

HB

286

SFIN

FILE

SENATE FINANCE COMMITTEE REPORT

REPORTED OUT

MAY 6 2005

SENATE FINANCE
COMMITTEE

DATE: 5/5/05

FURTHER:

DATE TURNED
IN TO OFFICE: 6 May 2005

Finance Committee considered

HOUSE BILL NO. 286

HB 286 VALUE OF ROYALTY ON GAS PRODUCTION

"An Act amending the manner of determining the royalty received by the state on gas production by directing the commissioner of natural resources to accept, under certain circumstances, the transfer price of the gas if established by transfer price order of the Regulatory Commission of Alaska; and providing for an effective date."

and recommends:

- be replaced with _____ CS _____ (_____)
- adopt previous 5 CS HB 286 (RES)
- attached amendment(s)
- adopt Letter of Intent by _____ Committee
- further referral to _____ Committee

CS Senate Bill:
 Same Title
 New Title

SCS House Bill:
 Same Title
 Technical Title
 Change
 New Title w/
 SCR # 16

~~NEW~~ ^{PREVIOUS} FISCAL NOTE(S):

Department	Date	Fiscal	Ind.	Zero	FN#
DNR	5/5/05			✓	#2
Revenue	5/5/05		*		#3
DCCED	5/5/05			✓	#4

PREVIOUS FISCAL NOTE(S):

Department	Date	Fiscal	Ind.	Zero	FN#
Commerce	4/21/05			✓	#1

APPROPRIATION - no fiscal note

SIGNATURES AND RECOMMENDATIONS:	DO PASS	DO NOT PASS	NO REC	AMEND
<i>[Signature]</i>			✓	
<i>[Signature]</i>			✓	
<i>[Signature]</i>	✓			
<i>[Signature]</i>	✓			
COCHAIR: <i>[Signature]</i>	✓			
COCHAIR: <i>[Signature]</i>	✓			

FISCAL NOTE

REPORTED OUT

MAY 6 2005

SENATE FINANCE
COMMITTEE

STATE OF ALASKA
2005 LEGISLATIVE SESSION

Fiscal Note Number: _____
Bill Version: SCS HB 286(res)
() Publish Date: _____

Revision Date/Time (Note if correction): _____ Dept. Affected: Revenue 04
Title Production Tax Credits RDU Tax and Treasury
Component Tax
Sponsor Rep. Samuels
Requester Senate Resources Component No. 2476

Expenditures/Revenues (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

OPERATING EXPENDITURES	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
Personal Services						
Travel						
Contractual						
Supplies						
Equipment						
Land & Structures						
Grants & Claims						
Miscellaneous						
TOTAL OPERATING

CAPITAL EXPENDITURES						
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CHANGE IN REVENUES ()						
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FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1037 GF/Mental Health						
Other (Specify Type--Do not abbreviate)						
TOTAL

Estimate of any current year (FY2005) cost: 0.0
Check this box (X) if funding for this bill is included in the Governor's FY 2006 budget proposal:

POSITIONS

Full-time						
Part-time						
Temporary						

ANALYSIS: (Attach a separate page if necessary)

This fiscal note only treats the tax related sections, sections 2 - 8.

This bill improves the AS 43.55.025 (production tax) exploration credit program enacted in 2003 in several important ways. It creates new rules in the Cook Inlet more appropriate for encouraging exploration in a well-explored, mature basin. It extends the time available for performing work that will qualify for the credit out to 2010 for everywhere except the North Slope. This should be particularly important in the Alaska Peninsula area where DNR has proposed a lease sale for the fall of 2005, as well as areas with exploration licenses. Finally, the bill introduces clarifying language about when the 20% , 40 % (and lack of opportunity for an 80%) credit apply. (continued on next page)

Prepared by: Dan Dickinson & Greg Bidwell Phone 269-6620
Division Tax Division Date/Time 5/5/05 8:12 AM
Approved by: Jerry Burnett, Special Assistant to the Commissioner Date 5/5/2005
Agency Department of Revenue

FISCAL NOTE

STATE OF ALASKA
2005 LEGISLATIVE SESSION

BILL NO. HB 286

ANALYSIS CONTINUATION

Although the credit will decrease state revenues in the short term, it should increase them over the long term. However it is impossible to predict with any certainty the exact size of either effect. Some of the considerations affecting revenues:

Given the infrastructure already developed in the Cook Inlet, minimum fields sizes smaller than 10 million barrels or 40 billion cubic feet of gas may be economic to develop. More typical fields in the Cook Inlet would be 20 million barrels of oil and 200 bcf of gas. Though it may take several years to bring into production, state revenue (royalty production tax, property tax and corporate income tax) from such an oil field would average 50 million dollars for its first producing decade. Gas fields can be brought on more quickly, and such a typical gas field could average \$180 million dollars in state revenue over its first decade. Thus if this program results in one or more typical incremental production opportunities from the Cook Inlet it will more than pay for itself.

At levels of exploration seen over the past several years, the 20 million dollar cap will kick in between 3 and 4 years from now. If there is incremental exploration, the cap will be reached earlier.

In the Alaska Peninsula, while we expect wells to be drilled from onshore facilities, given the remoteness of the region and the lack of infrastructure, we assume that on average these wells will qualify for a 30% credit, half qualifying for the 40% and half qualifying for the 20% credit. Thus we estimate \$7 million dollars a year in credits if there is sufficient Alaska Peninsula exploration. The credit might promote higher bidding (and thus state revenues) in the lease sale. We estimate the minimum economic fields size to be between 100 million and 200 million barrels of oil. Such a field, if discovered and developed, could yield about \$500 million dollars in state revenues over the first decade of production. Thus, if successful, the program will pay off more than an order of magnitude more than its costs.

Section 2 rewrites the statutory language to clear up confusion that has arisen over the original language. It makes clear that there are only four possible situations:

- (1) Well work more than three miles from an existing well, but not more than 25 miles from a unit that qualifies for a 20% credit,
- (2) Well work more than 25 miles from an existing unit but not more than 3 miles from an existing well that qualifies for a 20% credit (although this portion of the credit expires June 30, 2007),
- (3) Well work that is both 25 miles from an existing unit and 3 miles from an existing well that qualifies for a 40% credit, and
- (4) Seismic work not associated with a well that qualifies for a 40% credit.

There is no way to combine these to get an 80% credit for any given dollar outlay.

Section 3 does two things. It extends the sunset of the existing credit from 2007 to 2010 for all work performed south of the Brooks Range. In the Cook Inlet, while also extending the sunset to 2010, section 3 also sets new rules, effective July 1 2005, more appropriate for a mature basin like the Cook Inlet.

Section 4 harmonizes statute section (c) with the section one rewrites, and for the Cook Inlet introduces the notion that if the commissioner of DNR certifies that the target is separate exploration target, the well work qualifies for the credits as though it were three miles from another well – even though it may be closer.

Section 5 also has language that harmonizes statute section (d) with the other changes, and for the Cook Inlet reduces the qualifying distance from an existing unit from 25 miles to 10 miles.

Section 6 harmonizes section (e) with the earlier changes.

Section 7 clarifies the process whereby a Cook Inlet explorer can get the required certification from the commissioner of DNR to qualify for the credit with a separate exploration target. It also further limits the total of special Cook Inlet credit to 20 million dollars.

Section 8 sets forth several definitions pertinent to Cook Inlet.

MAY 6 2005

SENATE FINANCE
COMMITTEE

FISCAL NOTE

STATE OF ALASKA
2005 LEGISLATIVE SESSION

Fiscal Note Number: _____
Bill Version: HB286SCS(RES)-DNR-C
() Publish Date: _____

Revision Date/Time (Note if correction): _____ Dept. Affected: Natural Resources
Title: Value of Royalty on Gas Production RDU: Resource Development
Component: Oil and Gas Development
Sponsor: Rep. Samuels
Requester: Senate Finance Component No.: 439

Expenditures/Revenues (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

OPERATING EXPENDITURES	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
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						
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CHANGE IN REVENUES ()	***Indeterminate
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FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1037 GF/Mental Health						
Other (Specify Type--Do not abbreviate)						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

Estimate of any current year (FY2005) cost: 00

Check this box (X) if funding for this bill is included in the Governor's FY 2006 budget proposal:

POSITIONS

Full-time						
Part-time						
Temporary						

ANALYSIS: (Attach a separate page if necessary)

Section 1 of this bill amends AS 38 05 180(aa), a statute that relates to the royalty value of gas sold to a gas or electric utility that serves the general public. Under the state's oil and gas leases, a producer-lessee must pay the state royalties-in-value (cash) or royalties-in-kind (oil or gas). If the producer pays the gas royalty in-value, meaning that the producer sells the gas to its customer and then tenders a payment to the state, the producer is liable under the lease for a royalty value that is the higher of the producer's actual sales price (less certain allowed deductions) or the average royalty values for other producers in the same area based on their sales.

Under current law, AS 38 05 180(aa) provides that a gas producer can apply to the Commissioner of the Department of Natural Resources (the department) to have its royalty gas valued at its contract sales price to the utility.
(Continued on next page)

Prepared by: Mark D. Myers, Director Phone: 269-8E J0
Division: Oil and Gas Date/Time: 5/5/2005
Approved by: Tom Irwin, Commissioner Date: 5/5/2005
Agency: Natural Resources

FISCAL NOTE

STATE OF ALASKA
2005 LEGISLATIVE SESSION

BILL NO. HB286SCS(RES)-DI

ANALYSIS CONTINUATION

If the Commissioner approves the application, the state gives up the higher of value under the lease, relating to the average sales prices received by other producers as noted above. To obtain approval under AS 38.05.180(aa), the producer must present a negotiated, third-party arm's length contract for the Commissioner's consideration.

Section 1 would change current law to allow a producer-lessee that transfers its gas to an affiliated utility to apply for AS 38.05.180(aa) treatment. Under the bill, if a producer-lessee has an internal transfer price for gas consumed by its utility approved for ratemaking purposes by the Regulatory Commission of Alaska, it could apply to the department to have its transfer price used as its royalty value. In the absence of HB 286, the department would use the higher of value to determine the royalty value.

This bill (sections 2-8) would also extend the sunset date until 2010 on oil and gas exploration credits against production tax (SB 185, CH 59, SLA 03) for all areas south of 68 degrees, 15 minutes North latitude (south of the Brooks Range). It also amends the qualifications for work done in the Cook Inlet sedimentary basin.

***Indeterminate. Section 1: The department is unable to determine whether enacting HB 286, section 1 would have a negative fiscal impact on the state. If the transfer price were used for the royalty value, as the bill would permit with department approval, the impact would be negative if the transfer price was lower than the average of other producers' royalty values.

Indeterminate. Sections 2 - 8: The proposed Alaska Peninsula sale is tentatively scheduled for fall of 2005. An extension of the sunset deadline to the proposed Alaska Peninsula sale area may encourage additional or higher competitive bids, although these additional revenues are impossible to predict or quantify.

MAY 6 2005

SENATE FINANCE
COMMITTEE

FISCAL NOTE

STATE OF ALASKA
2005 LEGISLATIVE SESSION

Fiscal Note Number: _____
Bill Version: SCSHB 286 (RES)
() Publish Date: _____

Revision Date/Time (Note if correction): _____ Dept. Affected: Commerce
Title Value of Royalty on Gas Production RDU Regulatory Commission of Alaska (399)
Component Regulatory Commission of Alaska
Sponsor Samuels
Requester Senate Resources Component No. 2417

Expenditures/Revenues (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

OPERATING EXPENDITURES	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
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						
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CHANGE IN REVENUES ()						
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FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1037 GF/Mental Health						
Other (Specify Type--Do not abbreviate)						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

Estimate of any current year (FY2005) cost: 0.0
Mark this box (X) if funding for this bill is included in the Governor's FY 2006 budget proposal:

POSITIONS

Full-time						
Part-time						
Temporary						

ANALYSIS: (Attach a separate page if necessary)

This legislation contemplates changes to DNR's statute, AS 38, by directing the DNR Commissioner to accept, under certain circumstances, the transfer price of the gas if established by transfer price order of the Regulatory Commission of Alaska. Such activity is within the scope of the RCA's normal operations; consequently, no fiscal impact on the agency is anticipated.

Prepared by: Kate Giard, Chairman Phone (907) 263-2110
Division Regulatory Commission of Alaska Date/Time 5/5/05 9 54 AM
Approved by: Edgar Blatchford, Commissioner Date 5/5/2005
Agency Commerce, Community, and Economic Development



REPRESENTATIVE RALPH SAMUELS

HOUSE DISTRICT 29

Sponsor Statement

HB 286

"An Act amending the manner of determining the royalty received by the state on gas production by directing the commissioner of natural resources to accept, under certain circumstances, the transfer price of the gas if established by transfer price order of the Regulatory Commission of Alaska; and providing for an effective date."

Anchorage Municipal Light and Power is proposing a housekeeping amendment to AS 38.05.180(aa). The amendment will allow the Department of Natural Resources to use the transfer price for gas set by the Regulatory Commission of Alaska to value the State's share of royalty gas. The amendment reflects language as proposed by ML&P and modified at DNR's request. DNR does not oppose this amendment.

Since 1986, Alaska utilities have been able to use the price set in their long-term gas purchase contracts as the value for royalty gas values.

ML&P has used (aa) for the gas ML&P uses from its share of the Beluga River Field. DNR agreed to let ML&P continue to receive (aa) treatment based on the ML&P/Shell contract even after ML&P bought Shell's interest in the field. But that contract expires at the end of 2005. While ML&P's share in the Beluga River Field will assure ML&P of a supply of gas, in the absence of the proposed legislation, ML&P will not be able to continue to receive (aa) treatment for its gas.

The proposed legislation adds language that allows DNR to use the gas transfer price set by the RCA much like DNR uses the contract price for gas. The transfer price is the rate ML&P is required to charge itself for the Beluga Field gas it uses. The proposed amendment allows DNR to give (aa) treatment not only to an arms-length gas supply contract, but also to RCA-approved orders setting the transfer price when a utility uses its own natural gas.

The proposed amendment is consistent with the purpose of the original law. It will allow ML&P to continue to receive the benefits the Legislature intended to provide to consumers. It assures that rigorous and fair regulatory process will be used to set the price for royalty gas. The fiscal impact will be minimal compared to the (aa) treatment ML&P presently receives. This amendment will help ensure that Anchorage electric consumers have certainty and stability in their electric rates.

Email: Representative_Ralph_Samuels@legis.state.ak.us

Session: Alaska State Capitol, Juneau, Alaska 99801-1182 • Phone: (907) 465-2095 Fax: (907) 465-3810
Interim: 716 W. 4th Ave., Anchorage, Alaska 99501-2133 • Phone: (907) 269-0240 Fax: (907) 269-0242

ALASKA STATE LEGISLATURE



Official Business

SENATE RESOURCES COMMITTEE

Senator Tom Wagoner, Chair

State Capitol, Room 427

Juneau, AK 99801-1182

Phone: (907) 465-4907 Fax: (907) 465-4779

Senator Ralph Seekins, Vice-Chair

Senator Ben Stevens

Senator Kim Elton

Senator Fred Dyson

Senator Bert Stedman

Senator Gretchen Guess

SCS HB 286(RES)

Bill Explanation & Sectional Description

The Exploration Credits are now contained in this bill that accomplishes the following:

1. It extends the exploration credits adopted in 2003 to July 2, 2010, for every place in Alaska south of the Brooks Range.
2. It adopts a new set of rules for credits in the Cook Inlet Basin from 2005-2010.
3. It clarifies that certain situations have credits authorized through 2007 and that the new extended credits are under a different "situation" or standard.
4. It reinserts the Arctic National Wildlife Refuge for qualifying for the original credit, which is set to expire in 2007.

Sec. 1: Original HB 286

Sec. 2: Rewrites statute to conform to regulations developed for original credits and states that subsection (2) language is specific only to credits expiring in 2007.

Sec. 3: Extends sunset from 2007 to 2010 for work south of the Brooks Range and sets a time line for Cook Inlet basin credits - July 1, 2005 to July 1, 2010.

Sec. 4: Makes changes so Section 1 language is more precise and authorizes a "within 3 mile" standard for the Cook Inlet if the DNR commissioner certifies it as a separate exploration target.

Sec. 5: Makes changes so Section 1 language is more precise and reduces the distance from 25 miles to 10 miles for the Cook Inlet basin.

Sec. 6: Changes one phrase to make Section 1 language more precise.

Sec. 7: Clarifies process for Cook Inlet credits from DNR commissioner and limits Cook Inlet credits to 20 million dollars.

Sec. 8: Definitions relevant to Cook Inlet basin.

Sec. 9: Immediate effective date.

SENATE COMMITTEE REPORT

DATE: 5/3/05

FURTHER: Finance

DATE TURNED
IN TO OFFICE: 5/5/05

Resources Committee considered HOUSE BILL NO. 286

HB 286 VALUE OF ROYALTY ON GAS PRODUCTION

"An Act amending the manner of determining the royalty received by the state on gas production by directing the commissioner of natural resources to accept, under certain circumstances, the transfer price of the gas if established by transfer price order of the Regulatory Commission of Alaska; and providing for an effective date."

and recommends:

- be replaced with SCS HB 286 (RES) (_____)
- adopt previous _____ CS _____ (_____)
- attached amendment(s)
- adopt Letter of Intent by _____ Committee
- further referral to _____ Committee

CS Senate Bill:	
<input type="checkbox"/> Same Title	
<input checked="" type="checkbox"/> New Title	
SCS House Bill:	
<input type="checkbox"/> Same Title	
<input type="checkbox"/> Technical Title Change	
<input checked="" type="checkbox"/> New Title w/ SCR # <u>16</u>	

NEW FISCAL NOTE(S):

Department	Date	Fiscal	Indet.	Zero	FN#
DNR	5/5/05	✓			2
REV	5/5/05	✓			3
CEC	5/5/05			✓	4

PREVIOUS FISCAL NOTE(S):

Department	Date	Fiscal	Indet.	Zero	FN#
CEC	4/28			✓	1

APPROPRIATION - no fiscal note

SIGNATURES AND RECOMMENDATIONS:	DO PASS	DO NOT PASS	NO REC	AMEND
DYSON <i>[Signature]</i>	✓			
B STEVENS <i>[Signature]</i>	✓			
STEDMAN <i>[Signature]</i>	✓			
DEEKINS <i>[Signature]</i>	✓			
GUESS <i>[Signature]</i>			X	
WAGNER <i>[Signature]</i> CHR L	✓			
CHAIR: <i>[Signature]</i> ELTON			✓	