

2/01/12

BUDGET

OVERVIEW:

DEPARTMENT

OF LAW

MEMORANDUM

State of Alaska
Department of Law

TO: Representative Dugan
House Finance Committee

DATE: February 9, 2012

THROUGH: Representative Bill Stoltze
Co-Chair
House Finance Committee

TEL. NO: 465-3673

FROM: Dave Blaisdell, Director
Administrative Services
Department of Law

SUBJECT: Oil, Gas and Mining
Outside Counsel funding
for Department of Law

In House Finance Committee meeting on February 1st, you requested additional information on the Department of Law's \$9.05 million undesignated general fund request (UGF). I understood your question was whether the funding was an increase from the previous year and centered around the information provided on page 144 of Legislative Finance's, *The Fiscal Year 2013 budget: Legislative Fiscal Analyst's Overview of the Governor's Request*.

The request is not a \$9.05 million increase from FY12 and should be viewed as maintenance level funding. The chart below compares the amounts appropriated for FY12 and the FY13 request:

	FY12	FY13 Req
Outside Counsel – unrelated to the Gasline	\$ 8,116.0 *	\$ 6,150.0
Gasline funding	\$ 2,000.0	\$ 2,900.0
Total funding	\$ 10,116.0	\$ 9,050.0

*Including supplemental request

The \$6,150.0 is being treated as an increment in the budget but would be added to the Department's base budget as presented in the FY13 budget request. The \$2,900.0 is being treated as a one-time increment and will be backed out of the FY13 base by Legislative Finance and any related funding would be treated as an increment in the FY14 budget request.

Please let me know if you have additional questions.

2/8/12



Department of Law

Photo by Sheena Scott, © Law Webmaster



FY 13 Budget Overview

1/31/2012



MISSION

The Alaska Department of Law prosecutes crime and provides legal services to state government for the protection and benefit of Alaska's citizens.

Core Services

- Protecting the Safety and Financial Well Being of Alaskans
- Fostering Conditions for Responsible Development of Our Natural Resources
- Protecting the Fiscal Integrity of the State
- Promoting Good Governance

KEY STATISTICS (FY 13 GOVERNOR'S REQUEST)

Division	Attorneys	Support Staff	Total
Civil	166	141	307
Criminal	127	118	245
Administrative Services	2	19	21
Total	295	278	573

FY 13 Operating Budget Request

(Millions)

Division	FY13 Governor's Budget Request	FY12 Management Plan	Change
Civil	58.9	53.8*	5.1
Criminal	33.8	32.6	1.2
Administrative Services	4.5	4.2	0.3
BP Corrosion	0.0	9.0	<9.0>
Total	97.2	99.6	<2.4>

*Includes multi-year operating of \$2.0 million carried forward into FY12

FY 11 Return on Investment (Millions)

Commercial and Fair Business	7,036,470
Medicaid Recovery work	2,527,681
Environmental	3,129,127
Collections Unit	10,586,367
Oil, Gas and Mining	110,219,297
Regulatory Affairs and Public Advocacy	11,300,000
Total	<u>144,798,942</u>

PROTECTING ALASKANS



Protecting Alaskans Cases Received

Calendar Year 2011

Felonies	7,591
Misdemeanors	22,271
Child In Need of Aid	1,061
Other Cases	6,169



Protecting Alaskans

- Support Governor's Sexual Assault Domestic Violence Initiative
 - Increase victim services
 - Increase school attendance
- Screen and prosecute SA/DV cases
- Cold cases
- Promote legal representation of SA/DV victims



"Choose Respect" March, Deering Alaska

Protecting Alaskans Commercial and Fair Business

Consumer Protection Unit Suits/Settlements

- Resolved consumer complaints
- Pharmaceuticals
- Enforcement actions



Protecting Alaskans

State v. *BP Exploration Alaska (BPXA)*

- 2006 Prudhoe Bay pipeline shutdown due to corrosion
- Upcoming arbitration of royalty damage claim



Sludge buildup prevented corrosion detection equipment from working

FOSTERING RESPONSIBLE DEVELOPMENT



Fostering Responsible Development

Point Thomson (State v. Exxon et al)

- Lessees declined to produce unit reservoirs for more than two decades
- In 2005, State moved to terminate the Point Thomson unit and cancel the oil and gas leases
- Working on a settlement - Oral argument February 8 before the Alaska Supreme Court



Fostering Responsible Development Outer Continental Shelf Federal Litigation

- *Shell Exploration Plan for Summer 2012 Drilling in Beaufort Sea*
 - Federal agency BOEM approved plan
 - Native and environmental groups appealed
- *Shell and ConocoPhillips Exploration Plans for Chukchi Sea (Lease Sale 193)*
 - *Point Hope v. Salazar (2008)* challenged Lease Sale 193
 - State intervened
 - Court affirmed lease sale
 - More litigation however exploration plans can go forward



1/31/2012

Fostering Responsible Development Outer Continental Shelf State Litigation

- *Beaufort Sea Area Wide Lease Sale*
 - Resisting Environmental Destruction on Indigenous Lands (REDOIL) sued DNR over approval of Lease Sale
 - State petitioned Alaska Supreme Court to review
 - Petition granted



Fostering Responsible Development

Large Mine Permitting

Nunamta Aulukestai v. State

- DNR issued exploration permits to Pebble Limited Partnership
- Nunamta sued to challenge permits
- Court affirmed state's right to establish a permitting process
- Nunamta appealed



Fostering Responsible Development Bristol Bay Area Plan Litigation

State v. Nondalton Tribal Council

- Tribal councils sued state over how the area plan for Bristol Bay was adopted
- Alaska Supreme Court upheld DNR's process



Fostering Responsible Development

Clean Water Act Jurisdictional Guidance

- 43% of Alaska is wetlands
- EPA and Corps of Engineers want to expand amount of wetlands under jurisdiction of the Clean Water Act in Alaska
- Federal interpretation will increase federal oversight
- Alaska challenging the process and criteria



Fostering Responsible Development Tongass Timber

- Tongass National Forest was originally exempted from Roadless Rule
- U.S. District Court ruled in May 2011 that Tongass *not* exempt from Roadless Rule
- Alaska appealing decision to the 9th Circuit Court of Appeals
- Alaska filed a separate action in federal court that the Roadless Rule is invalid
- Alaska intervened in court case challenging Logjam timber sale
 - Sale upheld
 - Saved jobs for Southeast residents



Fostering Responsible Development

Navigable Waters/National Park Service

Water Regulations

- Alaska and John Sturgeon challenging the Park Service's legal interpretation
- National Park Service claims it can enforce federal regulations on navigable waters within Alaska
- Alaska claims Alaska National Interest Lands Conservation Act (ANILCA) prohibits the NPS from regulating where rivers are state-owned navigable waterways



Fostering Responsible Development Endangered Species Act

- State challenges unwarranted listings of species as “endangered” or “threatened” and critical habitat designations
 - Where populations are healthy
 - When based on speculative models



PROTECTING FISCAL INTEGRITY

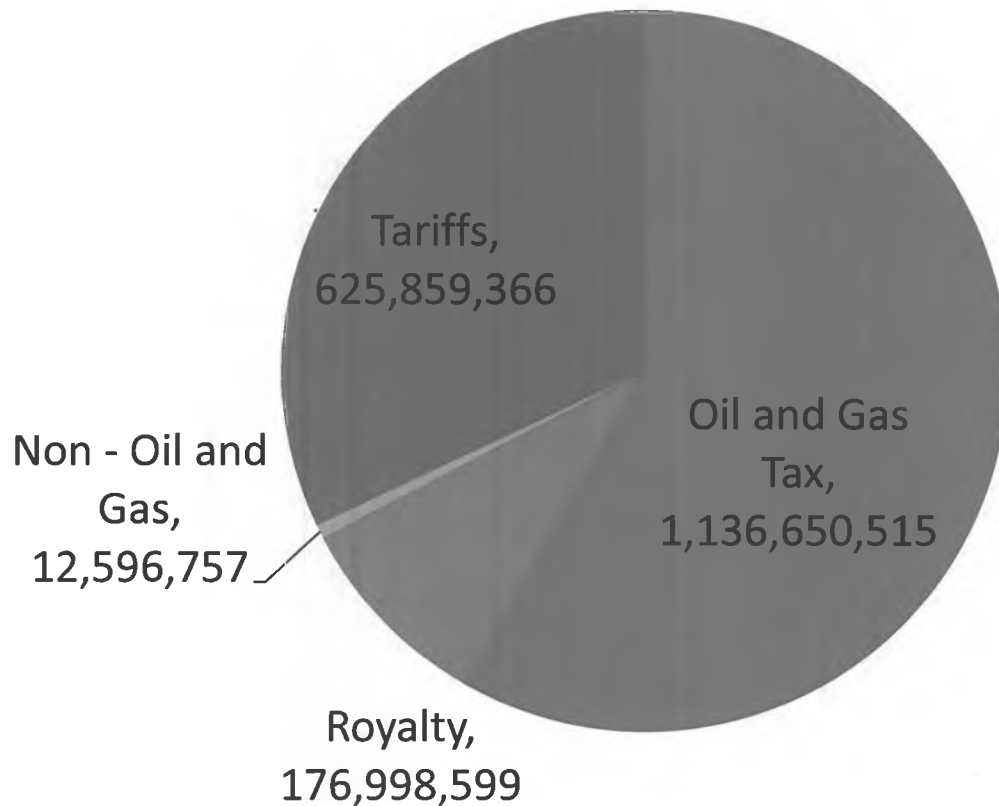


Protecting Fiscal Integrity

- *State v. Carlson*
 - Class action lawsuit against the Alaska Commercial Fisheries Entry Commission
 - Nonresident commercial fishermen got a money judgment plus interest
 - Alaska Supreme Court cut about \$50 million from the judgment
- Court overturned an earlier interest rate calculation



**Oil, Gas and Mining
Decisions and Settlements
FY00-FY10 (\$1.95 billion)**



Protecting Fiscal Integrity

TAPS Property Tax litigation

- 2006 Trans Alaska Pipeline property tax assessment on appeal to Alaska supreme court
- 2007-2009 superior court decision just issued - producer appeal expected
- Both decisions increase property tax revenues for state



Protecting Fiscal Integrity

TransAlaska Pipeline Tariff Litigation

- State challenges inclusion in TAPS tariffs of hundreds of millions of dollars in imprudently incurred capital project expenditures
- Joint hearing before the Federal Energy Regulatory Commission and State Regulatory Commission of Alaska is ongoing



PROMOTING GOOD GOVERNANCE



Promoting Good Governance

Education Constitutional Challenges

- Longstanding education funding cases settled
 - *Moore v. State*
 - Plaintiffs challenged the constitutional adequacy of rural school funding
 - *Kasayulie v. State*
 - Plaintiffs challenged state's method of financing school construction and valuation of public school trust land



The Department of Law
looks forward to working
with each of you.



DEPARTMENT OF LAW OIL, GAS AND MINING SECTION
MAJOR LITIGATION

01/24/2012

<u>Case</u>	<u>Approx. Start Date</u>	<u>Issue(s) and Status</u>	<u>Costs *</u>	<u>Value</u>
TAPS Interstate and Intrastate Tariffs Strategic Reconfiguration (SR)	December 2004	<p>Issue: Were \$100's of millions spent on pipeline capital project prudent expenditures? Project is currently about \$500 million over budget at project approval. There are other issues related to these tariffs (Phase II) that will be heard after the prudence phase (Phase I).</p> <p>Status: State, shippers, and carriers concluded seven weeks of concurrent hearings before the FERC and RCA on Phase I of the case in January 2012. The parties will file post-hearing briefs with the Commissions and, after the FERC ALJ issues a recommended decision, the parties will file responses to that proposed decision. We anticipate that the FERC will schedule Phase II of the case to start in early July.</p>	<p>DOL Expenditures as of 11/30: \$11,924,616</p> <p>Anticipated Future Costs: \$2.9 million through hearings before the Federal Energy Regulatory Commission and the Regulatory Commission of Alaska.</p>	\$15-20 million in refunds, \$100's of millions impact on future royalty and production tax
TAPS 2009-Forward Interstate and Intrastate Tariffs and Feeder Pipelines	December 2008	<p>Issue: Are newly filed TAPS interstate rates just and reasonable?</p> <p>Status: The FERC ALJ issued an order on cost pooling in November 2010. The parties filed exceptions to various points and are awaiting a final decision and order from the FERC.</p>	<p>DOL Expenditures as of 11/30: \$752,868</p> <p>Anticipated Future Costs: \$1 million for Commission remand on pooling issue to ALJ and for litigation of going forward rate issues.</p>	State settled primary issues resulting in about \$9 million in additional taxes and royalties.
Tesoro Corporate Income Tax Case (1994-1998)	2004	<p>Issue: Whether a company should have filed its tax returns on a unitary, combined basis and is subject to penalties.</p> <p>Status: Superior court ruled in favor of the state Tesoro appealed to the Alaska Supreme Court and filed its brief in late November.</p>	<p>DOL Expenditures as of 11/30: \$2,311,750</p> <p>Anticipated Future Costs: \$30,000 through a final decision at the Alaska Supreme Court.</p>	Approx. \$13 million.

* Costs are from inception of case. Anticipated Future Costs will change as a result of scheduling and substantive decisions from the tribunal, decisions by client agencies, and positions taken by opposing parties. Some of the cases, such as tariff disputes, property tax litigation, and royalty reopeners recur every year and the new cases may be consolidated with existing cases. These estimates do not reflect costs for the new cases.

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DEPARTMENT OF LAW OIL, GAS AND MINING SECTION
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Corporate Income Tax Case	Confidential	Status: Confidential	DOL Expenditures as of 11/30: \$113,679 Anticipated Future Costs: \$484,000	Confidential
TAPS Property Tax Case (Nonconfidential)	June 2006 June 2007 June 2008 June 2009 June 2010 June 2011	Issue: Whether DOR properly assessed property tax value of TAPS in 2006, 2007, 2008, 2009, 2010 and 2011. 2007-2009 cases consolidated for trial. Status: Nine week trial ended in November 2011 on consolidated 2007-2009 assessments. Judge Gleason entered a decision on December 29, 2011. 2010 and 2011 appeals awaiting scheduling for trial. The 2006 TAPS valuation has been appealed to Alaska Supreme Court. Judge Gleason's 2007-2009 decision raised the assessed values for all three years, and is consistent with her decision in the 2006 case.	DOL Expenditures as of 11/30: \$2,393,074 Anticipated Future Costs: \$1.6 million through trial on the 2007-2009 assessments and Alaska Supreme Court appeal of Judge Gleason's 2006 decision.	Decisions on appeal result in property tax revenue of \$92 million for 2007, \$124 million for 2008, \$154 million for 2009, \$194 million for 2010 and \$173 million for 2011. State directly receives approximately 48% of this property tax revenue with remainder apportioned among North Slope and Fairbanks Boroughs and City of Valdez. Superior court 2006 decision resulted in approx. \$112 million in additional property tax revenues. The superior court's 2007-2009 decision substantially raised the assessed value of TAPS, which will result in higher property taxes, but also higher TAPS tariffs because property taxes are an allowable pipeline expense in ratemaking methodology. The higher property taxes will be shared by the municipalities and the state, and the state's share will be offset to some degree by the higher tariff's effect on production tax and royalty revenues.

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Point Thomson Unit	The DNR unit default decision in 2005.	<p>Issue: Whether DNR's decision to terminate the Point Thomson Unit (PTU) due to the producers' refusal to commit to development of the unit should be upheld.</p> <p>Status: The Alaska Supreme Court accepted Law's petition for review of Judge Gleason's decision reversing DNR's unit termination decision. Oral argument before the Alaska Supreme Court is scheduled for February 8, 2012. Related proceedings before AOGCC, the OAH, and the Supreme and Superior Courts are also stayed pending final decision in the unit termination appeal. Estimated resolution is 2015 if the state wins petition and 2018 if the case goes to trial de novo. DNR Commissioner is in settlement negotiations.</p>	<p>DOL Expenditures as of 11/30: \$2,836,494</p> <p>Anticipated Future Costs: It could be as low as \$3.5 million for 1 lease terminations, appeals, and related proceedings if there is a remand to DNR, and as high as \$10 million if there is a trial de novo.</p>	Hundreds of millions in additional tax and royalty if the PTU is developed.
Royalty Audit Anadarko	2008	<p>Issue: Audit of 2004 – 2007 audit returns focusing on destination value.</p> <p>Status: Anadarko filed an administrative appeal in November 2011.</p>	<p>DOL Expenditures as of 11/30: \$15,000.</p> <p>Anticipated Future Costs: \$150,000.</p>	\$9 million
Royalty Settlement Agreement Reopener – BP	Late 2008	<p>Issue: The State is preparing to assess a claim under the Royalty Settlement reopener provisions regarding capital construction funds and other tax benefits that reduce BP's transportation costs.</p> <p>Status: Preparing arbitration claim. Anticipate resolution in 2013.</p>	<p>DOL Expenditures as of 11/30: \$413,401</p> <p>Anticipated Future Costs: \$1,000,000 through arbitration.</p>	\$15-20 million

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<u>Case</u>	<u>Approx. Start Date</u>	<u>Issue(s) and Status</u>	<u>Costs *</u>	<u>Value</u>
Royalty BP Audit 2007 - 2010	Late 2010	<p>Issue: Value and transportation costs in the 2007 – 2010 period. Approximate audit claim of \$6 million which includes approximately \$4 million related to the aforementioned Royalty Settlement Agreement Reopener – CCF issue.</p> <p>Status: DNR audit is in progress. Anticipate resolution in 2013 for leases not subject to royalty settlement.</p>	<p>DOL expenditures as of 06/30: in-house DOL staff only.</p> <p>Anticipated Future Costs: \$50,000</p>	\$6 million
Net Profit Share Audit BP in the MPU	2011	<p>Issue: BP NPSL development and operating costs and revenue at the Milne Point Unit 2006-2007.</p> <p>Status: Audit is in progress.</p>	<p>DOL Expenditures as of 11/30: in-house DOL staff only</p> <p>Anticipated Future Costs: \$300,000</p>	\$10 million
CP North Slope Oil Royalty Audit	2008	<p>Issue: 2004 – 2005 audit of CP new form leases on the North Slope, including CRU.</p> <p>Status: Audit issued 7/28/11; ConocoPhillips filed an administrative appeal in January 2012</p>	<p>DOL Expenditures as of 11/30: in-house DOL staff only.</p> <p>Anticipated Future Costs: \$400,000</p>	\$7 million
Net Profit Share Audit CP in the Colville River Unit	Mid-2009	<p>Issue: NPSL audit regarding development costs back to 1991.</p> <p>Status: Audit in progress.</p>	<p>DOL Expenditures as of 11/30: in-house DOL staff only.</p> <p>Anticipated Future Costs: \$50,000</p>	Not determined.
CP Royalty Audit Beluga River Unit	Late 2010	<p>Issue: Cook Inlet audit BRU.</p> <p>Status: Audit Issued June 2011 Working on confidentiality agreement for information sharing and case preparation.</p>	<p>DOL Expenditures as of 11/30: in-house DOL staff only.</p> <p>Anticipated Future Costs: \$100,000</p>	\$5 million

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DEPARTMENT OF LAW OIL, GAS AND MINING SECTION
MAJOR LITIGATION

01/24/2012

<u>Case</u>	<u>Approx. Start Date</u>	<u>Issue(s) and Status</u>	<u>Costs *</u>	<u>Value</u>
Marathon Cook Inlet Gas Audit of Ninilchik Unit	2008	Issue: Royalty value audit. Status: Paid under protest January 31, 2011 Administrative appeal filed with DNR July 2011	DOL Expenditure as of 11/30: in-house DOL staff only. Anticipated Future Costs: \$150,000	\$4.6 million
Northstar Production Allocation Dispute - BP	Late 2009	Issue: Dispute between the state and Murphy Exploration (Alaska) Inc. regarding allocation of production from the Northstar participating area between state and federal leases. Status: Preparing for hearing.	DOL Expenditure as of 11/30: \$599,488 Anticipated additional expenditure: \$500,000	\$160 million plus
Net Profit Share Audit BP in Endicott	2011	Issue: BP NPSL development and operating costs and revenue at the Endicott 2006-2007. Status: Audit is in progress. Anticipated to be issued 3/31/2012 at approximately \$2 million.		
CP North Slope Oil Royalty Audit	2010	Issue: 2006 audit of CP new form leases on the North Slope, including CRU. Status: Audit to be issued by 2/29/2012.		
Gas Pipeline	January 1, 2007	Issue: Implementation of AGIA Gas Pipeline, analysis of related state and federal legal issues including AGIA licensee reimbursements, represent state's interests before the FERC and federal agencies for gasline EIS and certification, analysis of state fiscal issues. Canadian legal issues related to gas pipeline through Canada.	DOL Expenditures as of 11/30: \$1,468,543 Approx. \$7.096 million Total to date	

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<u>Case</u>	<u>Approx. Start Date</u>	<u>Issue(s) and Status</u>	<u>Costs *</u>	<u>Value</u>
		<p>Status: DOL continues to require assistance of outside counsel with FERC and gas pipeline expertise for AGIA implementation related to Precedent Agreement process and timely FERC Certification as well as Canadian regulatory questions.</p>	<p>Anticipated Future Costs: The FY09-19 Gasline Operations Summary sets out DOL's anticipated costs for the next ten years. Please let me know if you need a copy of the Summary.</p>	
Quality Bank	There have been a series of cases and decisions on this issue since 1979.	<p>Issue: The producers and the State are disputing the method of monetarily accounting for commingling of different quality petroleum streams in TAPS.</p> <p>Status: A D.C. Circuit decision remanding proceedings to FERC was issued 1/18/2011.</p>	<p>DOL Expenditures as of 11/30: \$749,713 (past 6 years)</p> <p>Anticipated Future Costs: \$5,000 or less. (This case has been in litigation since 1979.)</p>	This case affects taxes and royalties to the State. However, the value to the State goes beyond absolute dollar amounts because insuring fair accounting for the value of the petroleum stream tendered to TAPS encourages continued investment in Alaska.

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