

HB

242

HFIN

FILE

HOUSE COMMITTEE REPORT

(11)

Date Referred to Committee: April 10, 1997

FURTHER REFERRALS:

Date of Committee Action: 4/24/97

The FINANCE Committee considered:

HB 242

HOUSE BILL NO. 242

ROYALTY/NET PROFIT SHARE PAYMENT

"An Act relating to unpaid, underpaid, and overpaid royalty and net profit share payments due on leases of state land and to the collection and payment of interest on those payments."

recommends it be replaced with the following committee substitute _____ [] the same title
 [] a new title

[] additional referral to _____ Committee
 [] attached amendment(s)

ADOPTS: _____ Letter of Intent

ATTACHES NEW FISCAL NOTE(S): (Dept) _____ APPROVES PREVIOUS: (Dept/Date) _____

[] fiscal note(s) _____ [] fiscal note(s) _____

[] zero fiscal note(s) DNR [] zero fiscal note(s) _____

SIGNING WITH RECOMMENDATIONS		DP	DNP	NR	AM
<i>Gene Therriault</i>	Therriault	X			
<i>Chuck Milder</i>	MILDER	X			
<i>Larry Martin</i>	martin	X			
<i>John & James</i>	J. DAVIS	X			
<i>W. Moses</i>	MOSES	X			
<i>Henry G. Daus</i>	g. Daus	X			
<i>Vicki Kelly</i>	Kelly	✓			
<i>Mark Hanley</i>	Hanley	X			
<i>Vic Kohring</i>	Kohring	X			

CO CHAIR'S SIGNATURE *Gene Therriault* *Mark Hanley*
 Therriault Hanley

FISCAL NOTE

STATE OF ALASKA
1997 LEGISLATIVE SESSION

BILL NO. HB242

Revision Date: _____ Dept Affected: Natural Resources
 Title: An Act relating to unpaid, underpaid, and BRU: Resource Development
overpaid royalty and net profit share payments due on leases... Component: Oil and Gas Development
 Sponsor: Special Committee on Oil & Gas
 Requestor: (H)FIN Component Serial No. #439

Expenditures/Revenues	(Thousands of Dollars)					
	FY98	FY99	FY00	FY01	FY02	FY03
OPERATING EXPENDITURES						
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0
CAPITAL EXPENDITURES	0.0	0.0	0.0	0.0	0.0	0.0
CHANGE IN REVENUES ()	0.0	0.0	0.0	0.0	0.0	0.0

FUND SOURCE	(Thousands of Dollars)					
1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1037 GF/Mental Health						
Other						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

Estimate of any current year (FY97) cost: \$ none

POSITIONS	FY98	FY99	FY00	FY01	FY02	FY03
FULL-TIME	0	0	0	0	0	0
PART-TIME	0	0	0	0	0	0
TEMPORARY	0	0	0	0	0	0

ANALYSIS: (Attach a separate page if necessary)

The staff who process the monthly royalty adjustments will use the time freed up from processing interest calculations on relatively 'minor' royalty adjustments to focus on larger royalty revenue issues. No new positions or expenditures are requested. No significant change in revenues can be identified at this time. Adjustments affected by this bill can be positive or negative for both the state and the lessees paying royalties. Historically, there has been no significant gain or losses in revenues due to interest payments on the types of adjustments affected by this bill. The changes proposed in the bill would allow staff to spend their time on activities that have the potential to generate revenue.

Prepared by: Ken Boyd, Director Phone: 269-8800
 Division: Oil and Gas Date: 15-Apr-97
 Approved by Commissioner: [Signature] Date: 4-15-97
 Agency: Natural Resources

ALASKA STATE LEGISLATURE

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REPRESENTATIVE MARK D. HODGINS
House District 9

Sponsor Statement HB 242

“An Act relating to unpaid, underpaid, and overpaid royalty and net profit share payments due on leases of state land and to the collection and payment of interest on those payments.”

HB 242 is designed to increase efficiency on how the Department of Natural Resources operates by amending the interest statutes as it pertains to oil & gas royalties. The intent of this change is to reduce the administrative workload and the cost for administering minor oil & gas royalty adjustments.

HB 242 is written in a manner that would strictly limit the type of oil & gas royalty transactions excluded from interest changes and then for only 30 days following the date of the payment. The types of royalty transactions targeted by **HB 242** are generally cleared up within 30 to 60 days of the due date. Normal oil & gas transactions cannot always be completed within 30 days of the production month causing frequent adjustments with 30 to 60 day period after the production month.

Research has been done to show that the cost of processing an adjustment averages \$75.00 per transaction. Add to that the application of oil interest and the transaction cost can be as high as \$150.00. Processing an interest transaction of a lesser value than the out-of-pocket cost is not in the state's best interest. The interest earned on an under or overpayment of \$16,000.00 is approximately \$150.00 which basically equals a “wash” with our administrative costs.

HB 242 will create a more cost-effective method of collecting oil royalties.

TYPICAL: OVER/UNDER-PAYMENT AMOUNTS

Annual Interest Rate Compounded Quarterly: 11%

Interest earned on \$150.00 or less:

In 30 days: \$1.38

In 60 days: \$2.75

In 90 days: \$4.13

Cost to process an underpayment or overpayment: \$150.00

NET RETURN in 30 days: \$1.38 Interest - \$150.00 Cost = -\$148.62

BREAK-EVEN CASE : OVER/UNDER-PAYMENT AMOUNTS

Annual Interest Rate Compounded Quarterly: 11%

Interest earned on \$16,000.00 :

In 30 days: \$146.67

In 60 days: \$293.33

In 90 days: \$440.00

Cost to process an underpayment or overpayment: \$150.00

NET RETURN in 30 days: \$146.67 Interest - \$150.00 Cost = -\$3.33

"A: a game of chance or skill made under AS 06.16,
 710: a permanent fund dividend under AS 43.23,
 711: a coin-operated device or punchboard under
 AS 43.36 or

712: a child support obligation under AS 25.27."
 Section 18(a) and (c), ch 108, SLA 1990 provide as follows: "a) The remedies and procedures provided by this Act apply to all revenue tax appeals in which a request for formal hearing is filed with the Department of Revenue on or after the effective date of this subsection. The remedies and procedures existing before the effective date of this subsection apply in all revenue tax appeals in which a request for formal hearing is filed with the Department of Revenue

before the effective date of this subsection, unless all of the parties to an appeal agree in writing to the remedies and procedures established by this Act.

"b) Until ASAA 1981(1), ASAA 1982(1) and other Department of Revenue regulations in effect on the effective date of this subsection are revised as necessary, those regulations continue to govern an administrative appeal of a Department of Revenue decision not within the jurisdiction of the office of tax appeals, including a decision regarding a

713: game of chance or skill under AS 06.16;
 721: permanent fund dividend under AS 43.23, and
 722: coin-operated device or punchboard under AS 43.36."

NOTES TO DECISIONS

Cited in *Principal Mut Life Ins Co v State, Div of Ins*, 790 P.2d 1023 (Alaska 1990).

Collateral references. — When right to refund of state or local taxes accrues within statutory limiting time for applying for refund. 4A ALR2d 1360.

Sec. 43.05.280. Interest on overpayments. (a) Interest shall be allowed and paid on an overpayment of a tax under this title at the rate and in the manner provided in AS 43.04.226(1).

(b) Interest shall be allowed and paid as follows:

(1) in the case of a credit, from the date of the overpayment to the due date of the amount against which the credit is taken;

(2) in the case of a refund, from the date of the overpayment to a date, as determined by the department, preceding the date of the refund check by not more than 30 days, whether or not the refund check is accepted by the taxpayer after tender of the check to the taxpayer; the acceptance of the refund check does not affect the right of the taxpayer to claim an additional overpayment and interest on the overpayment.

(c) If an overpayment of a tax imposed by this title is refunded within 90 days after the last date prescribed for filing the return of the tax, determined without regard to an extension of time for filing the return, or if the return is filed after the last filing date and the overpayment is refunded within 90 days after the date the return is filed, interest may not be allowed under (a) of this section on that overpayment. (§ 1 ch 94 SLA 1976; am § 3 ch 82 SLA 1982; am § 3 ch 23 SLA 1991)

Effect of amendments. The 1991 amendment, titled "rate and in the manner provided in AS effective October 31, 1991, in subsection (a), substituted "43.05.226(1)" for "rate prescribed in AS 43.05.225."

NOTES TO DECISIONS

Applied in *North Slope Borough v Sohio Petroleum Corp*, 545 P.2d 634 (Alaska 1976).

Collateral references. — Right to interest on income tax refund or credit in absence of specific controlling statute. 44 ALR2d 616.

Sec. 43.05.290. Criminal penalties. (a) A person who wilfully attempts to evade a tax imposed by this title is, in addition to other penalties provided by this title, guilty of a class C felony.

(b) A person required under this title to collect, account for, and pay over a tax imposed by this title who wilfully fails to collect or truthfully account for and pay over the tax at the time or times required by law or regulation is, in addition to other penalties provided by this title, guilty of a class C felony.

(c) A person required under this title to pay a tax, make a return, keep records, or supply information, who wilfully fails to pay the tax or estimated tax, make the return, keep the records, or supply the information at the time or times required by law or regulation is, in addition to other penalties provided by this title, guilty of a class A misdemeanor.

(d) A person who wilfully makes and subscribes a return or other document required under this title which contains or is verified by a written declaration that it is made under the penalties of perjury which the person does not believe to be true and correct as to every material matter is, in addition to other penalties provided by this title, guilty of a felony and, upon conviction, punishable by a fine of not more than \$25,000, or by imprisonment for not more than three years, or by both.

(e) A person who wilfully and knowingly aids or assists in, or procures, or counsels the preparation or presentation in connection with a matter arising under this title of a return, affidavit, claim, or other document that is fraudulent or is false as to a material matter is guilty of a felony whether or not the falsity or fraud is with the knowledge or consent of the person required to present the return, affidavit, claim, or document. Upon conviction, the person is punishable by a fine of not more than \$21,000, or by imprisonment for not more than three years, or by both.

(f) A person who wilfully delivers or discloses to the commissioner or the department a list, return, account, statement, or other document known by the person to be fraudulent or to be false as to a material matter is guilty of a class A misdemeanor.

(g) *Repealed, § 114 ch 6 SLA 1984.*

(h) A person engaging in or attempting to engage in a business, trade, profession, or occupation for which a license is required under this title, who wilfully fails to obtain the license, is guilty of a misdemeanor, and, upon conviction, is punishable by a fine of not more than \$2,000, or by imprisonment for not more than six months, or by both.

(i) In this section "person" includes, but is not limited to, an officer or employee of a corporation or a member or employee of a partnership, who, as officer, employee, or member, is under a duty to perform the act in respect to which the violation occurs. (§ 5 ch 113 SLA 1980; am § 114 ch 6 SLA 1984)

NOTES TO DECISIONS

Exclusiveness of remedy. — Where a statute provides for the payment of a license fee as the condition of doing any specified business, and also provides that a violator of the act shall, upon conviction, be punished by fine or imprisonment, the remedy by prosecution and punishment as prescribed by the statute is exclusive, unless there is some special

provision of law which permits the prosecution of a civil action to recover the license fee. *United States v Joudan*, 193 F.2d 196 (9th Cir 1952).

Subsection (e) of this section contains substantially the same language as former AS 43.30.336(c). In re Vogt, 642 P.2d 619 (Alaska 1982).

Collateral references. — Retailer's or buyer's defense against taxation of penalties for failure to

file, or deficiency in, state or local sales tax return. 20 ALR4th 962.

Article 4. Office of Tax Appeals.

Section

400 Office of tax appeals established
 406 Jurisdiction
 410 Appointment, term, reappointment
 416 Removal
 420 Administration

Section

426 Qualifications; code of conduct
 430 Notice of appeal from informal conference decision
 436 Rules and standards for decision
 440 Service of documents

(3) must be conditioned upon a royalty in amount or value of not less than 12.5 percent of production, except that the lessee who, proceeding under AS 38.05.131 — 38.05.134, under a lease issued in the Cook Inlet sedimentary basin who is the first to file with the commissioner a nonconfidential sworn statement claiming to be the first to have drilled a well discovering oil or gas in a previously undiscovered oil or gas pool and who is certified by the commissioner within one year of completion of that discovery well to have drilled a well in that pool that is capable of producing in paying quantities shall pay a royalty of five percent on all production of oil or gas from that pool attributable to that lease for a period of 10 years following the date of discovery of that pool, and thereafter the royalty payable on all production of oil or gas from the pool attributable to that lease shall be determined and payable as specified in the lease; the payment of the five percent royalty under this paragraph is authorized only to a holder of a lease who meets the requirements of AS 38.05.180(d);

(4) must include an annual rent of \$3 per acre or fraction of an acre initially paid to the state at inception of the lease and payable annually after that until the income to the state from royalty under that lease exceeds the rental income to the state under that lease for that year; and

(5) is subject to other conditions and obligations that are specified in the lease. (§ 2 ch 35 SLA 1994; am § 1 ch 53 SLA 1996)

Effect of amendments. — The 1996 amendment, effective September 4, 1996, in paragraph (3), added all the language following "12.5 percent of production."

Article 6. Leasing of Mineral Land.

Section	Section
135 Leasing generally; payments and interest	176 Potassium
137 Leasing agreements	177 Shallow natural gas leases
140 Limitations	180 Oil and gas leasing
145 Leasing procedure	181 Geothermal resources
180 Coal	182 Royalty on natural resources
185 Phosphates	183 Sale of royalty
190 Oil shale	184 Limitation on oil and gas leases in certain areas, and reacquisition of leases
195 Sodium	
170 Sulphur	

Editor's notes. — Section 18, ch. 75, SLA 1987 provides that "all minerals management or disposal decision made before June 16, 1987, is valid, whether or not the land was classified if other requirements of law were met."

Sec. 38.05.135. Leasing generally; payments and interest. (a) Except as otherwise provided, valuable mineral deposits in land belonging to the state shall be open to exploration, development, and the extraction of minerals. All land, together with tide, submerged, or shoreland, to which the state holds title to or to which the state may become entitled, may be obtained by permit or lease for the purpose of exploration, development, and the extraction of minerals. Except as specifically limited by AS 38.05.131 — 38.05.181, land may be withheld from lease application on a first-come, first-served basis, and offered only on a competitive bid basis when determined by the commissioner to be in the best interests of the state.

(b) When mineral land is to be leased, in addition to any other notice given, notice must also be given as provided in AS 38.05.945.

(c) Payment of a royalty or a net profit share payment to the state under a lease issued under AS 38.05.135 — 38.05.181 becomes due on the date and in the manner specified in the lease or in a regulation adopted by the commissioner.

(d) If a royalty or net profit share payment to which the state is entitled under AS 38.05.135 — 38.05.181 is not paid when it becomes due under (c) of this section, the royalty or payment bears interest in a calendar quarter at the rate of five percentage points above the annual rate charged member banks for advances by the 12th Federal Reserve District as of the first day of that calendar quarter, or at the annual rate of 11 percent, whichever is greater, compounded quarterly as of the last day of that quarter.

(e) Interest at the rate and in the manner provided in (d) of this section shall be allowed and paid on overpayment of a royalty or net profit share payment made under AS 38.05.135 — 38.05.181. (§ 1 art VIII ch 189 SLA 1959; am § 1 ch 30 SLA 1964; am § 1 ch 91 SLA 1967; am § 2 ch 71 SLA 1971; am § 10 ch 257 SLA 1976; am § 2 ch 155 SLA 1978; am § 1 ch 23 SLA 1991; am § 3 ch 35 SLA 1994)

Effect of amendments. — The 1991 amendment, effective October 31, 1991, added subsections (c) — (e).

The 1994 amendment, effective August 7, 1994, in subsection (a), made a section reference substitution in the present last sentence and deleted the former last sentence, relating to additional government incentives for exploration in unproven areas.

Editor's notes. — Section 6, ch. 23, SLA 1991, provides that, beginning on October 31, 1991, interest

accrues on underpayments and overpayments of royalties and net profit share payments, and on any interest accrued on them before October 31, 1991, "at the rates and in the manner specified in AS 38.05.135(d), added by § 1, ch. 23, SLA 1991."

Legislative history reports. — For the governor's transmittal letter concerning the enactment of (c) — (e) of this section by § 1, ch. 23, SLA 1991 (CCSR 188 (FIN)(old am)), see 1991 Senate Journal, p. 408.

NOTES TO DECISIONS

Cited in *Kirkpatrick v. Commissioner, Dep't of Natural Resources*, 381 P.2d 7 (Alaska 1964); *Moure v. State*, 583 P.2d 8 (Alaska 1978).

Collateral references. — 35 Am. Jur. 2d, Gas and Oil, §§ 64 to 77, 103 to 130, 206 to 227; 54 Am. Jur. 2d, Mines and Minerals, §§ 2, 11 to 60, 97 to 101, 120 to 145; 72 Am. Jur. 2d, States, Territories, and Dependencies, §§ 66 to 72.

73R C.J.S., Public Lands, § 197.

Prohibiting or regulating removal or exploitation of oil and gas, minerals, soil, or other natural products within municipal limits, 10 ALRS4 1226.

Grant, lease, exception, or reservation of oil and/or gas rights as including oil shale, 81 ALRSd 1109.

Sec. 38.05.137. Leasing agreements. The commissioner is authorized to enter into cooperative mineral leasing agreements with the United States regarding land which is the subject of a title dispute between federal and state authorities. Any such lease need not conform to the provisions of state law applicable to state leases issued under the authority of this chapter. (§ 2 ch 30 SLA 1964)

Collateral references. — 38 Am. Jur. 2d, Gas and Oil, §§ 206-227.

Sec. 38.05.140. Limitations. (a) A person may not take or hold coal leases or permits during the life of coal leases on state land exceeding an aggregate of 46,080 acres, except that a person may apply for coal leases or permits for acreage in addition to 46,080 acres, not exceeding a total of 5,120 additional acres of state land. The additional area applied for shall be in multiples of 40 acres and the application shall contain a statement that the granting of a lease for additional land is necessary for the person to carry on business economically and is in the public interest. On the filing of the application, except as provided by AS 38.05.177(a)(2)(C), the coal deposits in the land covered by the application shall be temporarily set aside and withdrawn from all other forms of disposal provided under AS 38.05.135 — 38.05.181.

(b) The commissioner shall, after posting notice of the pending application in the local land office, conduct public hearings on the application for additional acreage. After public hearings, to the extent the commissioner finds to be in the public interest and necessary for the applicant in order to carry on business economically, the commissioner may, under

regulations adopted by the commissioner, permit the person to take or hold coal leases or permits for an additional aggregate acreage of not more than 5,120 acres.

(c) A person may not take or hold at one time phosphate leases on state land exceeding in the aggregate 10,240 acres. A person may not take or hold sodium leases or permits during the life of sodium leases on state land exceeding in the aggregate acreage 5,120 acres, except that the commissioner may, where it is necessary in order to secure the economic mining of sodium compounds, permit a person to take or hold sodium leases or permits for up to 15,360 acres. A person may not take or hold at any one time oil or gas leases exceeding in the aggregate 500,000 acres granted on tide and submerged land and 500,000 acres on all land other than tide and submerged land, including leases held both as lessee and under option or operating agreement from others. Where more than a single person holds an interest in an oil or gas lease, each person shall be charged only with that percentage of the total acreage which corresponds to its percentage share of the total beneficial interest in the lease.

(d) The commissioner, for the purpose of encouraging the greatest ultimate recovery of coal, oil shale, phosphate, sodium, potassium, sulphur, and geothermal resources and in the interest of conservation of natural resources, after public hearing, or, when the state's title to land beneath navigable waters has been legally challenged by the United States and litigation initiated, may waive, suspend, refund, or reduce the rental, or minimum royalty, or reduce the royalty on an entire leasehold, or on any tract or portion of a leasehold segregated for royalty purposes, whenever the commissioner determines that it is necessary to do so in order to promote development, or that the lease cannot be successfully operated under its terms. If the commissioner, in the interest of conservation, directs or assents to the suspension of operations and production under a lease granted, the payment of acreage rental or of minimum royalty prescribed by the lease may be suspended during the period of suspension of operations and production. The term of the lease shall be extended by adding the period of suspension to the lease.

(e) The provisions of (d) of this section that apply to waiver, suspension, refund or reduction of rental of minimum royalty apply to rental or minimum royalty paid before or after June 19, 1970 on any lease covering land beneath navigable waters which, according to the records of the division of lands, is in effect on June 19, 1970.

(f) The submerged and shoreland lying north of 57 degrees, 30 minutes north latitude and east of 159 degrees, 49 minutes west longitude within the Bristol Bay drainage are designated as the Bristol Bay Fisheries Reserve. Within the Bristol Bay Fisheries Reserve no surface entry permit to develop an oil or gas lease or oil and gas exploration license may be issued on state owned or controlled land until the legislature by appropriate resolution specifically finds that the entry will not constitute danger to the fishery. (§ 2 art VIII ch 169 SLA 1959; am § 1 ch 68 SLA 1969; am §§ 1, 2 ch 208 SLA 1970; am §§ 3, 4 ch 71 SLA 1971; am § 1 ch 102 SLA 1972; am §§ 3, 5 ch 155 SLA 1978; am § 4 ch 35 SLA 1994; am § 3 ch 140 SLA 1996)

Effect of amendments. — The 1994 amendment, effective August 7, 1994, inserted "or oil and gas exploration license" in subsection (f). The 1996 amendment, effective October 9, 1996, inserted "except as provided by AS 38.05.177(a)(2)(C)," near the beginning of the last sentence of subsection (a).

Sec. 38.05.145. Leasing procedure. (a) Deposits of coal, phosphates, oil shale, sodium, potassium, oil, gas, geothermal resources and state land containing these deposits are subject to disposition under regulations, recommended by the director and adopted by the commissioner, and the provisions of AS 38.05.145 — 38.05.181. In applying the acreage limitations the commissioner may apply the rule of approximation. The uses of the rule of approximation made before March 31, 1960, by the commissioner are ratified.

(b) ~~Repealed, § 6 ch 155 SLA 1978.~~ (§ 3 art VIII ch 169 SLA 1959; am § 16 ch 61 SLA 1960; am § 3 ch 30 SLA 1964; am §§ 5, 6 ch 71 SLA 1971; am § 33 ch 71 SLA 1972; am § 6 ch 155 SLA 1978)

NOTES TO DECISIONS

Applied in *Moore v. State*, 553 P.2d 8 (Alaska 1976).

Collateral references. — Abandonment of oil or gas lease by parcel declaration, 18 ALR2d 951.

Rights of lessee to minerals extracted during the lease but remaining on the premises after its termination, 61 ALR2d 1131.

Recovery in case of geophysical or seismograph exploration or survey not authorized, 67 ALR2d 444.

"Mine" as used in written instrument, 92 ALR2d 868.

Rights of parties to oil and gas lease or royalty deed

after expiration of fixed term where production temporarily ceases, 100 ALR2d 686.

What constitutes reasonably necessary use of the surface of the leasehold by a mineral owner, lessee, or driller under an oil and gas lease or drilling contract, 83 ALR3d 18.

Duty of public authority to disclose to contractor information, allegedly in his possession, affecting cost or feasibility of project, 86 ALR3d 182.

Sec. 38.05.150. Coal. (a) The commissioner may, and upon the petition of a qualified applicant, shall divide coal land or the deposits of coal owned by the state into leasing tracts of 40 acres each, or multiples of 40 acres, and in the form which will permit the economical mining of the coal in the tract.

(b) Thereafter the commissioner may, upon the request of a qualified applicant or otherwise, from time to time, offer the land or deposits of coal for leasing. Each lease shall be awarded to a qualified applicant by competitive bidding or by the method prescribed by regulation.

(c) Where prospecting or exploration work is necessary to determine the existence or workability of coal deposits in an unclaimed and undeveloped area, the commissioner may issue to qualified applicants prospecting permits for a term of three years, covering not more than 5,120 acres with each permit. The commissioner shall grant a two-year extension of the initial three-year term of the permit if the permittee has conducted reasonably diligent prospecting or exploration activities in the area covered by the permit, has not been able to determine the existence and workability of coal deposits in the area, and wishes to continue prospecting or exploring in the area. The commissioner may grant up to three two-year extensions of the initial three-year term of the permit. At any time during the period of the permit, the permittee is entitled to a lease after submitting a mining plan satisfactory to the commissioner for that portion of the land in the permit as is shown to the satisfaction of the commissioner to contain coal in commercial quantities or to be needed for mining, reclamation, or processing the coal.

(3) For the privilege of mining or extracting the coal in the land covered by the lease, the lessee

(1) shall pay to the state the royalties specified in the lease; the royalties shall be fixed before offering the lease, and shall be effective for a period of not more than 20 years; the royalties shall be not less than five cents a ton of 2,000 pounds; the royalty payment is subject to the exploration incentive credit authorized by AS 27.30;

(2) shall also pay an annual rental, payable at the date of the lease and annually thereafter, on the land or coal deposits covered by the lease, at a rate fixed by the commissioner before offering the lease; the annual rental shall be effective for a period of not more than 20 years; the annual rental shall be not less than 25 cents an acre for the first year of the lease, not less than 50 cents an acre for the second year, third year, fourth year and fifth year, and not less than \$1 an acre for each year thereafter during the continuance of the lease; the rental for each year shall be credited against the royalties as they accrue for that year; each lease shall provide that the annual rental payment in

subject to adjustment at intervals of no more than 20 years and adjustments shall be based on the current rates for properties similarly situated.

(e) Each lease shall be for an indeterminate period upon condition of diligent development and continued operation of the mine, except when operation is interrupted by strikes, the elements, or casualties not attributed to the lessee.

(f) Notwithstanding AS 38.05.177, a lease entered into under this section gives the lessee the right to vent or remove methane and other gas held in association with the coal in the land covered by the lease to ensure safe coal mining operations. (§ 3(1) art VIII ch 169 SLA 1959; am § 17 ch 61 SLA 1960; am § 1 ch 71 SLA 1966; am §§ 2, 3 ch 68 SLA 1969; am § 1 ch 93 SLA 1984; am § 2 ch 88 SLA 1995; am § 4 ch 140 SLA 1998)

Effect of amendments. - The 1995 amendment, effective June 21, 1995, in subsection (d), added the paragraph designations, added "the royalty payment is subject to the exploration incentive credit authorized by AS 27.30," at the end of paragraph (1), and made minor stylistic changes.

The 1996 amendment, effective October 9, 1996, added subsection (f).

Editor's notes. - Under § 6, ch 86, SLA 1995, the

amendments to subsection (d) made by § 2, ch 86, SLA 1995 are "retroactive to January 1, 1995" and apply "to activities that qualify for the exploration incentive credit authorized by AS 27.30 that are undertaken after May 16, 1995."

Collateral references. - Grant, lease, exception, or reservation of "oil, gas, and other minerals, or the like," as including coal or metallic ore, 69 ALR3d 1148

Sec. 38.05.155. Phosphates. (a) The commissioner may lease to qualified applicants land belonging to the state which contains deposits of phosphates and associated and related minerals, when it is in the public interest to do so. The commissioner may lease land through advertisement, competitive bidding, or other methods prescribed by regulation. The land shall be leased in units reasonably compact in form and not exceeding 2,560 acres in each unit.

(b) Each lease shall be conditioned upon the payment to the state of the royalties specified in the lease. The commissioner shall fix the royalties in advance of offering the lease. The royalties shall be not less than five per cent of the gross value, at the point of shipment to market, of the output of phosphates or phosphate rock, and associated or related minerals. Each lease shall provide for the payment of a rental payable at the date of the lease and annually thereafter. The rental shall be not less than 25 cents an acre for the first year, 50 cents an acre for the second year and third year, and \$1 an acre for each year thereafter. The rental paid for any year shall be credited against the royalties for that year. Each lease shall be for a term of 20 years and so long thereafter as the lessee complies with the terms and conditions of the lease. (§ 3(2) art VIII ch 169 SLA 1959)

Sec. 38.05.160. Oil shale. (a) The commissioner may lease to a qualified person deposits of oil shale belonging to the state and the surface of as much of the land containing these deposits, or land adjacent to it, as may be required for the extraction and reduction of the lease minerals. The lease may not exceed 5,120 acres of land, and the terms of the lease shall be limited to the extraction of minerals from the oil shale so leased. The lease may be for indeterminate periods upon the conditions imposed by the commissioner.

(b) For the privilege of mining, extracting, and disposing of the oil or other minerals covered by the lease, the lessee shall pay to the state the royalties specified in the lease and an annual rental at the rate of 50 cents an acre for the land included in the lease. The rental paid for any one year shall be credited against the royalties accruing for that year. For the purpose of encouraging the production of petroleum products from shales, the commissioner may waive the payment of royalty and rental during the first five years of the lease. (§ 3(3) art VIII ch 169 SLA 1959)

Collateral references. - 35 Am Jur 2d, Gas and Oil, §§ 264-271

Secondary recovery of oil and gas, 93 ALR2d 451

Oil shale: grant, lease, exception, or reservation of oil and/or gas rights as including oil shale, 81 ALR3d 1109.

Sec. 38.05.165. Sodium. (a) The commissioner may grant a prospecting permit to a qualified applicant. The permit gives the exclusive right to prospect for chlorides, sulphates, carbonates, borates, silicates, or nitrates of sodium in land belonging to the state for a period of not exceeding two years. The area included in a prospecting permit may not exceed 2,560 acres of land in reasonably compact form. Upon showing to the satisfaction of the commissioner that valuable deposits of sodium minerals have been discovered by the permittee within the area covered by the permit, and that the land is chiefly valuable for these deposits, the permittee is entitled to a lease for all or a part of the land embraced in the prospecting permit at a royalty of not less than two per cent of the quantity or gross value of the output of sodium compounds and other related products at the point of shipment to market. The commissioner may lease land known to contain valuable deposits of sodium compounds that is not covered by permits or leases through advertisement, competitive bidding, or other methods prescribed by regulation. The area covered by a lease may not exceed 2,560 acres.

(b) Each lease shall be conditioned upon the same royalty payment specified in paragraph (a) and the payment in advance of a rental of 25 cents an acre for the first calendar year or fraction of it, 50 cents an acre for the second calendar year, third calendar year, fourth calendar year, and fifth calendar year, and \$1 an acre a year thereafter during the continuance of the lease. The rental for any one year shall be credited against royalties accruing for that year.

(c) A lease shall be for a period of 20 years with preferential right in the lessee to renew for successive periods of 10 years upon terms and conditions prescribed by the commissioner. (§ 3(4) art VIII ch 169 SLA 1959)

Sec. 38.05.170. Sulphur. (a) Under regulations adopted by the commissioner, the commissioner shall grant a prospecting permit for sulphur to a qualified applicant. The permit gives the applicant the exclusive right to prospect for sulphur, in land belonging to the state, for a period not exceeding two years. The area included in a permit may not exceed 2,560 acres of land in reasonably compact form. Upon showing to the satisfaction of the commissioner that valuable deposits of sulphur have been discovered by the permittee within the area covered by the permit, and that the land is chiefly valuable for these deposits, the permittee is entitled to a lease for all or a part of the land embraced in the prospecting permit, at a royalty of five per cent of the quantity or gross value of the output of sulphur at the point of shipment to market. The commissioner may lease land known to contain valuable deposits of sulphur that is not covered by permits or leases through advertisement, competitive bidding, or other methods prescribed by regulation. The area covered by the lease may not exceed 2,560 acres.

(b) Each lease shall be conditioned upon the payment by the lessee of the royalty fixed in the lease and the payment in advance of a rental of 50 cents an acre a year. The rental for any one year shall be credited against the royalties accruing for that year. (§ 3(5) art VIII ch 169 SLA 1959)

Sec. 38.05.175. Potassium. (a) Under regulations adopted by the commissioner, the commissioner may grant a prospecting permit to a qualified applicant. The permit gives the applicant the exclusive right to prospect for chlorides, sulphates, carbonates, borates, silicates, or nitrates of potassium, in land belonging to the state, for a period not exceeding two years. The area included in a permit may not exceed 2,560 acres of land in reasonably compact form. Upon showing to the satisfaction of the commissioner that valuable deposits of potassium compounds have been discovered by the permittee within the area covered by the permit, and that the land is chiefly valuable for these deposits, the permittee is entitled to a lease for all or a part of the land embraced in the prospecting permit, at a royalty of not less than two per cent of the quantity or gross value of the output of potassium compounds and other related products, except sodium, at the point

of shipment to market. The commissioner may lease land known to contain valuable deposits of potassium compounds that is not covered by permits or leases through advertisement, competitive bidding, or other methods prescribed by regulation. The area covered by the lease may not exceed 2,660 acres.

(b) Each lease shall be conditioned upon payment by the lessee of a royalty of not less than two per cent of the quantity or gross value of the output of potassium compounds and other related products, except sodium, at the point of shipment to market, and the payment in advance of a rental of 26 cents an acre for the first calendar year or fraction of it, 50 cents an acre for the second calendar year, third calendar year, fourth calendar year, and fifth calendar year, and \$1 an acre a year thereafter during the continuance of the lease. The rental for any one year shall be credited against royalties accruing for that year.

(c) Each lease shall be for a term of 20 years and so long thereafter as the lessee complies with the terms and conditions of the lease. (§ 3(6) art VIII ch 169 SLA 1959)

Sec. 38.05.177. Shallow natural gas leases. (a) The provisions of this section

(1) apply to gas, whether methane associated with and derived from coal deposits or otherwise, developed from a source that is onshore and within 3,000 feet of the surface; and

(2) do not apply to authorize lease of

(A) land

(i) that is subject to an oil and gas exploration license or lease issued under AS 405.131 — 38.05.134; or

(ii) that is leased under AS 38.05.180;

(B) the land (i) that is proposed to be subject to an oil and gas exploration license or lease issued under AS 38.05.131 — 38.05.134; or (ii) that is described in and part of a proposed oil and gas leasing program prepared under AS 38.05.180(b); however, the commissioner may waive the limitations of this subparagraph;

(C) the land that is held under a coal lease entered into under AS 38.05.150, unless the applicant for a shallow natural gas lease is also the lessee under AS 38.05.150 of that land; or

(D) the valid existing selections of the Alaska Mental Health Trust Authority made for the purpose of reconstituting the mental health trust established under the Alaska Mental Health Enabling Act, P.L. 84-830, 70 Stat. 709 (1956), that become subject to management under AS 38.05.801, or of land that has been designated by law for or is subject to designation for conveyance to the Alaska Mental Health Trust Authority; however, after consultation with the Alaska Mental Health Trust Authority, the commissioner may waive the limitations of this subparagraph.

(b) For the purpose of exploring for and developing shallow natural gas reservoirs, upon application, the director may lease to a person land for which the state owns the subsurface rights. A person applying for a lease under this subsection

(1) shall specify the area to be leased; the area to be leased may not exceed 5,760 acres; the lessee may not hold more than 46,080 acres of land under leases entered into under this section;

(2) may be required to pay a reasonable application fee of up to \$500.

(c) Within 20 days of receipt of a lease application, the director shall give notice under AS 38.05.945 of receipt of the lease application and call for comments from the public. The director's call for public comments must provide opportunity for public comment for a period of 60 days. If, after review of information received during the public comment period, the director determines that the discovery of a local source of natural gas would benefit the residents of an area, the director shall execute a lease for the area described

(b) of this section. The director shall execute the lease within 90 days after the close of the public comment period or, if review is required under AS 46.40, within 30 days after

the final consistency determination is made under AS 46.40, whichever is later. A lease entered into under this subsection gives the lessee the exclusive right to explore for, develop, and produce, for a term of three years, natural gas on the state land described in the lease; the right to explore for, develop, and produce is limited to gas derived from natural gas within 3,000 feet of the surface.

(d) A lease shall be automatically extended if and for so long thereafter as gas is produced in paying quantities from the lease and the lessee continues to meet all requirements of the lease. A lease issued under this section covering land on which there is a well capable of producing gas in paying quantities does not expire because the lessee fails to produce gas unless the lessee is allowed reasonable time to place the well on a producing status. If drilling has commenced on the expiration date of the primary term of the lease and is continued with reasonable diligence, including such operations as redrilling, sidetracking, or other means necessary to reach the originally proposed bottom hole location, the lease is extended for one year and for so long thereafter as gas is produced in paying quantities. A gas lease issued under this section that is subject to termination by reason of cessation of production does not terminate if, within 90 days after production ceases or a longer period determined at the discretion of the director, reworking or drilling operations are commenced on the land under lease and are thereafter conducted with reasonable diligence during the period of nonproduction. In addition, upon application by the lessee, the director may once extend a lease issued under (c) of this section for a period of not more than three years.

(e) The director may, following the procedures described in (c) of this section, adjust the boundaries of a lease entered into under this section as may be necessary to ensure development of natural gas within a reasonably compact area; a lease so adjusted under this subsection remains subject to the acreage limitations set out in (b)(1) of this section.

(f) A shallow gas lease must provide for payment to the state of annual rent in the amount of 50 cents per acre. The rent is due and payable on the dates determined in the lease. The director shall mail the lessee one written notice, certified return receipt requested, three weeks before the due date of the rent. If the lessee fails to pay rent, the director shall terminate the lease.

(g) The royalty payable on natural gas produced from a lease

(1) is

(A) 12.5 percent of the value of production removed or sold from the lease for gas exported from the state or gas that is produced in direct competition with gas on which a royalty at a rate of at least 12.5 percent is payable; and

(B) except as provided in (A) of this paragraph, 6.25 percent of the value of the production removed or sold from the lease; and

(2) shall be based upon production delivered in pipeline quality and free of all lease expenses, including but not limited to separation, cleaning, dehydration, gathering, salt water disposal, and preparation for transportation off the lease.

(h) A lease issued under this section is subject to the following terms and conditions and may be terminated by the director in the event of a breach of a term or condition:

(1) the lessee may surrender the lease or relinquish part of the lease at any time;

(2) the lease may not be transferred or assigned until a well capable of production of gas in paying quantities has been drilled on the lease; however, this paragraph does not prohibit the lessee from entering into a farm out agreement or similar arrangement with a third party under which the third party assists in exploration and development of production from the lease if the agreement or arrangement does not require a payment of consideration by the third party to the lessee, except that the lessee may retain an overriding royalty interest in the lease or may retain a net profit or other production payment.

(i) The applicant for a lease is responsible for conducting a title search for the area described in the lease application.

(j) A lease does not give the lessee the right to produce oil. A lease does not give the lessee the right to produce gas from sources that are not within 3,000 feet of the surface. If a well drilling for natural gas under a lease authorized by this section penetrates a formation capable of producing gas below 3,000 feet of the surface or penetrates a formation capable of producing oil, the owner or operator

(1) shall notify the department and the Alaska Oil and Gas Conservation Commission; and

(2) may not conduct further operations in the drilled well until the facility complies with all applicable laws and regulations relating to oil and gas exploration and production; however, this paragraph does not prevent the owner or operator from conducting activities that may be required by the Alaska Oil and Gas Conservation Commission to plug, plug-back, or abandon a well.

(k) The commissioner of natural resources may adopt only the regulations that are reasonable and that are necessary to implement, interpret, or make specific the provisions of this section or to establish procedures to govern application of the provisions of this section.

(l) A lessee obtaining a lease under this section may exercise the rights authorized by this section and the lease. The rights granted by the lease must be exercised in a manner that does not unreasonably interfere with eventual development of other mineral deposits on the land leased. However, in a lease entered into under AS 38.05.160 for land that is already leased under this section, coal may not be mined or extracted by the coal lessee from the coal lease without prior agreement with the lessee holding the lease issued under this section.

(m) Except as otherwise specifically provided in this section, the provisions of AS 38.05.135 — 38.05.184 apply to leases entered into under this section.

(n) In this section, "lease" means a shallow gas lease authorized by this section. (§ 5 ch 140 SLA 1996)

Cross references. — For legislative findings and purpose in connection with the enactment of this section, see § 1, ch 140, SLA 1996 in the Temporary and Special Acts. **Effective dates.** — Section 5, ch. 140, SLA 1996, which enacted this section, took effect on October 9, 1996.

Sec. 38.05.180. Oil and gas leasing. (a) The legislature finds that

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

- (A) maximize the economic and physical recovery of the resources;
- (B) maximize competition among parties seeking to explore and develop the resources;
- (C) maximize use of Alaska's human resources in the development of the resources;
- (2) it is in the best interests of the state

(A) to encourage an assessment of its oil and gas resources and to allow the maximum flexibility in the methods of issuing leases to

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

(ii) minimize the adverse impact of exploration, development, production, and transportation activity; and

(B) to offer acreage for oil and gas leases, specifically including

(i) state acreage that has been the subject of a best interest finding at annual areawide lease sales; and

(ii) land in areas that, under (d) of this section, may be leased without having been included in the leasing program prepared and submitted under (b) of this section.

(b) The commissioner shall biennially prepare and, between the first and the 15th day of the first regular session of each legislature, notify the legislature of the availability of, a five-year proposed oil and gas leasing program consisting of a schedule of proposed lease sales and specifying as precisely as practicable the location of tracts proposed to be

offered for oil and gas leasing during the calendar year in which the proposed program is made available to the legislature and the following four calendar years.

(c) Except as provided in (d) and (w) of this section, an oil and gas lease sale may not be held unless it was included in the proposed leasing programs submitted to the legislature during the two calendar years preceding the year in which the sale is held. A lease sale may not be held before the date it is scheduled in the proposed oil and gas leasing program.

(d) The commissioner

(1) may annually offer oil and gas leases of the acreage described in AS 38.05.036(e)(6)(G);

(2) may issue oil and gas leases in an area that has not been included in a leasing program prepared, in accordance with (b) of this section if the land to be leased

(A) was previously subject to a valid state or federal oil and gas lease;

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

(C) is adjacent to land owned or controlled by another party on which a discovery of commercial quantities of oil or gas has been made, and the commissioner finds, after hearing, that there is a reasonable probability that the land to be leased contains oil or gas in communication with the oil or gas discovered on the land of the other party;

(D) is adjacent to land included in the federal five-year Outer Continental Shelf leasing program under 43 U.S.C. 1344, and the commissioner makes a written finding, after hearing, that coordinated or simultaneous leasing with the federal government is in the public interest; or

(E) is the subject of an oil and gas exploration license issued under AS 38.05.131 — 38.05.134.

(e) Simultaneously with submission of the leasing program required under (b) of this section, the commissioner shall prepare and notify the legislature of the availability of a report containing the following:

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

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

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

(f) Except as provided by AS 38.05.131 — 38.05.134 and 38.05.177, the commissioner may issue oil and gas leases on state land to the highest responsible qualified bidder as follows:

(1) the commissioner shall issue an oil and gas lease to the successful bidder determined by competitive bidding under regulations adopted by the commissioner; bidding may be by sealed bid or according to any other bidding procedure the commissioner determines is in the best interests of the state;

(2) whenever, under any of the leasing methods listed in this subsection, a royalty share is reserved to the state, it shall be delivered in pipeline quality and free of all lease or unit expenses, including but not limited to separation, cleaning, dehydration, gathering, salt water disposal, and preparation for transportation off the lease or unit area;

(3) following a pre-sale analysis, the commissioner may choose at least one of the following leasing methods:

(A) a cash bonus bid with a fixed royalty share reserved to the state of not less than 12.5 percent in amount or value of the production removed or sold from the lease;

(B) a cash bonus bid with a fixed royalty share reserved to the state of not less than 12.5 percent in amount or value of the production removed or sold from the lease and a fixed share of the net profit derived from the lease of not less than 30 percent reserved to the state;

(C) a fixed cash bonus with a royalty share reserved to the state as the bid variable but not less than 12.5 percent in amount or value of the production removed or sold from the lease;

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

(E) a fixed cash bonus with a fixed royalty share reserved to the state of not less than 12.5 percent in amount or value of the production removed or sold from the lease with the share of the net profit derived from the lease reserved to the state as the bid variable;

(F) a cash bonus bid with a fixed royalty share reserved to the state based on a sliding scale according to the volume of production or other factor but in no event less than 12.5 percent in amount or value of the production removed or sold from the lease;

(G) a fixed cash bonus with a royalty share reserved to the state based on a sliding scale according to the volume of production or other factor as the bid variable but not less than 12.5 percent in amount or value of the production removed or sold from the lease;

(4) notwithstanding a requirement in the leasing method chosen of a minimum fixed royalty share, on and after March 3, 1997, the lessee under a lease issued in the Cook Inlet sedimentary basin who is the first to file with the commissioner a nonconfidential sworn statement claiming to be the first to have drilled a well discovering oil or gas in a previously undiscovered oil or gas pool and who is certified by the commissioner within one year of completion of that discovery well to have drilled a well in that pool that is capable of producing in paying quantities shall pay a royalty of five percent on all production of oil or gas from that pool attributable to that lease for a period of 10 years following the date of discovery of that pool, and thereafter the royalty payable on all production of oil or gas from the pool attributable to that lease shall be determined and payable as specified in the lease; for purposes of this paragraph, the reduced royalty authorized by this paragraph is subject to the following:

(A) only one reduction of royalty authorized by this paragraph may be allowed on each lease that qualifies for reduction of royalty under this paragraph;

(B) if, under this paragraph, application is made for a royalty reduction for a lease that was entered into before March 3, 1997, the commissioner may approve the application only if, on that date, the lease was a nonproducing lease that was not committed to a unit approved by the commissioner under (m) of this section, that is not part of a unit under (p) or (q) of this section, and that has not been made part of a unit under AS 31.05;

(C) if application for a royalty reduction is made under this paragraph for a lease on which a discovery royalty was claimed or may be claimed under the discovery royalty provisions of former AS 38.05.180(a) in effect before May 6, 1969, the commissioner shall disallow the application under this paragraph unless the applicant waives the right to claim the right to a reduced royalty under the discovery royalty provisions of former AS 38.05.180(a) in effect before May 6, 1969; and

(D) the commissioner shall adopt regulations setting out the standards, criteria, and definitions of terms that apply to implement the filing of applications for, and the review and certification of, discovery oil and gas royalty certifications under this paragraph.

(g) The share of the net profit derived from a lease reserved to the state under (f) of this section is royalty sale proceeds for the purposes of the Alaska permanent fund under AS 37.13.010.

(h) The commissioner may include terms in any oil and gas lease imposing a minimum work commitment on the lessee. These terms shall be made public before the sale, and may include appropriate penalty provisions to take effect in the event the lessee does not fulfill the minimum work commitment. If it is demonstrated that a lease has been proven unproductive by actions of adjacent lease holders, the commissioner may set aside a work commitment. The commissioner may waive for a period not to exceed one two-year period any term of a minimum work commitment if the commissioner makes a written finding that conditions preventing drilling or exploration were beyond the lessee's

reasonable ability to foresee or control or that the lessee has demonstrated through good faith efforts an intent and ability to drill or develop the lease during the term of the waiver.

(i) The commissioner 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 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.

(j) The commissioner

(1) may provide for an increase or decrease or otherwise modify royalty, to allow for production that would not otherwise be economically feasible, on individual leases, leases unitized as described in (p) of this section, leases subject to an agreement described in (a) or (t) of this section, or interests unitized under AS 31.05; the commissioner may act under this subsection to modify the royalty

(A) after June 20, 1995 and not later than July 1, 2015, so long as the authority to modify royalty under this subparagraph has been authorized or reauthorized by law within the ten years preceding the commissioner's action to modify the royalty, to allow for production from an oil or gas field or pool if

(i) the oil or gas field or pool has been delineated sufficiently to allow the commissioner to conduct the analyses and make the findings required by this subsection; and

(ii) the field or pool has not previously produced oil or gas for sale;

(B) to prolong the economic life of an oil or gas field or pool as costs per barrel or barrel equivalent increase; or

(C) to reestablish production of shut-in oil or gas;

(2) may not grant a royalty modification unless the lessee or lessees requesting the modification make a clear and convincing showing that a modification of royalty meets the requirements of this subsection and is in the best interests of the state;

(3) shall

(A) condition any royalty modification granted under this subsection in any way necessary to protect the state's best interests;

(B) describe, in the findings and determinations required by this subsection, the relevant factors, including price, projected production rate or volume, predicted ultimate recovery, and development, operating, and transportation costs, upon which the modification is based;

(C) for a modification under (1)(A) of this subsection, set out the terms and conditions, which

(i) must include a mechanism for adjusting royalty percentage based on price; using forecasts of the range of future prices and their probabilities, the mechanism must provide that the value of the potential revenue increases resulting from royalty percentage increases must exceed the value of the potential revenue losses resulting from royalty percentage decreases; and

(ii) may include, in addition to the royalty percentage adjustment based on price, which must meet the conditions specified in (i) of this subparagraph, a further adjustment based on production rate or volume from the field or pool; and

(D) for a modification under (1XB) or (1XC) of this subsection, set out the terms and conditions, which may include substitution of a sliding scale royalty or other mechanism to modify the royalty if there is a change in the relevant factors, such as price, projected production rate or volume, predicted ultimate recovery, and development, operating, and transportation costs, upon which the modification is based;

(4) may not grant a royalty modification for a field or pool

(A) under (1XA) of this subsection if the royalty modification for the field or pool would establish a royalty rate of less than five percent in amount or value of the production removed or sold from a lease or leases covering the field or pool;

(B) under (1XB) or (1XC) of this subsection if the royalty modification for the field or pool would establish a royalty rate of less than three percent in amount or value of the production removed or sold from a lease or leases covering the field or pool;

(5) may not grant a royalty modification under this subsection without including an explicit condition that the royalty modification is not assignable without the prior written approval of the commissioner; the commissioner shall, in the preliminary and final findings and determinations, set out the conditions under which the royalty modification may be assigned;

(6) shall require the lessee or lessees to submit, with the application for the royalty modification, financial and technical data that demonstrate that the requirements of this subsection are met; the commissioner shall

(A) require disclosure of the financial and technical data related to development, production, and transportation of oil and gas from the field or pool that are necessary to make a determination as to whether or not to grant the request for royalty modification; and

(B) keep the data described in (A) of this paragraph confidential under AS 38.06.025(a)(9) at the request of the lessee or lessees making application for the royalty modification; the confidential data may be disclosed by the commissioner to legislators and to the legislative auditor and as directed by the chair or vice-chair of the LB&A Committee to the director of the division of legislative finance, the permanent employees of their respective divisions who are responsible for evaluating a royalty modification, and to agents or contractors of the legislative auditor or the legislative finance director who are engaged under contract to evaluate the royalty modification, provided they sign an appropriate confidentiality agreement;

(7) may require the lessee or lessees making application for the royalty modification to pay for the services of an independent contractor, qualified to evaluate hydrocarbon development, production, transportation, and economics, who is selected by the commissioner to assist the commissioner in evaluating the application and financial and technical data; selection of an independent contractor under this paragraph is not subject to AS 36.30;

(8) shall

(A) make and publish a preliminary findings and determination on the royalty modification application; if the preliminary findings and determination concerns a royalty modification under (1XA) of this subsection, the preliminary findings and determination shall also be presented to the governor for the governor's approval or disapproval; the governor may not delegate a determination to approve or disapprove a preliminary findings and determination under this subparagraph;

(B) for a royalty modification under (1XA) of this subsection, if the governor approves the preliminary findings and determination under (A) of this paragraph,

(i) give reasonable public notice of the preliminary findings and determination;

(ii) concurrently with the issuance of the public notice, unless directed by the Legislative Budget and Audit Committee to do otherwise, make available copies of the commissioner's preliminary findings and determination on the royalty modification application and the supporting financial and technical data, including the work papers,

analyses, and recommendations of any contractors retained under (7) of this subsection, to persons authorized under (6XII) of this subsection to review the data; and

(iii) invite public comment on the preliminary findings and determination during a 30-day period for receipt of public comment;

(C) for a royalty modification under (1XB) or (C) of this subsection, if the preliminary findings and determination approves a royalty modification,

(i) give reasonable public notice of the preliminary findings and determination; and

(ii) invite public comment on the preliminary findings and determination during a 30-day period for receipt of public comment;

(8) shall address in any findings and determinations required under this subsection the reasonably foreseeable effects of the proposed royalty modification on the state's revenue;

(10) shall offer to appear before the Legislative Budget and Audit Committee to provide the committee a review of the commissioner's preliminary findings and determination on the royalty modification application and the supporting financial and technical data; if the Legislative Budget and Audit Committee accepts the commissioner's offer, the committee shall give notice of the committee's meeting to all members of the legislature; if, under (6XR) of this subsection, the financial and technical data must be kept confidential at the request of a lessee or lessees making application for the royalty modification, the commissioner may appear before the committee in executive session;

(11) shall make copies of the preliminary findings and determination available to

(A) the presiding officer of each house of the legislature;

(B) the chairs of the legislature's standing committees on resources; and

(C) the chairs of the legislature's special committees on oil and gas, if any;

(12) shall, within 30 days after the close of the public comment period under (8) of this subsection,

(A) prepare a summary of the public response to the commissioner's preliminary findings and determination;

(B) make a final findings and determination and present it to the governor for the governor's approval or disapproval; the governor may not delegate a decision to approve or disapprove a final findings and determination presented under this subparagraph; the commissioner's final findings and determination regarding a royalty modification, if approved by the governor, is final and not appealable to the court;

(C) transmit a copy of the final findings and determination prepared under (B) of this paragraph to the lessee or lessees making application for the royalty modification;

(D) with the consent of the lessee or lessees applying for the royalty modification, amend the lease or unitization agreement of the lessee or lessees applying for the royalty modification consistent with the commissioner's approved final findings and determination; and

(E) make copies of the final findings and determination available to each person who submitted comment under (8) of this subsection and who has filed a request for the copies;

(13) is not limited by the provisions of AS 38.05.134(3) or (f) of this section in the commissioner's determination under this subsection.

(k) The commissioner shall define all terms and adopt all regulations necessary for a reasonable understanding and evaluation of a particular bidding method before the public announcement of the terms of proposed sale employing that method.

(l) Subject to the provisions of AS 31.05, the commissioner has discretion to enter into an agreement whereby, with the consent of the lessee, the state's royalty share of oil and gas production may be stored or retained in storage by the lessee, or the commissioner may enter into an agreement with one or more of the affected field lease holders to trade current royalty production from a field for a like amount, kind, and quality of future production, on the condition that the state receives back its stored or traded royalty share during the first half of the estimated field life or no later than 15 years after start of production, whichever is sooner.

(m) An oil and gas lease must cover a reasonably compact area not exceeding 5,760 acres, and may be for a maximum period of 10 years, except that the commissioner may issue a lease for a period not less than five years upon a finding that it is in the best interests of the state. An oil and gas lease shall be automatically extended if and for so long thereafter as oil or gas is produced in paying quantities from the lease or if the lease is committed to a unit approved by the commissioner. A lease issued under this section covering land on which there is a well capable of producing oil or gas in paying quantities does not expire because the lessee fails to produce oil or gas unless the lessee is allowed reasonable time to place the well on a producing status. Upon extension, the commissioner may increase lease rentals so long as the increased rental rate does not exceed 150 percent of the rate for the preceding year. If drilling has commenced on the expiration date of the primary term of the lease and is continued with reasonable diligence, including such operations as redrilling, sidetracking, or other means necessary to reach the originally proposed bottom hole location, the lease continues in effect until 90 days after drilling has ceased and for so long thereafter as oil or gas is produced in paying quantities. An oil and gas lease issued under this section which is subject to termination by reason of cessation of production does not terminate if, within 60 days after production ceases, reworking or drilling operations are commenced on the land under lease and are thereafter conducted with reasonable diligence during the period of nonproduction.

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

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

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

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

(q) A plan authorized by (p) of this section, which includes land owned by the state, may contain a provision vesting the commissioner, or a person, committee, or state

agency, with authority to modify from time to time the rate of prospecting and development and the quantity and rate of production under the plan. All leases operated under a plan approved or prescribed by the commissioner are excepted in determining holdings or control under AS 38.05.140. The provisions of this section concerning cooperative or unit plans are in addition to and do not affect AS 31.05.

(r) Producing acreage on a known geologic structure of a producing oil or gas field is excluded from chargeability as against the acreage limitation provisions of AS 38.05.140.

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

(t) The commissioner may prescribe conditions and approve, on conditions, drilling, or development contracts made by one or more lessees of oil or gas leases, with one or more persons, when, in the discretion of the commissioner, the conservation of natural resources or the public convenience or necessity requires it or the interests of the state are best served. All leases operated under approved drilling or development contracts and interests under them, are excepted in determining holding or control under AS 38.05.140. The commissioner may not decrease royalty on a lease or leases that are subject to a drilling or development contract except as provided in (j) of this section.

(u) To avoid waste or to promote conservation of natural resources, the commissioner may authorize the subsurface storage of oil or gas whether or not produced from state land, in land leased or subject to lease under this section. This authorization may provide for the payment of a storage fee or rental on the stored oil or gas, or, instead of the fee or rental, for a royalty other than that prescribed in the lease when the stored oil or gas is produced in conjunction with oil or gas not previously produced. A lease on which storage is so authorized shall be extended at least for the period of storage and so long thereafter as oil or gas not previously produced is produced in paying quantities.

(v) *[Repealed, § 36 ch 94 SLA 1980.]*

(w) Notwithstanding any other provisions of this section, land that was subject to a best interest finding issued within the previous 10 years may be, at the discretion of the commissioner, immediately offered for lease, under regulations adopted by the commissioner, upon terms appearing most advantageous to the state; however, noncompetitive leasing is prohibited. The commissioner shall establish a royalty determined to be in the public interest but not less than 12½ percent. A lease must provide for payment to the state of rental but need not adhere to the rental schedule in (n) of this section nor to the 5,760-acres-per-lease limitation in (m) of this section. The lease term may not exceed 10 years, except as provided in (o) of this section.

(x) A lessee conducting or permitting any exploration for, or development or production of, oil or gas on state land shall provide the commissioner access to all noninterpretive data obtained from that lease and shall provide copies of that data, as the commissioner may request. The confidentiality provisions of AS 38.05.035 apply to the information obtained under this subsection.

(y) A noncompetitive lease existing at October 10, 1978 shall be extended for a period of two years and so long thereafter as oil and gas is produced in paying quantities. A noncompetitive lease extended under this subsection is subject to the regulations in force at the expiration of the initial five-year term of the lease. No extension may be granted, however, unless within a period of 90 days before the expiration date an application for

extension is filed by the record title holder or an assignee whose assignment has been filed for approval, or an operator whose operating agreement has been filed for approval.

(a) No leases may be issued under this section without the inclusion of the following language: "The landowners' royalty share of the unit production allocated to each separately owned tract shall be regarded as royalty to be distributed to and among, or the proceeds of it paid to, the landowners, free and clear of all unit expense and free of any lien for it." Leases issued in violation of this subsection shall, for all purposes, be construed as containing the language required by this subsection.

(aa) Within 90 days after the written request of a lessee of a lease issued under this section or of a lessee of federal land from which the state is entitled under applicable federal law to receive a share of the royalty on gas production, the commissioner shall enter into an agreement with the lessee to use or accept the price for the gas established in the contract between the lessee and a gas or electric utility as the value of the state's royalty share of gas production sold by the lessee under the contract

(1) but only if the primary function of the utility with which the lessee has entered into the contract is to provide, either directly or by selling at wholesale to another utility, gas or electricity to the general public, including residential consumers, within the utilities' service areas, and the utility with which the lessee has entered into the contract is not an affiliated interest, as that term is defined in AS 42.05.990, with the lessee or with a subsequent purchaser of more than 10 percent of the utility's gas or electricity; and

(2) unless the commissioner makes a written finding, based on clear and convincing evidence, that

(A) the contract price is unreasonably low;

(B) the prospective reduction in royalty receipts would not be balanced by increased benefits to in-state gas and electric consumers;

(C) the lessee and the utility are related in management, ownership, or other aspect; and

(D) the contract price is not in the best interest of the state.

(bb) In (aa) of this section,

(1) "gas or electric utility" includes an electric cooperative organized under AS 10.25, a municipal utility, and a gas or electric utility regulated under AS 42.05; provided that if the contract gas is transmitted to consumers through a pipeline and the gas utility either owns the pipeline or is related in ownership to the owner of the pipeline, then the gas utility qualifies as a "gas or electric utility" within the meaning of this paragraph only if it is bound or agrees to be bound by the covenants set out in AS 38.35.120;

(2) "price for the gas established in the contract" includes tax reimbursement amounts, deliverability and other charges, and other forms of consideration paid by the gas or electric utility under the contract;

(3) "state's royalty share of gas production"

(A) includes payments on federal leases made to the state under 30 U.S.C. 191;

(B) does not include the state's royalty share of gas production from land patented to the state under

(i) P.L. 84-830, 70 Stat. 709 (Alaska Mental Health Enabling Act);

(ii) 38 Stat. 1214 (Act of March 4, 1915); or

(iii) 43 U.S.C. 1635 in settlement of the claims of the state under 38 Stat. 1214.

(cc) The provisions of (aa) of this section do not prohibit the commissioner from accepting any payment on a federal lease tendered by the federal agency responsible for determination and transmittal of the payment to the state under 30 U.S.C. 191 or otherwise due the state as the state's royalty share of gas production irrespective of the state's acceptance of the use of the contract price for purposes of determining royalty share on gas production under that subsection. (§ 3(7) art VIII ch 169 SLA 1959; am § 18 ch 61 SLA 1960; am § 1 ch 124 SLA 1962; am §§ 4 — 7 ch 30 SLA 1964; am § 20 ch 70 SLA 1964; am § 2 ch 91 SLA 1967; am § 1 ch 65 SLA 1968; am § 1 ch 88 SLA 1970; am

§ 1 ch 155 SLA 1978; am § 16 ch 160 SLA 1978; am §§ 3, 4 ch 65 SLA 1979; am § 6 ch 18 SLA 1980; am § 36 ch 94 SLA 1980; am §§ 1 — 5 ch 111 SLA 1980; am §§ 11, 12 ch 161 SLA 1984; am § 1 ch 89 SLA 1985; am § 2 ch 65 SLA 1986; am §§ 3, 4 ch 124 SLA 1990; am § 6 ch 134 SLA 1990; am §§ 1 — 3 ch 63 SLA 1993; am §§ 5, 6 ch 35 SLA 1994; am § 1 ch 36 SLA 1994; am §§ 67, 68 ch 21 SLA 1995; am §§ 2 — 6 ch 85 SLA 1995; am § 42 ch 30 SLA 1996; am § 2 ch 63 SLA 1996; am §§ 2 — 4 ch 138 SLA 1996; am § 6 ch 140 SLA 1996)

Revisor's notes. — In 1990, a reference to (m) of this section was deleted from the last sentence of (w) of this section to correct a manifest error in § 4, ch. 124, SLA 1990.

In 1995, in subsection (a), "communization" was substituted for "communication" to correct a manifest error in § 4, ch. 85, SLA 1995.

In 1998, in the first sentence of subsection (a), "communization" was substituted for "communication" to correct a printing error.

In 1996, in subsection (w), "state of rental" was substituted for "state or rental" to correct an error that occurred in printing ch. 155, SLA 1978.

Cross references. — For establishment of drilling units for pools, see AR 31.05.100; for legislative findings in connection with the 1996 amendment to this section, see § 1, ch. 65, SLA 1996, in the Temporary and Special Acts.

For provisions superseding (aa) and (bb) of this section that are applicable to the state's share of royalty production of gas produced after January 2, 1969 and before June 12, 1993 from certain federal leases, see § 4, ch. 63, SLA 1993 in the Temporary and Special Acts.

For legislative authorization of amendment of the Northstar Unit oil and gas leases between the State of Alaska and BP Exploration (Alaska) Inc., see § 3, ch. 138, SLA 1998 Temporary and Special Acts.

Effect of amendments. — The 1995 amendment in subsection (h) substituted "if it is" for "should it be" at the beginning of the third sentence and added the last sentence.

The 1996 amendment added subsections (aa) and (bb).

The first 1990 amendment rewrote subsection (j) and substituted "10 years" for "five years" in the last sentence of subsection (w).

The second 1990 amendment substituted "biennially" for "annually" and "15th day of the first regular session of each legislature" for "fifteenth day of each regular legislative session" in subsection (b).

The 1993 amendment, effective June 12, 1993, in subsection (aa), inserted "or of a lessee of federal land from which the state is entitled under applicable federal law to receive a share of the royalty on gas production" and "or accept," added paragraph (1), added the paragraph (2) designation, and redesignated former paragraphs (1)-(4) as present subparagraphs (2XA)-(2XD) respectively; in subsection (bb), rewrote paragraph (3); and added subsection (c).

The first 1994 amendment, effective August 7, 1994, in subsection (d), made minor stylistic changes and added paragraph (5) (now (2XE)); and, in subsection (f), substituted "Except as provided by AS 38.05.131 — 38.05.134, the" for "The" at the beginning and made minor stylistic changes.

The second 1994 amendment, effective May 10,

1994, in subsection (c), deleted the former second and third sentences, relating to lease sale delays and reschedulings, respectively.

The first 1995 amendment, effective August 8, 1995, in subsection (b), deleted "submit to the legislature" following "prepare and," inserted "notify the legislature of the availability of," and substituted "made available" for "submitted"; and, in the introductory language of subsection (a), substituted "prepare and notify" for "submit to" and inserted "of the availability of."

The second 1995 amendment, effective June 20, 1995, rewrote subsection (j), added the present third sentence in subsection (g), and added the last sentence in subsections (a) and (l).

The first 1996 amendment, effective May 16, 1996, substituted "prepared" for "submitted," and deleted ", to the legislature" in the introductory language of subsection (d).

The second 1996 amendment, effective September 4, 1996, rewrote subsection (f).

The third 1996 amendment, effective October 8, 1996, in subsection (a), in paragraph (2), added the subparagraph (A) designation, redesignated subparagraphs (A) and (B) as (B) and (C), and added subparagraph (B); in subsection (d), added paragraph (1), added the paragraph (2) designation, and redesignated paragraphs (1)-(5) as subparagraphs (A)-(E), and, in subsection (w), rewrote the first sentence.

The fourth 1996 amendment, effective October 9, 1996, inserted a section reference in subsection (f) and made a minor stylistic change.

Editor's notes. — Section 6, ch. 65, SLA 1996 provides that subsection (aa) of this section "applies to agreements to establish for a lease issued under AS 38.05.180 the in-value royalties on gas production that is sold under a contract entered into on or after May 30, 1996, between the state's lessee and a gas or electric utility."

Opinions of attorney general. — Former AS 38.05.306(a) did not apply to actions approving unit agreements in which one automatic consequence of unitization would be extension of the lease term where the leases were issued prior to September 22, 1977, since extension of a lease term upon unitization did not constitute "renewal" within the meaning of former AS 38.05.306(a); moreover, there was good reason to believe that former AS 38.05.306(a) would also be inapplicable in the case of a unit involving state leases issued after September 22, 1977. November 25, 1977, Op. Att'y Gen.

The public notice requirement of AS 38.05.948 probably does not apply in the automatic lease term extension that occurs as a consequence of unitization since such extension is a measure to enhance the feasibility of unitized operation, not a disposal action. November 25, 1977, Op. Att'y Gen.

NOTICE TO DECISIONS

Purpose of section. — The provisions of this section were intended to insure that leases on valuable oil and gas producing state lands will be made available to the public on a fair and equitable basis, that the state will be adequately compensated for its natural resources, and that the state's resources are developed in an orderly fashion. For the commissioner to decide that these purposes are furthered by providing for bidding by cash bonus cannot be said to be unreasonable. *Kelly v. Zamarelli*, 488 P.2d 906 (Alaska 1971).

The assessment of the state's oil and gas resources serves at least two legitimate government objectives. First, knowledge of the production potential of state land in various areas is critical to the determination of where development should occur and where preservation is appropriate. Second, knowledge of the oil and gas production potential of the state's lands promotes the state's economic welfare by maximizing the amount it receives for the lease of its lands. *State, Dept. of Natural Resources v. Arctic Slope Regional Corp.*, 834 P.2d 134 (Alaska 1991).

Construction of section. — The legislature has given the commissioner "broad authority" concerning competitive bidding procedures. *Champion Oil Co. v. Herbert*, 678 P.2d 961 (Alaska), cert. denied, 439 U.S. 980, 99 S. Ct. 565, 58 L. Ed. 2d 650 (1978).

Former subsection (d) of this section did not embody an overbroad delegation of legislative authority to the commissioner. *Champion Oil Co. v. Herbert*, 678 P.2d 961 (Alaska), cert. denied, 439 U.S. 980, 99 S. Ct. 565, 58 L. Ed. 2d 650 (1978).

Power to change law respecting lease extensions is vested in state. — The governmental power to change the law respecting the granting of lease extensions, vested in Congress prior to statehood and preserved by § 6(k) of the Alaska Statehood Act, became vested in the state when the lands subject to the lease were granted to the state as its property. *Kirkpatrick v. Commissioner, Dept. of Natural Resources*, 391 P.2d 7 (Alaska 1964).

And has been exercised by the Alaska Land Act. — The state has exercised its power to change the law respecting lease extensions by the Alaska Land Act and by regulations adopted under its authority. *Kirkpatrick v. Commissioner, Dept. of Natural Resources*, 391 P.2d 7 (Alaska 1964).

Lands classified by Statehood Act as competitive. — The language of this section is not directed to a situation where lands have been classified as competitive by the Alaska Land Act itself, and where there is no room for the exercise of the commissioner's authority to make classifications. *Kirkpatrick v. Commissioner, Dept. of Natural Resources*, 391 P.2d 7 (Alaska 1964) (decided under prior law).

Effect of Alaska Statehood Act and statutes on pre-statehood federal leases. — For effect of the Alaska Statehood Act and statutes enacted by the Alaska State Legislature on oil and gas leases of Alaska lands issued by the United States Department of the Interior while Alaska was a territory of the United States, see *Kirkpatrick v. Commissioner, Dept. of Natural Resources*, 391 P.2d 7 (Alaska 1964).

"Commercial quantities" construed. — See *Pan*

Am. Petroleum Corp. v. Shell Oil Co., 456 P.2d 12 (Alaska 1969).

The words "bonus" and "royalty" in their broadest concepts and meanings are conflicting and overlapping. On the other hand, when it is necessary that they be distinguished, there is a narrower concept of the two terms as they are ordinarily and commonly used and understood in the oil and gas industry in which they do not conflict but are harmonious. In this narrower sense, a reservation or a payment of a part or percentage of production under a lease which is to continue throughout the life of the lease is regarded as "royalty," and a sum certain to be paid in cash or out of production is regarded as "bonus." *Kelly v. Zamarelli*, 488 P.2d 906 (Alaska 1971).

In its broadest sense, "bonus" is any consideration given for a lease over and beyond the usual 16th royalty, whether the additional consideration be paid or payable and whether paid in cash or payable out of production. *Kelly v. Zamarelli*, 488 P.2d 906 (Alaska 1971).

In its broadest aspect, "royalty" is a share of the product or profit reserved by the owner for permitting another to use the property. In this broad sense, a sum certain to be paid out of production, although "bonus" in that it is consideration in addition to the usual 16th royalty, would also be "royalty." *Kelly v. Zamarelli*, 488 P.2d 906 (Alaska 1971).

Choosing concept of "bonus" most commonly encountered. — In choosing the concept of "bonus" most commonly encountered in the oil and gas industry, defendants acted neither unreasonably nor arbitrarily. *Kelly v. Zamarelli*, 488 P.2d 906 (Alaska 1971).

Requiring compensation for lease immediately upon award of lease. — It is not unreasonable for the commissioner to determine that it is in the state's best interest to receive compensation for the lease immediately upon the award of the lease, rather than to wait for uncertain sums to arrive in the form of premium royalties. *Kelly v. Zamarelli*, 488 P.2d 906 (Alaska 1971); *Champion Oil Co. v. Herbert*, 678 P.2d 961 (Alaska), cert. denied, 439 U.S. 980, 99 S. Ct. 565, 58 L. Ed. 2d 650 (1978).

Considering only cash portions of bids. — In considering only the cash portion of plaintiffs' 33 bids, defendants acted pursuant to valid regulations which provided that a lease would be awarded to the bidder offering the highest cash bonus. Since other bids on the 33 tracts contained higher cash offerings than plaintiffs' bids, the defendants acted properly in determining that the high cash bids on those 33 tracts were the apparent high bids, not plaintiffs' bids. *Kelly v. Zamarelli*, 488 P.2d 906 (Alaska 1971).

Commissioner empowered to grant royalty reduction. — This section empowers the commissioner of the Department of Natural Resources, not the director, division of lands, to grant the specified royalty reduction. *Union Oil Co. v. State Dept. of Natural Resources*, 626 P.2d 1357 (Alaska 1974).

Applied in Union Oil Co. v. State, 674 P.2d 1266 (Alaska 1978); *Hammond v. North Slope Borough*, 645 P.2d 760 (Alaska 1982); *Cherron U.S.A., Inc. v. LeRoche*, 683 P.2d 923 (Alaska 1983).

Stated in McKinnon v. Alpetro Co., 833 P.2d 281 (Alaska 1981).

Collateral references. — Abandonment of oil or gas lease by parol declaration, 13 ALR2d 961.

Validity of compulsory pooling or unitization statute or ordinance requiring owners or lessees of oil and gas lands to develop their holdings as a single drilling unit and the like, 37 ALR2d 484.

Oil and gas as "mineral" within deed, lease, or license, 37 ALR2d 1440.

Secondary recovery of oil and gas, 93 ALR2d 451.

Rights of parties to oil and gas lease or royalty deed after expiration of fixed term where production temporarily ceases, 100 ALR2d 886.

Right and measure of recovery for breach of obligation to drill exploratory oil or gas wells, 4 ALR2d 284.

"Dry hole" as "well" within undertaking to drill well, 18 ALR2d 480.

Water use: construction of oil and gas lease provision giving lessee free use of water from lessor's land, 23 ALR2d 1434.

Construction of oil and gas leases as in the lessee's

right and duty of geophysical or seismograph exploration or survey, 28 ALR2d 1429.

Distillate: rights, under oil and gas lease, deed, or sales contract, to "distillate," "condensate," or "natural gasoline", 38 ALR2d 988.

Meaning of "paying quantities" in oil and gas lease, 43 ALR2d 8.

Validity, construction, and application of entirety clause in gas and oil lease, 48 ALR2d 706.

Abandoned well: duty and liability as to plugging oil or gas well abandoned or taken out of production, 60 ALR2d 240.

Grant, lease, exception, or reservation of "oil, gas, and other minerals, or the like," as including coal or metallic ores, 89 ALR2d 1146.

Market value: meaning of, and proper method for determining, market value or market price in oil and gas lease requiring royalty to be paid on standard measured by such terms, 10 ALR4th 732.

Sec. 38.05.181. Geothermal resources. (a) The commissioner may, under regulations adopted by the commissioner, grant prospecting permits and leases to a qualified person to explore for, develop, or use geothermal resources. When title to the surface parcel is held by a person other than the state, that person shall have a preferential right to a geothermal prospecting permit or lease for the area underlying the surface parcel. The surface owner must exercise the preference right within 30 days after receiving notice of the application for a permit, or by agreeing to meet the terms of a bid within 60 days after receiving notice of the acceptance of the bid for a lease.

(b) The commissioner may designate a geothermal area or portion of it a competitive geothermal area. A designation as a competitive geothermal area must be on the basis of substantial geologic indications of geothermal resources or on the basis of competitive interest in geothermal resources of the area.

(c) On state land that has not been declared a competitive geothermal area or withdrawn from geothermal prospecting, the commissioner may issue a prospecting permit to the first qualified applicant. The permit conveys an exclusive right, for a period of two years, to prospect for geothermal resources on state land included under the permit. The commissioner has discretion to renew the permit for an additional one-year term. A holder of a prospecting permit has the right, upon the showing of a discovery of geothermal resources in commercial quantities and the submission of a development plan acceptable to the commissioner, to convert the permit to a noncompetitive lease at a royalty rate under (g) of this section. The conversion privilege must be exercised not later than 30 days after the expiration of the permit. If the land included within the permit is designated a competitive geothermal area during the permit term, the permitter must apply for a noncompetitive lease within 30 days after notification of the designation or forfeit the conversion privilege and the exclusive right to prospect.

(d) On state land that is designated a competitive geothermal area and is not subject to an existing prospecting permit, the commissioner may issue geothermal leases to the highest bidder by competitive bidding procedures established by regulations adopted by the commissioner. At the discretion of the commissioner, competitive lease sales may be by oral or sealed bid, on the basis of a cash bonus, profit share, or royalty share.

(e) Prospecting permits and geothermal leases granted under this section must, except in the case of parcels subject to a preference right under (b) of this section, be issued for at least 40 acres but not more than 2,560 acres. A person may not own, or hold an interest in, geothermal leases covering more than 51,200 acres. However, geothermal leases in commercial production, individually or under a unit operation or well spacing or pooling arrangement, do not count against the acreage limitation. All prospecting permits and geothermal leases are subject to an annual rental, payable in advance, of \$3 per acre. The rental for a year shall be credited against royalties accruing for that year.

(f) A geothermal lease shall be issued for a primary term of 10 years and may be renewed for an additional term of five years if the lessee is actively engaged in drilling operations. A geothermal lease is valid for the duration of commercial production. Beginning 20 years after the initiation of commercial production and at 10-year intervals thereafter, the commissioner may renegotiate the rentals and royalties due on a geothermal lease.

(g) Each geothermal lease shall be conditioned upon payment by the lessee of a royalty of not less than 10 percent but not more than 15 percent of the gross revenues derived from the production, sale, or use of geothermal resources under the lease. Royalties may be taken in kind rather than in value if the commissioner determines that taking in kind would be in the best interest of the state.

(h) Regulations adopted by the commissioner to implement this section shall be adopted in accordance with the Administrative Procedure Act (AS 44.62). (§ 1 ch 71 SLA 1971; am § 6 ch 104 SLA 1971; am §§ 34 — 36 ch 71 SLA 1972; am §§ 40, 41 ch 127 SLA 1974; am § 4 ch 175 SLA 1980)

Cross references. — For geothermal resources generally, see AS 41.06. For legislative policy with respect to geothermal resources, see § 1, ch 175, SLA 1980 in the Temporary and Special Acts.

Collateral references. — Construction and appli-

cation of Geothermal Steam Act of 1970 (30 USCS § 1001 et seq.), pertaining to leases of government lands for development of geothermal steam resources, 40 ALR 7ed 814.

Sec. 38.05.182. Royalty on natural resources. (a) Any royalty provided for in AS 38.05.135 — 38.05.181 may be taken in kind rather than in money if the commissioner determines that the taking in kind would be in the best interest of the state. However, royalties on oil and gas shall be taken in kind unless the commissioner determines that the taking in money would be in the best interest of the state.

(b) The commissioner shall submit a determination to take royalty in money to the legislature at the first opportunity during a current session or, if the legislature is not in session, at the next regular session. The legislature, within 60 days or by the adjournment of the session, whichever comes sooner, may revoke the determination by concurrent resolution. (§ 1 ch 56 SLA 1970; am § 7 ch 71 SLA 1971; am § 1 ch 9 SSSLA 1974; am § 5 ch 218 SLA 1976; am § 1 ch 146 SLA 1977; am § 8 ch 112 SLA 1980)

Revisor's notes. — Enacted as AS 38.05.182. Renumbered in 1970.

NOTES TO DECISIONS

Quoted in *McKinnon v Alpetco Co.*, 833 P2d 281 (Alaska 1981)

Collateral references. — 38 Am Jur 2d, Gas and Oil, §§ 189 to 198.
64 C.J.S., Mines and Minerals, §§ 185 to 192, 213 to 218.

What constitutes "royalty" on oil or gas production within language of conveyance, exception or reservation, 4 ALR2d 482.

Construction and effect of provision in mineral lease requiring payment of minimum rent or royalty, 28 ALR2d 1013.

Solid mineral royalty as real or personal property, 64 ALR2d 728.

Solid mineral royalty under mining lease as real or

personal property for purpose of payment of damages in condemnation proceedings, 68 ALR2d 736.

Expenses and taxes deductible by lessee in computing lessor's oil and gas royalty or other return, 73 ALR2d 1068.

Payment of stipulated minimum royalties or annual rental under solid mineral lease as precluding lessor's claim of forfeiture or abandonment, 87 ALR2d 1076.

"Shut-in royalty" payment provisions in oil and gas leases, 96 ALR2d 346.

Rights of parties to oil and gas lease or royalty deed after expiration of fixed term where production temporarily ceases, 100 ALR2d 885.

disposal in whole or in part of a right to receive future mineral production under a state lease under this chapter, shall be by competitive bid and the sale, exchange or other disposal made to the highest responsible bidder, except that competitive bidding is not required when the commissioner, after prior written notice to the Alaska Royalty Oil and Gas Development Advisory Board under AS 38.06.050, determines that the best interest of the state does not require it or that no competition exists.

(b) When competitive bids are required, the commissioner, after prior written notice to the Alaska Royalty Oil and Gas Development Advisory Board, may reject all bids on a determination that because of the amount of the bids, the lack of responsibility on the part of the bidders, or for reasons consistent with the criteria set out in AS 38.06.070, the acceptance of the bids would not be in the best interest of the state.

(c) If the commissioner determines that a sale, exchange or other disposal of a mineral obtained by the state as a royalty under AS 38.05.182 or of a right to receive future mineral production under a state lease under this chapter shall be made otherwise than by competitive bid, and the Alaska Royalty Oil and Gas Development Advisory Board has been notified in writing of that determination, the commissioner shall make public in writing the specific findings and conclusions upon which that determination is based.

(d) Oil or gas taken in kind by the state as its royalty share may not be sold or otherwise disposed of for export from the state until the commissioner determines that the royalty-in-kind oil or gas is surplus to the present and projected intrastate domestic and industrial needs. The commissioner shall make public, in writing, the specific findings and reasons on which the determination is based.

(e) When a sale, exchange or other disposal of oil or gas taken in kind by the state as its royalty share, or a sale, exchange or other disposal in whole or in part of a right to receive future royalty oil or gas, under a state lease under this chapter is made other than by competitive bid, the sale, exchange or other disposal shall be awarded by the commissioner to the prospective buyer whose proposal offers the maximum benefits to citizens of the state. The commissioner shall consider

- (1) the cash value offered;
- (2) the projected effects of the sale, exchange or other disposal on the economy of the state;
- (3) the projected benefits of refining or processing the oil or gas in the state;
- (4) the ability of the prospective buyer to provide refined products or by-products for distribution and sale in the state with price or supply benefits to the citizens of the state; and
- (5) the criteria listed in AS 38.06.070(a).

(f) The commissioner may not enter into a contract for the sale of royalty oil unless the contract provides that any material amendment to the contract that appreciably reduces the consideration received by the state requires prior approval of the legislature.

(g) AS 38.05.035(e) does not apply to a sale, exchange, or other disposal of oil or gas under this section.

(h) Upon legislative approval, the commissioner may enter into a contract to sell royalty gas taken in kind by the state to a gas or electric utility at a negotiated price for the gas if the commissioner, after considering the consumer benefits, other benefits, and detriments of the sale, makes a written finding that the sale is in the best interest of the state. In this subsection,

- (1) "gas or electric utility" has the meaning given in AS 38.06.180(bb);
- (2) "royalty gas taken in kind by the state" does not include royalty gas taken in kind by the state from gas production on land patented to the state under
 - (A) P.L. 84-830, 70 Stat. 709 (Alaska Mental Health Enabling Act);
 - (B) 38 Stat. 1214 (Act of March 4, 1915); or
 - (C) 43 U.S.C. 1635 in settlement of the claims of the state under 38 Stat. 1214. (§ 1 ch 58 SLA 1970; am § 3 ch 9 SSSLA 1974; am §§ 9, 10 ch 112 SLA 1980; am § 2 ch 68 SLA

1984; am § 2 ch 105 SLA 1984; am § 1 ch 64 SLA 1985; am § 3 ch 55 SLA 1986; am § 6 ch 134 SLA 1990)

Revisor's notes. — Enacted as AS 38.05.183. Renumbered in 1970.

Cross references. — For legislative findings in connection with the 1986 amendment to this section, see § 1, ch 55, SLA 1986, in the Temporary and Special Acts.

Effect of amendments. — The 1986 amendment added subsection (g).

The 1990 amendment added subsection (h).

The 1990 amendment deleted a provision pertaining to an annual report by the commissioner at the end of the second sentence of subsection (d).

NOTES TO DECISIONS

Waiver of competitive bidding. — An initial waiver of competitive bidding and a second waiver at the time of amendment removed any obligation to

open the contract to competitive bidding. *McKinnon v. Alpetco Co.*, 833 P.2d 281 (Alaska 1981).

Sec. 38.05.184. Limitation on oil and gas leases in certain areas, and reacquisition of leases. (a) The legislature finds that Kachemak Bay is an area of extraordinary abundance and diversity of marine life that has provided, and will continue to provide in the future, a basis for one of the state's most important commercial fisheries; that recent information discloses that even minute quantities of oil released into the marine environment may be harmful to the larval forms of crabs and other marine life and that the existence of gyral currents within the bay may increase the likelihood of oil coming into contact with these valuable commercial fish and shellfish species; and that therefore oil and gas development in the bay, at this time, presents an undue hazard to this valuable state renewable resource.

(b) No additional oil or gas leases may be issued by the department or any other state agency for the exploration for or the development or production of oil and gas on state-owned land and waters seaward of the mean higher high water line, beginning at Anchor Point; then around the perimeter of Kachemak Bay, to Point Pogibshi; then west to the three mile limit of state land and waters; then north to a point three miles west of Anchor Point; then east to the mean higher high water line of Anchor Point, the point of beginning.

(c) [Repealed, § 61 ch 50 SLA 1989.]

(d) [Repealed, § 61 ch 50 SLA 1989.]

(e) [Repealed, § 61 ch 50 SLA 1989.]

(f) [Repealed, § 61 ch 50 SLA 1989.]

(g) [Repealed, § 61 ch 50 SLA 1989.] (§ 1 ch 113 SLA 1976; am § 61 ch 50 SLA 1989)

Effect of amendments. — The 1989 amendment, effective May 27, 1989, repealed subsections (c) — (g).

Article 7. Mining Rights.

Section	Section
188 Generally	230 Lien for performance of annual labor
190 Qualifications	235 Lien for annual labor is independent of other liens
195 Mining claims	240 Labor defined for AS 38.05.210 — 38.05.235
200 Changes in locations and amended notices	242 Definitions for AS 38.05.210 — 38.05.240
205 Mining leasing	245 Prospecting sites
207 Production license	250 Prospecting permits and leases on tide and submerged land
210 Annual labor	252 Extralateral rights under shore, tide, and submerged land
211 Annual rental	255 Surface use of land or water
212 Production royalty	255 Abandonment
215 Notice to co-owners to contribute to cost of annual labor or improvements and forfeiture for failure to contribute	270 Transfer
220 Recording the notice to contribute and affidavits	275 Recognition of locations
225 Lienholder may perform the annual labor	

Editor's notes. — Section 18, ch. 75, SLA 1987 or not the land was classified if other requirements of law were met." provides that "all minerals management or disposal decision made before June 18, 1987, is valid, whether

Sec. 38.05.185. Generally. (a) The acquisition and continuance of rights in and to deposits on state land of minerals, which on January 3, 1959, were subject to location under the mining laws of the United States, shall be governed by AS 38.05.185 — 38.05.275. Nothing in AS 38.05.185 — 38.05.275 affects the law pertaining to the acquisition of rights to mineral deposits owned by any other person or government. The director, with the approval of the commissioner, shall determine that land from which mineral deposits may be mined only under lease, and, subject to the limitations of AS 38.05.300, that land that shall be closed to mining. State land may not be closed to mining or mineral location except as provided in AS 38.05.300 and unless the commissioner makes a finding that mining would be incompatible with significant surface uses on the state land. State land may not be restricted to mining under lease unless the commissioner determines that potential use conflicts on the state land require that mining be allowed only under written leases issued under AS 38.05.205 or the commissioner has determined that the land was mineral in character at the time of state selection. The determinations required under this subsection shall be made in compliance with land classification orders and land use plans developed under AS 38.05.300.

(b) The failure on the part of a mining lessee or a locator to comply strictly with AS 38.05.185 — 38.05.275 and regulations adopted under those sections does not invalidate the rights of a mining lessee or a locator if it appears to the satisfaction of the commissioner that the mining lessee or the locator complied as nearly as possible under the circumstances of the case, and that no conflicting rights are asserted by any other person.

(c) Unless otherwise provided, the usages and interpretations applicable to the mining laws of the United States as supplemented by state law apply to AS 38.05.185 — 38.05.275. (§ 1 art. IX ch 169 SLA 1959; am § 19 ch 81 SLA 1960; am § 1 ch 123 SLA 1961; am § 1 ch 108 SLA 1981; am § 1 ch 52 SLA 1993)

Revisor's notes. — In 1984, the phrase "the mining leases or" was inserted following "the satisfaction of the commissioner that" in (b) of this section under AS 01.05.031(b)(7); and the former last sentence of (b) was designated as subsection (c).

Cross references. — For location and develop-

ment of mining claims on federal public domain, see AS 27.10.

Effect of amendments. — The 1993 amendment, effective September 1, 1993, in subsection (a), made minor stylistic changes and, in the fourth sentence, inserted "except as provided in AS 38.05.300 and"

NOTES TO DECISIONS

Applied in *Hayes v. A.I. Asasca*, 846 P.2d 131 (Alaska 1993).

Cited in *Trustees for Alaska v. State*, Dep't of

Natural Resources, 736 P.2d 324 (Alaska 1987); *Kile v. Bellini*, 758 P.2d 1282 (Alaska 1988).

Collateral references. — 54 Am. Jur. 2d, Mines and Minerals, §§ 23, 167.
58 C.J.S., Mines and Minerals, § 4 et seq.

Sec. 38.05.190. Qualifications. (a) The right to acquire exploration and mining rights under AS 38.05.185 — 38.05.275 may be acquired or held only by

- (1) citizens of the United States at least 18 years of age;
- (2) legal guardians or trustees of citizens of the United States under 18 years of age on behalf of the citizens;
- (3) persons at least 18 years of age who have declared their intention to become citizens of the United States;