

SB

510

SENATE COMMITTEE REPORT

FIRST COMMITTEE OF REFERRAL

Date of _____ 5-DAY NOTICE
IN ACCORDANCE WITH UNIFORM RULE 23

FURTHER: FINANCE

**FISCAL NOTE(S) ATTACHED _____ **
IN ACCORDANCE WITH AS 24.08.035
(see below)

4/19/33 DATE TURNED INTO OFFICE _____
Mr. President:

RESOURCES _____ Committee considered SB 510

ceiling on the state's royalty rate on coal leases; efd

and recommended:

- replace with CS _____ same title
- attached amendment(s) and new title
- do pass
- do not pass
- no recommendation
- individual recommendations
- further referral to _____
- letter of intent adopted and attached
- ** Committee attached or adopted fiscal note(s)
 zero fiscal impact

MEMBERS SIGNING DO PASS

[Signature]

OTHER RECOMMENDATIONS

[Signature] No Rec
[Signature] No Rec

[Signature]

 Chairman signature and recommendation

Committee Backup Attached

STATE OF ALASKA

DEPARTMENT OF NATURAL RESOURCES

OFFICE OF THE COMMISSIONER

STEVE COWPER, GOVERNOR

400 WILLOUGHBY AVE.
JUNEAU, ALASKA 99801-1798
PHONE: (907) 486-2400

April 8, 1988

Mr. Joseph Usibelli, Jr.
Usibelli Coal Mine, Inc.
P.O. Box 1000
Healy, Alaska 99743

Dear Mr. Usibelli:

The Department of Natural Resources has carefully reviewed Usibelli Coal Mine, Inc.'s (UCM), request for royalty relief for coal leases ADL 20633 and 31543.

The Commissioner of the Department of Natural Resources has the discretion to waive, suspend, refund, or reduce the royalty under two circumstances:

- (1) if she finds that such a reduction is necessary to promote development; or
- (2) if she finds the lease cannot be successfully operated at the royalty level.

Usibelli Coal Mine based its request for royalty relief on the "necessary to promote development" provision and did not assert that the operation cannot be successfully operated with the increased royalty. Therefore, our analysis was limited to the consideration of whether a royalty reduction is necessary to promote development.

Generally, requests for royalty reduction in order to promote development are granted as an incentive to extract resources not recoverable under current operating practices. In this instance, the argument has been made that an increase in royalty, as required by regulations adopted by the Department in 1982 (see 11 AAC 85.220) will adversely affect future development.

UCM has been paying a coal royalty of 5¢ per ton on one lease and 10¢ per ton on a second lease, for an average royalty of 7.5¢ per ton. This rate equals less than one-half of one percent of adjusted gross value.

Mr. Joseph Unibelli, Jr.

-2-

April 8, 1988

Under the 1982 regulations, all coal leases issued or renewed by the State of Alaska must include a minimum royalty of 5 percent of adjusted gross value (5 percent AGV).

UCM requested a royalty rate equivalent to 1.5 percent adjusted gross value (1.5 percent AGV).

The issue becomes whether the 5 percent AGV royalty rate is reasonable in terms of both a fair return to the state and in terms of promoting development. In this regard, it is helpful to note that coal royalty in New Mexico is 12.5 percent of all revenues; Montana's rate is 12.5 percent of gross value; and Wyoming's coal royalty is 12.5 percent of the selling price. The current royalty for federal coal leases is 12.5 percent AGV.

In comparison, the Department finds that Alaska's lower royalty of 5 percent AGV provides both a fair return to the state, while recognizing the competitive advantage necessary for our emerging coal export industry.

Therefore, the Department cannot grant the full permanent reduction in royalty relief as requested by UCM. The information provided did not demonstrate that such a reduction for leases ADL 20633 and 51545 is necessary to promote development. However, our analysis indicates that an immediate increase in royalty as set out in regulation will put an unreasonable burden on UCM and your customers. Therefore, we find that a phased increase to the full royalty is warranted.

Under the authority granted by AS 38.05.140(d), the Department will phase in the 5 percent AGV royalty over a period of three years, as outlined in the schedule below:

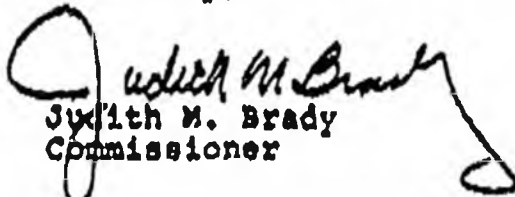
<u>LEASE</u>	<u>FOR THE PERIOD</u>	<u>ROYALTY</u>
ADL 20633	Nov. 1, 1987 - April 30, 1988	\$0.29/ton
	May 1, 1988 - April 30, 1989	\$0.60/ton
	May 1, 1989 - April 30, 1990	\$0.90/ton
	After May 1, 1990	5% AGV
ADL 51545	May 1, 1987 - April 30, 1988	\$0.29/ton
	May 1, 1988 - April 30, 1989	\$0.60/ton
	May 1, 1989 - April 30, 1990	\$0.90/ton
	After May 1, 1990	5% AGV

Further, the Department will grant your request for a partial refund of royalties paid at the 5 percent AGV rate during the period from May 1, 1987, for ADL 51545 and from November 1, 1987, in order to be consistent with the phased payment schedule. Such refund will be taken as credit against future royalty payments. The Division of Mining will contact you soon to outline this procedure.

Mr. Joseph Usibelli, Jr. ... -3-

April 8, 1988

Sincerely,

A handwritten signature in cursive script that reads "Judith M. Brady". The signature is written in dark ink and is positioned above the typed name and title.

Judith M. Brady
Commissioner

cc: Gerald Gallagher, Director
Division of Mining

USIBELLI COAL MINE, INC.
P.O. Box 1000
Healy, Alaska
99743

5 February 1988

Senator Jack Coghill
Alaska State Legislature
P.O. Box V (MS 3100)
Juneau, Alaska 99811

Dear Senator Coghill:

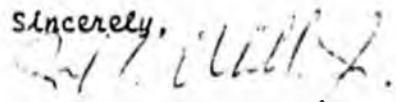
Usibelli Coal Mine Incorporated has filed the necessary documents with the Department of Natural Resources to pursue a reduction in royalty for two producing leases in the Healy area, ADL 20633 and ADL 21545. The formal request has been made to set the rate per ton at .29 cents.

Current regulations, 11 AAC 85.220(b), require royalty be paid at the rate of five percent of adjusted gross value of the coal. This estimate may be converted to a cents per ton figure, which currently equates to approximately .96 cents per ton. This represents a sizable increase from the established rate of .05 and .10 cent per ton rate previously paid on the respective leases.

This change in royalty rates, coupled with an increase on the lease rental which swelled from one dollar to three dollars per acre, will have major impacts both in the short and long term. Price adjustments of this magnitude would lead to an immediate decline in development, and most definitely would jeopardize our current export contract.

A copy of the original request to the Division of Mining concerning this subject has been enclosed. I would be exceedingly grateful if you would write the Division Director, Mr. Gerry Gallagher, lending your support for granting the reduction in royalty for these leases.

Sincerely,


Joseph E. Usibelli Jr.
PRESIDENT

JEUf:cpb

19 October 1987

Coal Royalty Reduction

Alaska statute 38.05.140(d) establishes the criteria to be considered in dealing with a request for royalty reduction. The law in part states the following. "The commissioner for the purpose of encouraging the greatest ultimate recovery of coal, and in the interest of conservation of natural resources, after public hearing, may waive, suspend, refund or reduce the rental or minimum royalty,, whenever (1) the commissioner determines that it is necessary to do so in order to promote development OR (2) that the lease cannot be successfully operated under its terms."

The companion or implementing regulations located in 11 AAC 82.665 only address the statute as expressed in section (2), where a lease cannot be successfully operated within its terms. The aspect of promoting development is never touched upon or eluded to by the regulation.

In lieu of the foregoing, the case is pled to the commissioner outside the requirements found in the regulation 11 AAC 82.665. The request as presented will utilize a number of administrative file papers dating from 1980 and 1981, when the coal leasing and royalty regulations were being tampered with.

The first exhibit is a paper titled "Alaska's Coal Leasing Program" authored by Laurel A. Murphy of ADNR in November of 1980. Presented as part of the first paragraph is the mention of a felt need to reform the State's coal management program. The first three pages explore the inconsistent approach shared between the administration and the legislature in making changes to the coal program. Pages four through ten form the ADNR view of the necessary changes that will need to be addressed when the drafting of coal regulations are finally proposed.

In August of 1981 a study group of cabinet level officials under the direction of then Governor Jay Hammond issued a report #141 which dealt with the taxation and royalty sections of the coal regulations. Immediately a response was issued by Mr. William Noll of Suneel Alaska Corp. and by an industry group of coal operators and leaseholders. Both documents have been included for your reference.

Although the coal industry fought the hard fight during administrative hearings on the royalty issue, the State stood by their post and adopted the 5% of adjusted gross value standard. If we view the study #141 and the response by industry, only one paper can be claimed prophetic in nature.

A frustrated attempt was made to compare taxation policies for coal with that of the oil industry. After the drop in oil prices the last two years, the elected and the governed of Alaska quickly realized that revenues generated by oil production can never be matched or replaced by another industry either severally or collectively.

The term "maximum benefit" to Alaskans was a prevalent theme of the Hammona study, but the position paper of the industry group differs with the interpretation. Tax dollars as the benefit versus year round jobs was never fully evaluated.

Alaska is now and will be recognized into the next century as one of the potential suppliers of large quantities of coal to the Pacific Rim. However, what must be remembered is that the fragility of that marketplace is determined by the product price as delivered at the bussbar.

Usibelli Coal Mine in concert with Suneel Alaska broke a barrier when the first shipload of coal reached Korea. This marked the first sub-bituminous coal ever sold in the international marketplace. Current royalty increases have strained this relationship, and dramatic price increases could lead to the contract being cancelled. The same principle could also impact present negotiations to supply coal to Taiwan. Is this a benefit for the Alaskan people? Loss of jobs both at the mine and port facilities, coupled with those in support businesses, would be looked upon unfavorably by a majority.

The issue at hand is the same that existed in 1981; too much too soon. There remains in 1987 one sole producer of coal in Alaska. Flawed thinking still permeates many minds of those desiring to compare our taxation policies and other regulatory requirements with the western United States. The true facts are that we mine a product of lower quality on a BTU basis, have much higher cost in compliance with ASMCRA and other programs, all which tend to remove us from our competitive position in world markets. Results of in-state impacts to Alaskan consumers can't be discounted either.

The State must make a decision as to what is in the "best interest" of Alaskans. A look in retrospect points to the fact that the industry has to expand before you seek to extract revenue from them.

Coal Royalty Reduction
October 19, 1987
Page 3

The facts are plain as they relate to development. If the current markets are turned away, then development is surely impacted. Based upon sound and prudent principles, we seek your intervention in this request for royalty relief.

Should you desire to discuss this matter further, please don't hesitate to contact me.

Sincerely,

Joseph E. Usibelli Jr.
PRESIDENT

JEU:nms



Official Business

Alaska State Legislature

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

February 17, 1988

Jerry Gallagher, Director
Division of Mining
Department of Natural Resources
P.O. Box 107016
Anchorage, AK 99510-7016

Dear Mr. Gallagher:

We are writing in support of Usibelli Coal Mine, Inc.'s (UCM) request for a reduction in royalty for their two producing leases in Healy. After reviewing their request, we believe it has merit.

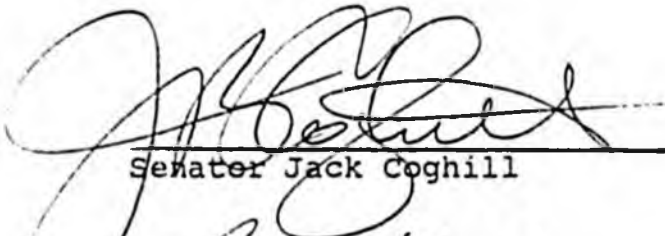
Current royalty regulations may well have a detrimental short and long term effect on UCM. Its export contract could be jeopardized and further development could decrease. Alaska statute allows the Commissioner of the Department of Natural Resources to waive, suspend, refund, or reduce the royalty to promote development or if the lease cannot be successfully operated under its terms. The "best interest" of Alaska is to keep our one existing coal mine producing.

The royalty rate should not be at a level that makes the product noncompetitive, especially considering the growth potential for the business in export markets. At the level requested by Usibelli, \$.29/ton, the product would be competitively priced in the current marketplace. Continued development, foreign and domestic, can take place and a steady, secure supply of coal for the Interior would be assured. A reduction means retaining jobs at the mine, the loading facility, and in the support industry and it means the potential for additional employment in the coal mining and related industries.

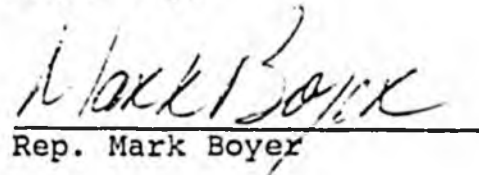
page two
Mr. Jerry Gallagher
February 17, 1988

Please make our comments part of the hearing records. Thank you for the opportunity to participate in this important decision.

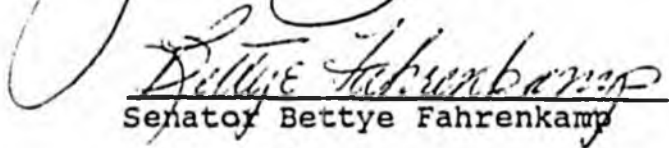
Sincerely,



Senator Jack Coghill



Rep. Mark Boyer



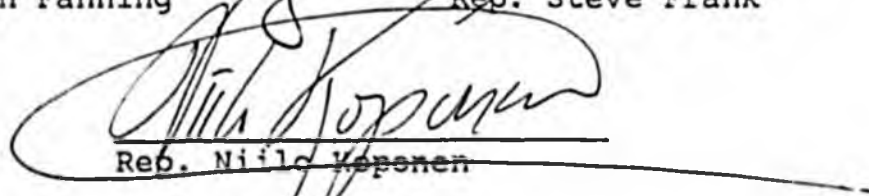
Senator Bettye Fahrenkamp



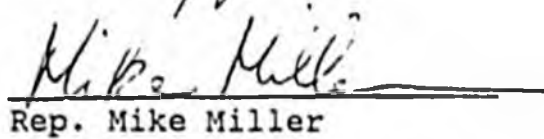
Senator Ken Fanning



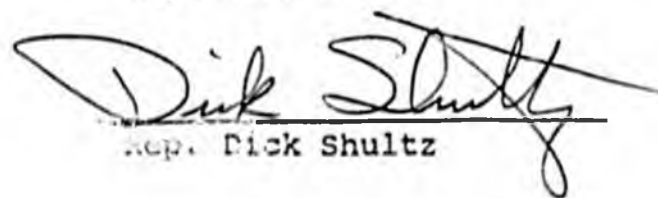
Rep. Steve Frank



Rep. Niilo Kopenen



Rep. Mike Miller



Rep. Dick Shultz

Alaska State Legislature

PRESIDENT

907-465-3755



MAR 1 1988

JAN FAIKS
POST OFFICE BOX V
JUNEAU, ALASKA 99811

Senate

February 25, 1988

Jerry Gallagher
Director
Division of Mining
Department of Natural Resources
Post Office Box 107016
Anchorage, Alaska 99510-7016

Dear Mr. Gallagher:

The coal industry is an important sector in Alaska's economy. Alaska contains 40 percent of the nation's known coal reserves, and yet currently our production accounts for only 0.2 percent of the total annual U.S. production.

The greatest opportunity for expansion of the coal industry in Alaska is through export. One of the key factors impacting the competitiveness of Alaskan coal in international markets is cost.

Current regulations (11 AAC 85.220(b)) require royalty to be paid at the rate of five percent of adjusted gross value of the coal, which currently equates to \$.96 per ton, and represents a substantial increase from previously established rates. This royalty increase has negatively impacted the cost competitiveness of Alaskan coal, and could have a further detrimental effect on the expansion of export markets for Alaskan coal.

For these reasons, I strongly urge the Department of Natural Resources to grant Usibelli Coal Mine's request to set the royalty rate at \$.29 per ton. The gains in employment and economic activity which will result from this change are definitely in the State's best interest, and are crucial to the further development of the Alaskan coal and support industries.

The economic future of Alaska depends upon the development of a strong and diversified private sector. The State of Alaska absolutely must continue to work as a partner with

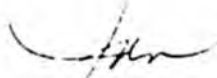
OUT OF SESSION

3111 C STREET, SUITE 525 ANCHORAGE, ALASKA 99503 907-561-7610

7

the coal industry in order to create more new jobs and economic activity at a time when the people of Alaska need it the most.

Sincerely,



Jan Faiks
Senator

cc: Commissioner Brady

JF:dp

SB 509: "An Act relating to the termination date, members, and reports of the Alaska Minerals Commission; and providing for an effective date."

Background: The Minerals Commission was created by the 1986 Legislature and established in the Department of Commerce and Economic Development. Administrative support for the commission is provided by the Division of Business Development.

The commission was charged under statute to make recommendations to the Legislature and the Governor on ways to mitigate constraints on the development of minerals in the state. The commission has complied with that legislative mandate by drafting and submitting two reports to the Governor and the Legislature.

Many of the commission's legislative recommendations have been introduced in bills during the 1987 and 1988 legislative sessions and many of the commission's administrative recommendations have been the subject of review and adoption by state agencies. The legislative and administrative response to the commission's recommendations is strong evidence that the commission has taken its statutory directive seriously and responded effectively.

Alaska's mineral industry has begun a recovery and there is enormous potential for the emergence of a dramatically expanded and productive mining sector over the next five to ten years: a time when the state's economy critically needs growth in its nonpetroleum sectors. The advisory role of the Alaska Minerals Commission will continue to be valuable to the Legislature and the administration during this period.

Position: While the department has provided support through personal services, it is not capable of supporting travel and contractual services for commission members and staff. A Fiscal Note for \$22.5 for contractual and travel has been submitted. It is also noteworthy that the commission has been partially supported by the private sector as individual commission members and their companies have often funded travel and per diem of members.

The Department of Commerce and Economic Development feels the Minerals Commission has served the state well and supports SB 509 to extend the commission's time of service.

Kathy Marshall for

J. Anthony Smith, Commissioner
Department of Commerce and
Economic Development

4/22/88

Date

STATE OF ALASKA
1988 LEGISLATIVE SESSION

BILL VERSION: SB 510
PUBLISH DATE: _____

FISCAL NOTE

REQUEST: _____

Revision Date: _____ Agency Affected: _____
 Title: SB 510 An Act relating to a ceiling BRU: Minerals Management
on the state's royalty rate on coal leases
 Sponsor: Fahrenkamp Components: _____
 Requestor: Senate Resources

EXPENDITURES/REVENUES: (Thousands of Dollars)

OPERATING	FY 88	FY 89	FY 90	FY 91	FY 92	FY 93
PERSONAL SERVICES	0	0	0	0	0	0
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	0	0	0	0	0	0

CAPITAL	0	0	0	0	0	0
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REVENUE	0	0	0	0	0	0
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FUNDING: (Thousands of Dollars)

GENERAL FUND	0	0	0	0	0	0
FEDERAL FUNDS						
OTHER						
TOTAL						

POSITIONS:

FULL-TIME	0	0	0	0	0	0
PART-TIME						
TEMPORARY						

ANALYSIS : (Attach a separate page if necessary)

The Department of Natural Resources anticipates no additional expenditures will be necessary to implement this legislation, however, there will be revenue impact, as discussed on the attached sheet.

Prepared by: Lawrence Ostrovsky Phone: 4/21/88
 Division: Commissioner's Office Date: 465-2400

Approved by Commissioner: [Signature] Date: 465-2400
 Agency: Department of Natural Resources

Distribution (by preparer):
 Legislative Finance
 Legislative Sponsor
 Requestor
 Office of Management and Budget
 Impacted Agency(ies)

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Fiscal Impact of SB 510

Year	Coal Tonnage	Producers	3E ACV Revenue	SB 510 Revenue	Annual Revenue Loss	Cumulation Revenue Loss
1988	1,600,000	UCH	\$1,536,000	\$480,000	\$1,056,000	\$1,056,000
1989	1,600,000	UCH	\$1,536,000	\$480,000	\$1,056,000	\$2,112,000
1990	1,600,000	UCH	\$1,536,000	\$480,000	\$1,056,000	\$3,168,000
1991	2,600,000	UCH and Washburn	\$2,496,000	\$780,000	\$1,716,000	\$4,884,000
1992	2,600,000	UCH and Washburn	\$2,496,000	\$780,000	\$1,716,000	\$6,600,000

Prepared by: TWR Division of Mining
April 22, 1988



Alaska State Legislature

SENATE SPECIAL COMMITTEE ON OIL AND GAS

SENATOR BETTYE FAHRENKAMP
CHAIRMAN
SENATOR JACK COGHILL
SENATOR PAUL FISCHER

P.O. BOX V
JUNEAU, AK 99811
(907) 465-3834

M E M O R A N D U M

TO: Senator Coghill, Chairman
Senate Resources Committee

FROM: Senator Bettye Fahrenkamp, Chairman *BF*
Senate Special Committee on Oil and Gas

RE: SB 510, An Act relating to a ceiling on the state's
royalty rate on coal leases; and providing for an
effective date.

DATE: April 22, 1988

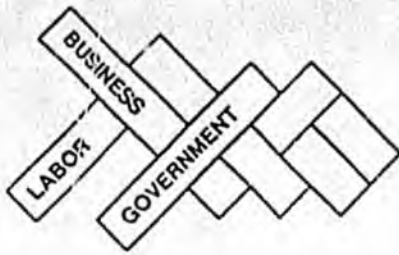
Thank you for scheduling SB 510.

Current statutes require state royalties to be paid for the privilege of mining or extracting coal. Royalty rates are not permitted to be set lower than five cents per ton. However, a maximum rate has not been set. This lack of legislative direction has allowed the Department of Natural Resources to establish, by regulation, royalty rates of five percent of adjusted gross value.

SB 510 would require that the existing methodology of setting coal royalty rates on a cents per ton basis be maintained, and would establish a ceiling of thirty cents per ton for all coal leases.

This kind of stability in setting royalty rates will encourage continued coal production and development for both foreign and domestic markets.

Thank you for your consideration.



MAR 3 1988
UNIFIED FAIRBANKS

**UNIFIED FAIRBANKS
RESOLUTION URGING RESTRAINT IN LEVYING
INCREASED ROYALTIES ON COAL**

WHEREAS, the State of Alaska is proposing to collect royalties on coal produced by the Usibelli Coal Mine which represents an increase from approximately .08 per ton (current average) to 0.98 per ton (an increase of approximately 12%); and,

WHEREAS, such an increase could be passed along to the Alaska Railbelt consumer in the form of higher electricity and heating rates; and,

WHEREAS, an increase of this magnitude could price Usibelli coal out of the export markets which have earned for Alaska a total of \$78 million dollars since exports to South Korea commenced in 1985; and which are critical to the financial well being of the ARR; and

WHEREAS, the royalty increases are in addition to rental on acreage, mining license taxes and corporate taxes are paid by Usibelli Coal Mine to the State of Alaska.

NOW THEREFORE BE IT RESOLVED, that UNIFIED FAIRBANKS urges restraint in levying royalties on coal produced by Usibelli Coal Mine at Healy. Royalty rates should be maintained at present levels, especially in view of the difficult international market conditions.

This resolution was passed at the meeting of Unified Fairbanks on Tuesday, February 23, 1988.

Sincerely,

UNIFIED FAIRBANKS


Charles P. Rees, President

CPR:slg:resolution 2-25-88:UFMN2