE OF LOUISIANA


HERBERT W. THOMPSON,
COMMISSIONER OF CONSERVATION

**DONATIONS FOR WILDLIFE REFUGES, WILDLIFE MANAGEMENT
AREAS, AND PUBLIC HUNTING GROUNDS—
APPLICABILITY OF CERTAIN LAWS**

ACT NO. 36

SENATE BILL NO. 23

AN ACT

To enact R.S. 58:765; to provide that the provisions of R.S. 30:148.1 - 148.7 and R.S. 47:648.1 shall not authorize the breach of any term or condition of a donation which has been accepted by the state involving any state wildlife refuge, wildlife management area, or public hunting ground; and to provide for related matters.

Be it enacted by the Legislature of Louisiana:

Section 1. R.S. 58:765 is hereby enacted to read as follows:

5765. Donations for wildlife refuges, wildlife management areas, and public hunting grounds; applicability of certain laws

The provisions of R.S. 30:148.1 - 148.7 and R.S. 47:648.1 shall not authorize the breach of any term or condition of any donation which has been accepted by the state involving any state wildlife refuge, wildlife management area, or public hunting ground.

Section 2. This Act shall become effective upon signature by the governor or, if not signed by the governor, upon expiration of the time for bills to become law without signature by the governor, as provided by Article III, Section 18 of the Constitution of Louisiana.

Approved December 24, 1986.

SENATE BILL NO. 590

BY MR. NUNEZ AND REPRESENTATIVES M. HEBERT, LOWENTHAL AND
RUSSELL

ACT NO. 763

AN ACT

To enact Part I-C of Chapter 6 of Title 47 of the Louisiana Revised Statutes of 1950, to be comprised of R.S. 47:648 through 652, and Subpart A-2 of Part II of Chapter 2 of Title 30 of the Louisiana Revised Statutes of 1950, to be comprised of R.S. 30:148.1 through 148.7, relative to the Louisiana Economic Acceleration Program (LEAP); to provide for the Louisiana Economic Acceleration Program and a declaration of policy; to provide for definitions; to suspend severance tax on production from certified LEAP oil and natural gas wells; to dedicate severance tax revenues accruing from certified LEAP oil and natural gas well production; to establish the Louisiana Economic Diversification Fund and provide therefor; to suspend state natural gas royalties from certified LEAP oil and natural gas wells; to dedicate state oil production royalty revenues from certified LEAP oil and natural gas wells; to establish the LEAP Tax Warrant Fund and provide therefor; to dedicate state natural gas production royalty revenues from certified LEAP oil and natural gas wells; and to provide for related matters.

Be it enacted by the Legislature of Louisiana:

Section 1. Part I-C of Chapter 6 of Title 47 of the Louisiana Revised Statutes of 1950, comprised of R.S. 47:648 through 652, is hereby enacted to read as follows:

PART I-C. LOUISIANA ECONOMIC ACCELERATION PROGRAM,
SEVERANCE TAX SUSPENSION

§648. Louisiana Economic Acceleration Program (LEAP), declaration
of policy

A. In recognition of the need to accelerate Louisiana's economic recovery, ease unemployment and state fiscal problems, while providing a

funding mechanism for long-term economic diversification, the legislature hereby enacts the Louisiana Economic Acceleration Program (LEAP).

B. The Louisiana Economic Acceleration Program has three major components: the suspension of severance tax on oil and natural gas production from certified LEAP oil and natural gas wells and state natural gas royalties until January 1, 1990 or until the posted price of West Texas Intermediate, the United States benchmark crude, equals or exceeds twenty-nine dollars and fifty cents per barrel, whichever occurs first; a consumer natural gas incentive tax warrant to qualified Louisiana industries and utilities of five cents per thousand cubic feet of certified LEAP gas consumed in Louisiana in excess of 1985 natural gas consumption levels, which incentive is funded by the state's oil royalties from certified LEAP oil and natural gas wells; and a dedication of certified LEAP oil and natural gas well severance and royalty revenues to economic diversification upon resumption of collection on and after January 1, 1990 or the date on which the posted price of West Texas Intermediate, the United States benchmark crude, equals or exceeds twenty-nine dollars and fifty cents per barrel, whichever occurs first. Those revenues to be maintained in the Louisiana Economic Diversification Fund, for appropriation by the legislature.

C. The legislature further recognizes that the Louisiana Economic Acceleration Program will in no way:

- (1) affect existing mineral production in the state;
- (2) affect current oil or natural gas severance and royalty revenues; or
- (3) draw from the state general fund for tax incentives for the consumption of natural gas from a certified LEAP oil and natural gas well.

§649. Definitions

Unless the context otherwise requires the words defined in this Section have the following meaning when found in this Part:

(1) A "certified LEAP oil and natural gas well" is one designated as such by the assistant secretary of conservation after determining that:

(a) the well is a discovery well drilled as a wildcat well or a subsequent developmental well in the same field.

(b) the well was completed between July 1, 1986 and January 1, 1990 or the date on which the posted price of West Texas Intermediate, the United States benchmark crude, equals or exceeds twenty-nine dollars and fifty

cents per barrel, whichever occurs first, and

(c) the drilling operator has certified that Louisiana residents were employed to the maximum extent possible during exploration and production activities in connection with the well.

(d) the drilling operator has certified that, to the maximum extent possible, at least ten percent of the operator's service contracts related to the well have been made available to minority-owned businesses.

(2) A "wildcat well" is one so designated by the assistant secretary of conservation, drilled in search of oil or natural gas accumulations located in a non-productive area, away from a known productive geological structure.

(3) "Qualified industries and utilities" are ones so designated by the Department of Revenue and Taxation, based on a review of an application for a tax warrant incentive submitted within thirty days after the close of the fiscal year by a Louisiana industry or utility, in accordance with R.S. 30:148.6, certifying as to its 1985 natural gas consumption base load and, for the application year, its annual natural gas consumption, as well as its natural gas consumption from certified LEAP oil and gas wells.

(4) A "Louisiana resident" is a person who has resided in this state continuously for thirty days immediately prior to the effective date of employment.

§650. Severance tax suspension on production from certified LEAP oil and
natural gas wells

All severance taxes on production from certified LEAP oil and natural gas wells are hereby suspended until January 1, 1990 or until the posted price of West Texas Intermediate, the United States benchmark crude, equals or exceeds twenty-nine dollars and fifty cents per barrel, whichever occurs first. On and after January 1, 1990 or the date on which the posted price of West Texas Intermediate, the United States benchmark crude, equals or exceeds twenty-nine dollars and fifty cents per barrel, whichever occurs first, all production from certified LEAP oil and natural gas wells shall be subject to severance taxes as provided in Chapter 6 of Title 47 of the Louisiana Revised Statutes.

§651. Dedication of severance tax revenues accruing from certified LEAP oil
and natural gas well production

Beginning January 1, 1990 or as soon as the posted price of West Texas

Intermediate, the United States benchmark crude, equals or exceeds twenty-nine dollars and fifty cents per barrel, whichever occurs first, all severance tax revenues accruing from certified LEAP oil and natural gas well production shall be credited to the Louisiana Economic Diversification Fund, as provided in R.S. 47:652.

**§652. Department of Revenue and Taxation; Louisiana Economic
Diversification Fund**

A. Beginning January 1, 1990 or as soon as the posted price of West Texas Intermediate, the United States benchmark crude, equals or exceeds twenty-nine dollars and fifty cents per barrel, whichever occurs first, funds received by the Department of Revenue and Taxation, in the form of severance taxes on production from certified LEAP oil and natural gas wells shall be deposited immediately upon receipt into the state treasury.

B. After compliance with the requirements of Article VII, Section 9(B) of the Constitution of Louisiana relative to the Bond Security and Redemption Fund, and prior to moneys being placed in the state general fund, an amount equal to that deposited as required by Subsection A hereof shall be credited to a special fund hereby created in the state treasury to be known as the Louisiana Economic Diversification Fund. The moneys in this fund shall be used solely as provided by Subsection C hereof and only in the amounts appropriated by the legislature. All unexpended and unencumbered moneys in this fund at the end of the fiscal year shall remain in the fund. The moneys in this fund shall be invested by the state treasurer in the same manner as moneys in the state general fund, and interest earned on the investment of these moneys shall be credited to this fund, again, following compliance with the requirement of Article VII, Section 9(B) relative to the Bond Security and Redemption Fund.

C. The moneys in the Louisiana Economic Diversification Fund shall be used solely for statutorily defined economic diversification programs as appropriated by the legislature.

Section 2. Subpart A-2 of Part II of Chapter 2 of Title 30 of the Louisiana Revised Statutes of 1950, comprised of R.S. 30:148.1 through 148.7, is hereby enacted to read as follows:

SUBPART A-2. LOUISIANA ECONOMIC ACCELERATION PROGRAM (LEAP);

STATE ROYALTIES AND LEAP TAX WARRANT FUND

§148.1. Louisiana Economic Acceleration Program (LEAP), policy

A. In recognition of the need to accelerate Louisiana's economic recovery, ease unemployment and state fiscal problems, while providing a funding mechanism for long-term economic diversification, the legislature hereby institutes the Louisiana Economic Acceleration Program.

B. There are three major components to the Louisiana Economic Acceleration Program: the suspension of severance tax on oil and natural gas production from certified LEAP oil and natural gas wells and state natural gas royalties until January 1, 1990 or until the posted price of West Texas Intermediate, the United States benchmark crude, equals or exceeds twenty-nine dollars and fifty cents per barrel, whichever occurs first; a consumer natural gas incentive tax warrant to qualified Louisiana industries and utilities of five cents per thousand cubic feet of gas from certified LEAP oil and natural gas wells consumed in excess of 1985 natural gas consumption levels, which incentive is funded by the state's oil royalties from certified LEAP oil and natural gas wells; and a dedication of certified LEAP oil and natural gas well severance and royalty revenues to economic diversification upon resumption of collection on and after January 1, 1990 or the date on which the posted price of West Texas Intermediate, the United States benchmark crude, equals or exceeds twenty-nine dollars and fifty cents per barrel, whichever occurs first, those revenues to be maintained in the Louisiana Economic Diversification Fund, for appropriation by the legislature.

C. The legislature further recognizes that the Louisiana Economic Acceleration Program will in no way:

- (1) affect existing mineral production in the state;
- (2) affect current oil and natural gas severance and royalty revenues;

or

- (3) draw from the state general fund for tax incentives for the consumption of LEAP natural gas.

§148.2. Definitions

Unless the context otherwise requires the words defined in this Section have the following meaning when found in this Subpart:

(1) A "certified LEAP oil and natural gas well" is one so designated by the assistant secretary of conservation after a determination in accordance with rules promulgated under the Administrative Procedure Act that:

(a) the well is a discovery drilled as a wildcat well, or a subsequent developmental well in the same field; and

(b) the well was completed between July 1, 1986 and January 1, 1990 or the date on which the posted price of West Texas Intermediate, the United States benchmark crude, equals or exceeds twenty-nine dollars and fifty cents per barrel, whichever occurs first; and

(c) the drilling operator has certified that Louisiana residents were employed to the maximum extent possible during exploration and production activities in connection with the well.

(d) the drilling operator has certified that, to the maximum extent possible, at least ten percent of the operators service contracts related to the well have been made available to minority-owned businesses.

(2) A "wildcat well" is one so designated by the assistant secretary of conservation, drilled in search of oil or natural gas accumulations located in a non-productive area, away from a known productive geological structure.

(3) "Qualified industries and utilities" are ones so designated by the Department of Revenue and Taxation, based on review of an application for a tax warrant incentive, submitted within thirty days after the close of the fiscal year by a Louisiana industry or utility, in accordance with R.S. 30:148.6, certifying as to its 1985 natural gas consumption baseload and, in the application year, its annual natural gas consumption, as well as its natural gas consumption from LEAP wells.

(4) A "Louisiana resident" is a person who has resided in this state continuously for six months immediately prior to the effective date of employment.

§148.3. Suspension of state natural gas royalties from certified LEAP oil and natural gas wells

All state natural gas royalties on production from certified LEAP oil and natural gas wells are hereby suspended until January 1, 1990 or until the posted price of West Texas Intermediate, the United States benchmark crude, equals or exceeds twenty-nine dollars and fifty cents per barrel, whichever occurs first. On and after January 1, 1990 or the date the posted price of

West Texas Intermediate, the United States benchmark crude, equals or exceeds twenty-nine dollars and fifty cents per barrel, whichever occurs first, all production from certified LEAP oil and natural gas wells shall be subject to royalty collections as provided in Part II of Chapter 2 of Title 30 of the Louisiana Revised Statutes.

**§148.4. Dedication of state oil production royalty revenues
from certified LEAP oil and natural gas wells**

A. All state oil production royalty revenues accruing from certified LEAP oil and natural gas wells between July 1, 1986 and January 1, 1990 or the date on which the posted price of West Texas Intermediate, the United States benchmark crude, equals or exceeds twenty-nine dollars and fifty cents per barrel, whichever occurs first shall be credited to the LEAP Tax Warrant Fund, as provided in R.S. 30:148.5.

B. All state oil production royalty revenues from certified LEAP oil and natural gas wells accruing on and after January 1, 1990 or the date on which the posted price of West Texas Intermediate, the United States benchmark crude, equals or exceeds twenty-nine dollars and fifty cents per barrel, whichever occurs first, shall be credited to the Louisiana Economic Diversification Fund, as provided in R.S. 47:652.

§148.5. State Mineral Board; LEAP Tax Warrant Fund

A. Funds received by the State Mineral Board in the form of oil production royalty payments from certified LEAP oil and natural gas wells between July 1, 1986 and January 1, 1990 or the date on which the posted price of West Texas Intermediate, the United States benchmark crude, equals or exceeds twenty-nine dollars and fifty cents per barrel, whichever occurs first, shall be deposited immediately upon receipt into the state treasury.

B. After compliance with the requirements of Article VII, Section 9(B) of the Constitution of Louisiana, relative to the Bond Security and Redemption Fund, and prior to moneys being placed in the state general fund, an amount equal to that deposited as required by Subsection A hereof shall be credited to a special fund hereby created in the state treasury to be known as the LEAP Tax Warrant Fund. The moneys in this fund shall be used solely as provided by Subsection C hereof and only in the amounts appropriated by the legislature. All unexpended and unencumbered moneys in this fund at the end of the fiscal year shall be transferred to the Louisiana Economic

Diversification Fund. The moneys in this fund shall be invested by the state treasurer in the same manner as moneys in the state general fund, and interest earned on the investment of these moneys shall be credited to this fund again, following compliance with the requirement of Article VII, Section 9(B) relative to the Bond Security and Redemption Fund.

C. The moneys in the LEAP Tax Warrant Fund shall be used solely for transfers to the state general fund to cover tax warrants issued to qualified industries and utilities as incentives for the consumption of natural gas from LEAP wells, as provided in R.S. 30:148.6.

§148.6. LEAP Tax Warrants; issuance by Department of Revenue and Taxation; transfer of funds to the general fund; required appropriations

A. In accordance with the provisions of this Section, the Department of Revenue and Taxation shall issue tax warrants to qualified industries and utilities as an incentive to use natural gas from certified LEAP oil or natural gas wells between July 1, 1986 and January 1, 1990 or the date on which the posted price of West Texas Intermediate, the United States benchmark crude, equals or exceeds twenty-nine dollars and fifty cents per barrel, whichever occurs first.

B. Beginning at the end of fiscal year 1986-1987, and for the end of each fiscal year prior to January 1, 1990 or the date on which the posted price of West Texas Intermediate, the United States benchmark crude, equals or exceeds twenty-nine dollars and fifty cents per barrel, whichever occurs first, the Department of Revenue and Taxation shall calculate the tax warrants due to qualified industries and utilities for that fiscal year within sixty days of the close of the fiscal year. The amount of tax warrants due to a qualified industry or utility shall be equal to five cents per cubic feet of gas consumed by the qualified industry or utility during the fiscal year which is in excess of the 1985 natural gas consumption base load and which is equal to the amount of gas consumed by the qualified industry or utility during the fiscal year from certified LEAP oil and natural gas wells.

C. If the amount of tax warrants calculated for all qualified industries and utilities exceeds the total amount of the LEAP Tax Warrant Fund, the department shall make a pro rata reduction in the amount of tax warrants calculated for each qualified industry or utility.

D. The tax warrants shall be issued by the department within sixty days after the close of the fiscal year according to the calculations in this Section and the tax warrants shall be used as provided in Subsection F before the end of the fiscal year subsequent to issuance of the warrants.

E. Upon notification by the Department of Revenue and Taxation to the treasurer of the amount of tax warrants issued under this Section, the treasurer shall transfer an amount equal to the amount of tax warrants issued from the LEAP Tax Warrant Fund into the general fund.

F. The tax warrants may be used by the qualified industry or utility to pay any direct tax which is paid and remitted by the qualified industry or utility directly to the state or directly to a political subdivision of the state.

G. The legislature shall appropriate in each fiscal year sufficient funds to allow the treasurer to immediately honor and pay all warrants presented to the treasurer by a political subdivision of the state.

§148.7. Louisiana Economic Diversification Fund, state natural gas production royalty revenues from certified LEAP oil and natural gas wells

On and after January 1, 1990 or the date on which the posted price of West Texas Intermediate, the United States benchmark crude, equals or exceeds twenty-nine dollars and fifty cents per barrel, whichever occurs first, all state natural gas production royalty revenues accruing from certified LEAP oil and natural gas wells shall be credited to the Louisiana Economic Diversification Fund, as provided in R.S. 47:652, to be used solely for state economic diversification programs, as appropriated by the legislature.

Section 3. This Act shall become effective July 1, 1986.

PRESIDENT OF THE SENATE

SPEAKER OF THE HOUSE OF REPRESENTATIVES

GOVERNOR OF THE STATE OF LOUISIANA

APPROVED: _____



P.O. BOX 129 BARROW, ALASKA 99723
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HB 471

February 29, 1988

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The Honorable Max F. Gruenberg, Jr.
House of Representatives
Alaska State Legislature
Pouch V (Mail Stop 3100)
Juneau, AK 99811

Re: HB 471

Dear Representative Gruenberg:

The Arctic Slope Regional Corporation (ASRC) has recently received a copy of your proposed legislation on royalty and tax waivers referenced above. Although we have not had an opportunity to fully review this proposal, we would like to urge general support of the concept.

ASRC has consistently worked to ensure that smaller oil and gas fields on both State and private lands in Alaska are developed. We have been involved in the TAPS tariff proceedings for more than a decade, in large part because of our concern that the tariffs were too high and discouraged development of smaller deposits of oil and gas. Unfortunately, we are still having to litigate the TAPS tariff settlement. While fields of several hundred million barrels of oil may be large in lower 48 environments, this is not the case in remote areas of Alaska.

We support your efforts to help ensure that valuable resources can be developed in smaller fields on State oil and gas leases. This is particularly important at this point in our State's economy when resource development activity needs critical encouragement. Waiver of royalties and taxes to help get a field into production should provide benefit to the State and its residents in the long term.

Very truly yours,

Jacob Adams, President
ARCTIC SLOPE REGIONAL CORPORATION

cc: Representative Al Adams
Representative Adelheid Hermann
Representative Sam Cotten