

01/24/2018

Overview:

Alaska's Oil and  
Gas Royalty  
Unitization  
Process

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Alaska's Oil and Gas Royalty Unitization  
Process</SUBJECT><COMM>SRES30</COMM></TARGET>

# Alaska Oil and Gas Fundamentals

*Senate Resources Committee*

*Presented by:*

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Alaska Department of Natural Resources

*January 24, 2018*



# Types of Oil and Gas Contracts

- There are 3 basic types of oil and gas contracts in the world:
  - Service Contracts
    - Where the resource owner hires a company to develop the resource
    - Uncommon, found in places like Iraq
  - Production Sharing Agreements
    - Where the resource owner develops the resource along side a partner
    - Common in resource owning regions
  - Concession Agreements
    - Where the resource owner allows another party to develop the resource on their behalf
    - Common in private owner regions
- Each type of contract has different distributions of risk, reward, responsibility, and ownership

# Types of Oil and Gas Contracts

- Alaska's system was largely imported from federal law, which was used to lease lands before Statehood
  - Mineral Leasing Act of 1920
  - Alaska Constitution Article 8, Section 12
  - Alaska Land Act
- U.S. jurisdictions generally confer oil and gas rights by lease

# Oil and Gas Leasing in Alaska

- A **lease** is a contract between the State and the leaseholder
  - Both parties agree to the terms of the lease and to fulfill the obligations therein
- A lease cannot be altered unilaterally
  - The parties may mutually agree to alter drilling, producing, and royalty requirements through a unit agreement
    - AS 38.05.180(p)
  - DNR has authority to reduce royalty rates through the royalty modification process
    - AS 38.05.180(j)
  - Otherwise, material changes to the lease require legislative approval.

# Oil and Gas Leasing in Alaska

- The lease gives the exclusive right to the resources for a set amount of time (*primary term*)
  - Our leases reserve a portion of those produced resources for the State, at a rate defined in the lease, called a *royalty*
  - The leaseholder also agrees to pay *rent* while they hold the lease, which is deductible from royalty payments
  - At the time of the lease issuance, the lessee makes an upfront payment, called a *bonus*, in order to secure the lease
  - After a lease is issued, the ownership of a lease may be transferred to a new lessee through an application process that includes approval of the transfer by the Director of the Division
  - A lessee may extend a lease past its primary term by actively drilling, producing, unitizing, or seeking a lease extension in limited circumstances.

# Oil and Gas Leasing in Alaska

- Oil and gas leasing of State land is now only conducted by competitive auction, often called a *lease sale*
  - Federal lands within the state are leased by the BLM
  - Federal waters are leased by BOEM
- A state lease sale is carried out by DNR
  - Prior to a lease sale, the *Leasing Section* of the Division of Oil and Gas issues a sale notice, which describes the terms of the leases being offered
    - The *Resource Evaluation* and *Commercial* sections assist in defining those lease terms
- State land may also be *licensed* under the Exploration License Program (AS 38.05.131-.134)
  - Licenses may be converted to leases if work commitments met

# Oil and Gas Leasing in Alaska

- A lease sale can be conducted as an “areawide” or a “special” lease sale
  - An areawide lease sale occurs annually, in the fall
  - A special lease sale is conducted in special circumstances, covering only specific lands
- The Commissioner decides which type of **bid variable** is used to determine the high bidder after analysis by Division staff
  - The bonus bid is typically used as the bid variable for recent Areawide lease sales
  - Other bid variables have been explored in the past
    - Some of those leases still exist today

# Oil and Gas Leasing History in Alaska

- North Slope leases issued prior to 1980 all reserved a 1/8 royalty (12.5%) for the State
  - Around 300 leases issued prior to 1980 are still active today, on these lease forms often called *DL-1 leases*
- During the 1980's, the department offered alternative lease terms
  - One such term is a Net Profit Share Lease (NPSL) which reserves a portion of producer profits for the State, in addition to the royalty
    - 24 NPSLs are still active today
  - Another experimental lease term was a “sliding scale” lease, in which the amount of royalty depended on certain price or production levels
    - 11 sliding scale leases are still active today
- Today, all new North Slope leases are issued on a 1/6 fixed royalty
  - Unless the lease is below the royalty line, then 1/8<sup>th</sup>



# Exploration and Development

- A lease is not needed for a seismic permit to explore resources on state land
- A lessee (also called a Working Interest Owner) must obtain a ***Plan of Operations*** to conduct operations to explore and develop the lease (11 AAC 83.158 and 11 AAC 83.346)
  - WIO must demonstrate compliance with the mitigation measures attached to each lease to minimize the adverse impacts of exploration and development
- The *Permitting* Section adjudicates seismic permits and Plans of Operations

# Oil and Gas Unitization

- WIOs often combine their leases into a single **Unit** for joint development
- Unitization provides economic efficiencies, avoids waste of oil and gas resources, and minimizes impact to the environment
- The state approves a **Unit Agreement** between WIOs that provides for joint development as if the area was all one lease
  - The entity in charge of the Unit operations, typically one of the WIOs, is called the Unit **Operator**
- The WIOs enter a separate agreement, called a **Unit Operating Agreement**, with each other to define the rights and responsibilities of each participant
- Unitization extends leases past their primary term
- The *Units* section adjudicates the formation and administration of units, drawing on expertise from other sections, including the *Resource Evaluation* and *Commercial* sections

# Oil and Gas Units

- DNR regulates and manages Units under a combination of statute, regulation, and lease and unit agreement terms.
- Units have a five year initial term
  - The Unit automatically extends if there is a unit well certified as being capable of producing in paying quantities and the Operator is either producing or conducting operations under an approved Plan to achieve production.
  - If production ceases, the Operator must be diligently conducting operations to return production or the unit automatically terminates.
  - The Operator may seek a discretionary extension if it has been conducting exploration operations under an approved Plan of Exploration.
- Units expand or contract based on the resources and Operator's plans
  - Ten years after unit formation, DNR has discretion to contract the unit.
  - Ten years after sustained production starts, the unit contracts to the acreage contained in Participating Areas.

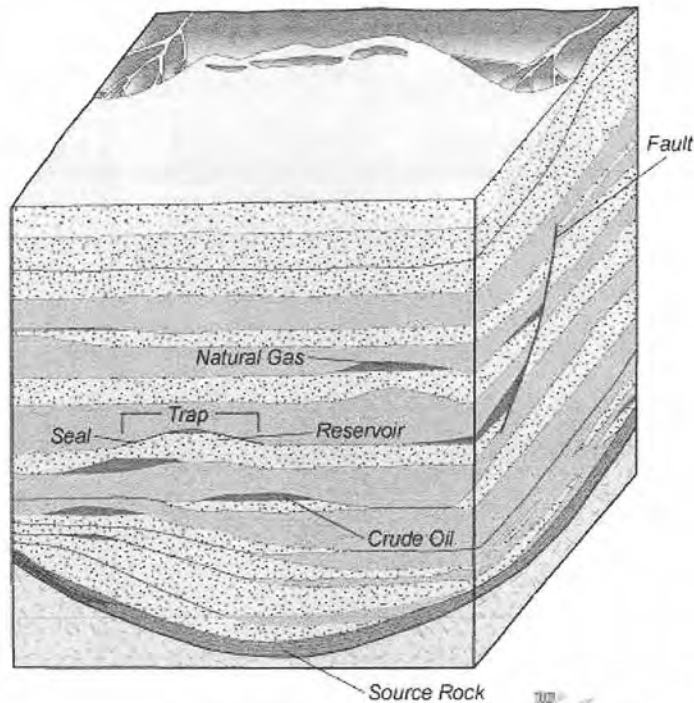
# Unit Plans

- At unit formation and in subsequent years, the Operator submits a Unit ***Plan of Exploration (POE)*** or ***Plan of Development (POD)***.
  - A POE is appropriate when an operator is conducting initial exploration. DNR determines the term of a POE.
  - Once any part of the unit is ready for development, the Operator then submits PODs. PODs must be submitted annually.
  - Both types of Plans specify short and long term plans for the Unit.
  - Failure to perform the work commitments set forth in a POE or POD is a default of the unit agreement. The Commissioner may issue a notice of default that sets forth how the Operator may “cure” the default. Failure to cure can lead to unit termination.
- POEs and PODs set forth the type of work commitments the Operator is making for the coming POE or POD period. Before the Operator may conduct the operations to carry out that work, the Operator also needs a Plan of Operations.

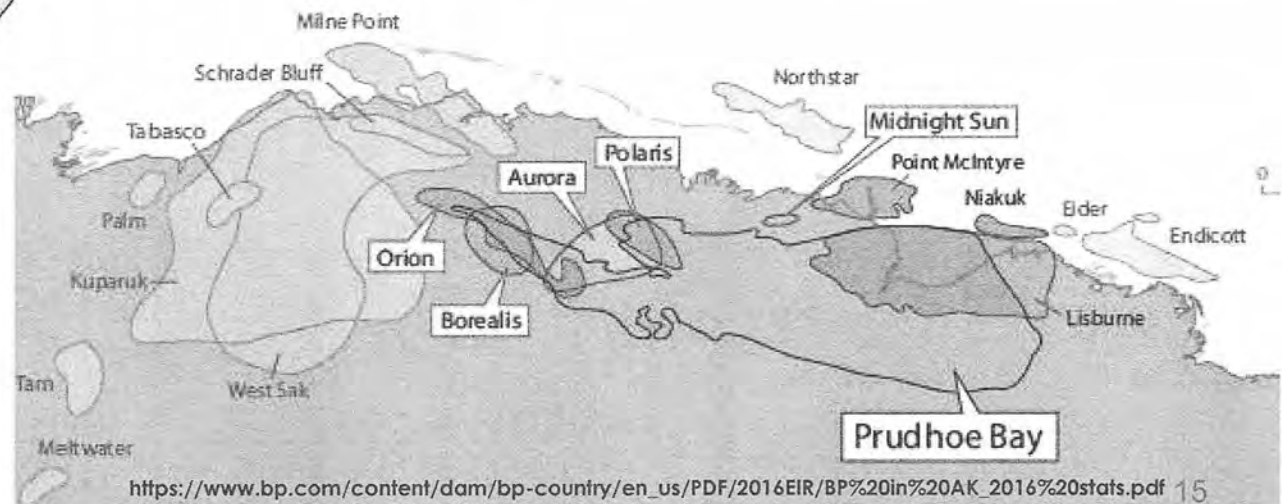
# Participating Areas

- When an Operator is ready to produce, it applies for a **Participating Area (PA)** within a Unit (11 AAC 83.351)
  - The purpose of a PA is to keep track of the production from each tract for purposes of calculating royalty for that tract in accordance with that tract's lease terms.
  - When approving a PA, DNR defines the percentage of the production that will be allocated to each tract, called a **Tract Factor**
    - As new information is collected during production, Tract Factors are occasionally updated by a process called a **Redetermination**
  - A Unit may include multiple PAs, one for each delineated reservoir.
    - DNR may also approve a PA that includes more than one reservoir
  - PAs are different from AOGCC-determined "pools." The extent of a PA is based on both the technical aspects of the reservoir and the Operator's plans for developing it. The AOGCC determines pools based solely on the technical aspects.

# Participating Areas



- Generally, an area encompassing the portion of a hydrocarbon reservoir that is capable of contributing to production
- A unit may include multiple PAs.
- A single tract within a unit may be divided into multiple PAs



# Accounting and Audit

- Producers are required to provide monthly royalty payments and report how they calculated those amounts
  - These payment amounts and production volumes are publicly available at the DNR website
- DOG has its own accountants that track payments of royalties
  - This is the *Accounting* section
- DOG also has 6 years to conduct an audit of any reports, to ensure compliance and accuracy
  - This is the *Audit* section

# Net Profit Share Leases

- A NPSL is just like a regular lease, except it also requires a percentage of net profits to be paid
  - Example: 12.5% royalty plus 30% of net revenues after capital costs and operating are recovered
- Pre-production costs go into a “development account”
- Once production starts, net revenues pay down the development account balance
  - Net revenues are gross revenues minus costs
    - Costs include operating costs, maintenance capital, well drilling, taxes, etc.
- Complicated accounting and auditing requires significantly more attention than simple fixed royalty lease provisions
- NPSL payments are not considered royalty payments (they are considered rental payments)

# Royalty Modifications

- One of the limited circumstances where the parties can modify lease terms is royalty modification
  - Royalty modification is limited to certain circumstances
    - AS 38.05.180(j)
    - To extend the life of a project
    - To push a marginal project into development
    - To restart production from an abandoned project
- Operators may apply for a royalty reduction
  - Must provide evidence that it is necessary
- DOG *Commercial* section evaluates the application, proposes modifications, and writes a best interest finding

# RIK vs RIV

- The lease reserves a percentage of production for the State
  - We have the option to receive the monetary value of that production if we choose (*royalty-in-value or RIV*)
  - If we choose to accept the royalty barrels as physical oil (*royalty-in-kind or RIK*), we must sell those barrels ourselves
- As a general rule, we try to select whichever generates more revenue for the State
- Historically, about 95% of North Slope royalty oil is sold as RIK to in-state refineries
  - DOG *Commercial* is responsible for negotiating RIK contracts
  - We typically can make more money because RIV barrels include a higher transportation to California than the marine differential allowance in the RIK contracts

# Regions

- Revenue to State from the same barrel of oil produced in different regions\*

	UGF	Restricted	Total
State Land**	\$4.84	\$3.16	\$8.00
NPRA	\$1.75	\$3.13	\$4.88
ANWR	\$3.30	\$1.58	\$4.88
Other Federal Land	\$4.53	\$2.85	\$7.38
3-6 Miles Offshore	\$0.84	\$0.85	\$1.69
>6 Miles Offshore	\$0.00	\$0.00	\$0.00
Native Corp Land	\$2.06	\$0.00	\$2.06

\*Assumes \$50 wellhead value at all locations, 12.5% royalty rate, paying the 4% gross minimum tax, and a lease newer than 1979. Numbers are greatly simplified and approximated to show scale, not to be used for any other purpose.

\*\*Includes submerged lands up to 3 miles offshore

# THANK YOU!



550 W. 7<sup>TH</sup> AVE, STE. 1100, ANCHORAGE, AK 99501  
[www.dog.dnr.alaska.gov](http://www.dog.dnr.alaska.gov)

STATE OF ALASKA  
DEPARTMENT OF NATURAL RESOURCES  
DIVISION OF OIL AND GAS

**BID FORM FOR AREAWIDE OIL & GAS LEASE SALE**

Instructions on how to complete this form are available in the Sale Announcement and Instructions to Bidders at <http://dog.dnr.alaska.gov/Services/LeaseSale>.

Areawide Oil & Gas Lease Sale Name \_\_\_\_\_ Lease Sale Tract (LST) \_\_\_\_\_ Parcel (North Slope Only) \_\_\_\_\_

Each bidder listed below must be qualified in order to bid. All lease-interest percentages must be expressed in percentages with the fractional interest carried out to no more than five decimal places. The sum of the lease-interests covered by this bid must equal 100.00000 percent without rounding.

Bidder	% Lease Interest	Qualification File No.	Bidder Name	Individual Bidder or Bidder Agent Authorized Signature	Date
No. 1	_____	_____	Agent Name and Title (type or print): _____	_____	_____
No. 2	_____	_____	Agent Name and Title (type or print): _____	_____	_____
No. 3	_____	_____	Agent Name and Title (type or print): _____	_____	_____
No. 4	_____	_____	Agent Name and Title (type or print): _____	_____	_____

Estimated Acreages for lease sale tracts are listed in Attachment A of the Sale Announcement and Instructions to Bidders. The Total Bid Per Acre controls in case of a discrepancy.

Total Bid Per Acre      Estimated Acreage      Total Estimated Bonus Bid  
 \$ \_\_\_\_\_ /Acre X \_\_\_\_\_ Acre = \$ \_\_\_\_\_

Enclosed is \$ \_\_\_\_\_, a bid deposit equal to or greater than the Minimum Bid Deposit, which is **20%** of the Total Estimated Bonus Bid, as required by the Sale Announcement and Instructions to Bidders.

I/We certify by signing this form that 1) this bid discloses the percentage interest of each person or entity who has any working interest in this bid or in any lease issued in response to it and 2) if awarded a lease pursuant to this bid, all successful bidders who have a working interest in the lease at the time of the lease award notice will execute all copies of the lease form specified in the Sale Announcement and Instructions to Bidders and comply with all other requirements of the award notice, including the posting of any required bond, or shall forfeit the entire amount deposited with this bid.

AS 38.05.035(a) authorizes the director to decide what information is needed to process an application for the sale or use of state land and resources. This information is made a part of the state public land records and becomes public information under AS 40.25.110 and AS 40.25.120 (unless the information qualifies for confidentiality under AS 38.05.035(a)(9) and confidentiality is requested). Public information is open to inspection by you or any member of the public. A person who is the subject of the information may challenge its accuracy or completeness under AS 44.99.310, by giving a written description of the challenged information, the changes needed to correct it, and a name and address where the person can be reached. False statements made in an application for a benefit are punishable under AS 11.56.210.

STATE OF ALASKA  
DEPARTMENT OF NATURAL RESOURCES  
DIVISION OF OIL AND GAS

**BID FORM FOR AREAWIDE OIL & GAS LEASE SALE**

The person designated to act as the agent on behalf of all bidders in connection with this bid is:

**Bid Agent**

Agent Name \_\_\_\_\_ Title \_\_\_\_\_

Telephone Number(s) \_\_\_\_\_

Email Address \_\_\_\_\_

Instructions for return of bid deposit, if unsuccessful. \_\_\_\_\_

If this bid is determined to be the apparent high bid, and if a lease is awarded, future lease notices and correspondence are to be mailed to the notification lessee as designated by name and address specified below.

**Notification Lessee**

Bidder Name \_\_\_\_\_

Mailing Address \_\_\_\_\_

City \_\_\_\_\_ State \_\_\_\_\_ ZIP Code \_\_\_\_\_

If this bid is determined to be the apparent high bid, and if a lease is awarded, future award notices and issued leases may be delivered by private delivery or courier to the name and physical address specified below. The address must be a location acceptable to private delivery or courier services.

**Delivery Address**

Bidder Name \_\_\_\_\_ ATTN \_\_\_\_\_

Physical Address\* \_\_\_\_\_

City \_\_\_\_\_ State \_\_\_\_\_ ZIP Code \_\_\_\_\_

Phone \_\_\_\_\_

STATE OF ALASKA  
DEPARTMENT OF NATURAL RESOURCES

Competitive Oil and Gas Lease      ADL No.

THIS LEASE is entered into \_\_\_\_\_, between the State of Alaska, "the state," and

"the lessee," whether one or more, whose sole address for purposes of notification is under Paragraph 25.

In consideration of the cash payment made by the lessee to the state, which payment includes the first year's rental and any required cash bonus, and subject to the provisions of this lease, including applicable stipulation(s) and mitigating measures attached to this lease and by this reference incorporated in this lease, the state and the lessee agree as follows:

1. GRANT. (a) Subject to the provisions in this lease, the state grants and leases to the lessee, without warranty, the exclusive right to drill for, extract, remove, clean, process, and dispose of oil, gas, and associated substances in or under the following described tract of land:

containing approximately \_\_\_\_\_ acres, more or less (referred to in this lease as the "leased area"); the nonexclusive right to conduct within the leased area geological and geophysical exploration for oil, gas, and associated substances; and the nonexclusive right to install pipelines and build structures on the leased area to find, produce, save, store, treat, process, transport, take care of, and market all oil, gas, and associated substances and to house and board employees in its operations on the leased area. The rights granted by this lease are to be exercised in a manner which will not unreasonably interfere with the rights of any permittee, lessee or grantee of the state consistent with the principle of reasonable concurrent uses as set out in Article VIII, Section 8 of the Alaska Constitution.

(b) For the purposes of this lease, the leased area contains the legal subdivisions as shown on the attached plat marked Exhibit A.

(c) If the leased area is described by protracted legal subdivisions and, after the effective date of this lease, the leased area is surveyed under the public land rectangular system, the boundaries of the leased area are those established by that survey, when approved, subject, however, to the provisions of applicable regulations relating to those surveys. If for any reason the leased area includes more acreage than the maximum permitted under applicable law (including the "rule of approximation" authorized in AS 38.05.145 and defined in AS 38.05.965 (18)), this lease is not void and the acreage included in the leased area must be reduced to the permitted maximum. If the state determines that the leased area exceeds the permitted acreage and notifies the lessee in writing of the amount of acreage that must be eliminated, the lessee has 60 days after that notice to surrender one or more legal subdivisions included in the leased area comprising at least the amount of acreage that must be eliminated. Any subdivision surrendered must be located on the perimeter of the leased area as originally described. If a surrender is not filed within 60 days, the state may terminate this lease as to the acreage that must be eliminated by mailing notice of the termination to the lessee describing the subdivision eliminated.

(d) If the State of Alaska's ownership interest in the oil, gas, and associated substances in the leased area is less than an entire and undivided interest, the grant under this lease is effective only as to the state's interest in that oil, gas, and associated substances, and the royalties and rentals provided in this lease must be paid to the state in the proportion that the state's interest bears to the entire undivided fee.

(e) The state makes no representations or warranties, express or implied, as to title, or access to, or quiet enjoyment of, the leased area. The state is not liable to the lessee for any deficiency in title to the leased area, nor is the lessee or any successor in interest to the lessee entitled to any refund due to deficiency in title for any rentals, bonuses, or royalties paid under this lease.

2. RESERVED RIGHTS. (a) The state, for itself and others, reserves all rights not expressly granted to the lessee by this lease. These reserved rights include, but are not limited to:

(1) the right to explore for oil, gas, and associated substances by geological and geophysical means;

(2) the right to explore for, develop, and remove natural resources other than oil, gas, and associated substances on or from the leased area;

(3) the right to establish or grant easements and rights-of-way for any lawful purpose, including without limitation for shafts and tunnels necessary or appropriate for the working of the leased area or other lands for natural resources other than oil, gas, and associated substances;

(4) the right to dispose of land within the leased area for well sites and well bores of wells drilled from or through the leased area to explore for or produce oil, gas, and associated substances in and from lands not within the leased area; and

(5) the right otherwise to manage and dispose of the surface of the leased area or interests in that land by grant, lease, permit, or otherwise to third parties.

(b) The rights reserved may be exercised by the state, or by any other person or entity acting under authority of the state, in any manner that does not unreasonably interfere with or endanger the lessee's operations under this lease.

3. TERM. This lease is issued for an initial primary term of \_\_\_\_\_ years from the effective date of this lease. The term may be extended as provided in Paragraph 4 below.

4. EXTENSION. (a) This lease will be extended automatically if and for so long as oil or gas is produced in paying quantities from the leased area.

(b) This lease will be extended automatically if it is committed to a unit approved or prescribed by the state, and will remain in effect for so long as it remains committed to that unit.

(c) (1) If the drilling of a well whose bottom hole location is in the leased area has commenced as of the date on which the lease otherwise would expire and is continued with reasonable diligence, this lease will continue in effect until 90 days after cessation of that drilling and for so long as oil or gas is produced in paying quantities from the leased area.

(2) If oil or gas in paying quantities is produced from the leased area, and if that production ceases at any time, this lease will not terminate if drilling or reworking operations are commenced on the leased area within sixty days after cessation of production and are prosecuted with reasonable diligence; if those drilling or reworking operations result in the production of oil or gas, this lease will remain in effect for so long as oil or gas is produced in paying quantities from the leased area.

(d) If there is a well capable of producing oil or gas in paying quantities on the leased area, this lease will not expire because the lessee fails to produce that oil or gas unless the state gives notice to the lessee, allowing a reasonable time, which will not be less than sixty days after notice, to place the well into production, and the lessee fails to do so. If production is established within the time allowed, this lease is extended only for so long as oil or gas is produced in paying quantities from the leased area.

(e) If the state directs or approves in writing a suspension of all operations on or production from the leased area (except for a suspension necessitated by the lessee's negligence), or if a suspension of all operations on or production from the leased area has been ordered under federal, state, or local law, the lessee's obligation to comply with any express or implied provision of this lease requiring operations or production will be suspended, but not voided, and the lessee shall not be liable for damages for failure to comply with that provision. If the suspension occurs before the expiration of the primary term, the primary term will be extended at the end of the period of the suspension by adding the period of time lost under the primary term because of the suspension. If the suspension occurs during an extension of the primary term under this paragraph, upon removal of that suspension, the lessee will have a reasonable time, which will not be less than six months after notice that the suspension has been removed, to resume operations or production. For the purposes of this subparagraph, any suspension of operations or production specifically required or imposed as a term of sale or by any stipulation made a part of this lease will not be considered a suspension ordered by law.

(f) If the state determines that the lessee has been prevented by force majeure, after efforts made in good faith, from performing any act that would extend the lease beyond the primary term, this lease will not expire during the period of force majeure. If the force majeure occurs before the expiration of the primary term, the primary term will be extended at the end of the period of force majeure by adding the period of time lost under the primary term because of the force majeure. If the force majeure occurs during an extension of the primary term under this paragraph, this lease will not expire during the period of force majeure plus a reasonable time after that period, which will not be less than 60 days, for the lessee to resume operations or production.

(g) Nothing in subparagraphs (e) or (f) suspends the obligation to pay royalties or other production or profit-based payments to the state from operations on the leased area that are not affected by any suspension or force majeure, or suspends the obligation to pay rentals.

5. RENTALS. (a) The lessee shall pay annual rental to the state in the amount of \$10.00 per acre or fraction of an acre.

(b) The state may increase the annual rental rate as provided by law upon extension of this lease beyond the primary term.

(c) Annual rental paid in advance is a credit on the royalty or net profit share due under this lease for that year.

(d) The lessee shall pay the annual rental to the State of Alaska (or any depository designated by the state with at least 60 days notice to the lessee) in advance, on or before the annual anniversary date of this lease. The state is not required to give notice that rentals are due by billing the lessee. If the state's (or depository's) office is not open for business on the annual anniversary date of this lease, the time for payment is extended to include the next day on which that office is open for business. If the annual rental is not paid timely, this lease automatically terminates as to both parties at 11:59 p.m., Alaska Standard Time, on the date by which the rental payment was to have been made.

6. RECORDS. (a) The lessee shall keep and have in its possession books and records showing the development and production (including records of development and production expenses) and disposition (including records of sale prices, volumes, and purchasers) of all oil, gas, and associated substances produced from the leased area. The lessee shall permit the State of Alaska or its agents to examine these books and records at all reasonable times. Upon request by the state, the lessee's books and records shall be made available to the state at the state office designated by the state. These books and records of development, production, and disposition must employ methods and techniques that will ensure the most accurate figures reasonably available without requiring the lessee to provide separate tankage or meters for each well. The lessee shall use generally accepted accounting procedures consistently applied.

(b) The lessee shall maintain accurate records of lease working interest and secondary overriding royalty interest ownership and shall submit the information to the state within 15 days upon receipt of request.

7. APPORTIONMENT OF ROYALTY FROM APPROVED UNIT. 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. Under this provision, the state's royalty share of any unit production allocated to the leased area will be regarded as royalty to be distributed to, or the proceeds of it paid to, the state, free and clear of all lease or unit expenses (and any portion of those expenses incurred away from the unit area), including, but not limited to, expenses for separating, cleaning, dehydration, gathering,

saltwater disposal, and preparing oil, gas, or associated substances for transportation off the unit area, and free of any lien for them.

8. PAYMENTS. All payments to the State of Alaska under this lease must be made payable to the state in the manner directed by the state, and unless otherwise specified, must be tendered to the state at:

DEPARTMENT OF NATURAL RESOURCES  
550 WEST 7<sup>TH</sup> AVENUE, SUITE 1410  
ANCHORAGE, ALASKA 99501-3561  
ATTENTION: FINANCIAL SERVICES SECTION

or in person at either of the Department's Public Information Centers located at

550 W. 7<sup>th</sup> Ave., Suite 1260  
Anchorage, Alaska

3700 Airport Way  
Fairbanks, Alaska

or to any depository designated by the state with at least 60 days notice to the lessee.

9. PLAN OF OPERATIONS. (a) Except as provided in (b) of this section, a plan of operations for all or part of the leased area must be approved by the commissioner before any operations may be undertaken on or in the leased area.

(b) A plan of operations is not required for:

- (1) activities that would not require a land use permit; or
- (2) operations undertaken under an approved unit plan of operations.

(c) Before undertaking operations on or in the leased area, the lessee shall provide for full payment of all damages sustained by the owner of the surface estate as well as by the surface owner's lessees and permittees, by reason of entering the land.

(d) An application for approval of a plan of operations must contain sufficient information, based on data reasonably available at the time the plan is submitted for approval, for the commissioner to determine the surface use requirements and impacts directly associated with the proposed operations. An application must include statements and maps or drawings setting out the following:

- (1) the sequence and schedule of the operations to be conducted on or in the leased area, including the date operations are proposed to begin and their proposed duration;
- (2) projected use requirements directly associated with the proposed operations, including the location and design of well sites, material sites, water supplies, solid waste sites, buildings, roads, utilities, airstrips, and all other facilities and equipment necessary to conduct the proposed operations;
- (3) plans for rehabilitation of the affected leased area after completion of operations or phases of those operations; and
- (4) a description of operating procedures designed to prevent or minimize adverse effects on other natural resources and other uses of the leased area and adjacent areas, including fish and wildlife habitats, historic and archeological sites, and public use areas.

(e) In approving a lease plan of operations or an amendment of a plan, the commissioner will require amendments that the commissioner determines necessary to protect the state's interest. The commissioner will not require an amendment that would be inconsistent with the terms of sale under which the lease was obtained, or with the terms of the lease itself, or which would deprive the lessee of reasonable use of the leasehold interest.

(f) The lessee may, with the approval of the commissioner, amend an approved plan of operations.

(g) Upon completion of operations, the lessee shall inspect the area of operations and submit a report indicating the completion date of operations and stating any noncompliance of which the lessee knows, or should reasonably know, with requirements imposed as a condition of approval of the plan.

10. PLAN OF DEVELOPMENT. (a) Except as provided in subparagraph (d) below, within 12 months after completion of a well capable of producing oil, gas, or associated substances in paying quantities, the lessee shall file an application for approval by the state of an initial plan of development that must describe the lessee's plans for developing the leased area. No development of the leased area may occur until a plan of development has been approved by the state.

(b) The plan of development must be revised, updated, and submitted to the state for approval annually before or on the anniversary date of the previously approved plan.

(c) The lessee may, with the approval of the state, subsequently modify an approved plan of development.

(d) If the leased area is included in an approved unit, the lessee will not be required to submit a separate lease plan of development for unit activities.

11. INFORMATION ACQUIRED FROM OPERATIONS. (a) The lessee shall submit to the state, at the Department of Natural Resources, Division of Oil & Gas (Division), all geological, geophysical, and engineering data obtained from the lease within 30 days following completion, abandonment, or suspension of each well, pilot hole, and plugged back well bore. The lessee shall also submit to the Division, on behalf of the state, data acquired subsequent to completion, abandonment, or suspension of each well, pilot hole, and plugged back well bore within 30 days following acquisition of those data. The Division, on behalf of the state, may waive receipt of operational data from some development, service, or injection wells, and will inform the operator of the waiver in writing prior to data submittal.

Data shall be submitted according to the instructions set out in Attachment 1.

Submission of data under this paragraph does not affect any statutory or regulatory obligation to submit data or other information to the state or any of its agencies.

(b) Any data submitted to the state, at the Department of Natural Resources, Division of Oil & Gas will be available at all times for use by the state and its agents, and will be held confidential as provided in AS 38.05.035(a)(8) and its applicable regulations. In accordance with AS 38.05.035(a)(8)(C), in order for geological, geophysical, and engineering data to be held confidential, the lessee must request confidentiality at the time of submission and mark the data "CONFIDENTIAL" in compliance with applicable regulations.

12. DIRECTIONAL DRILLING. This lease may be maintained in effect by directional wells whose bottom hole location is on the leased area but that are drilled from locations on other lands not covered by this lease. In those circumstances, drilling will be considered to have commenced on the leased area when actual drilling is commenced on those other lands for the purpose of directionally drilling into the leased area. Production of oil or gas from the leased area through any directional well surfaced on those other lands, or drilling or reworking of that directional well, will be considered production or drilling or reworking operations on the leased area for all purposes of this lease. Nothing contained in this paragraph is intended or will be construed as granting to the lessee any interest, license, easement, or other right in or with respect to those lands in addition to any interest, license, easement, or other right that the lessee may have lawfully acquired from the state or from others.

13. DILIGENCE AND PREVENTION OF WASTE. (a) The lessee shall exercise reasonable diligence in drilling, producing, and operating wells on the leased area unless consent to suspend operations temporarily is granted by the state.

(b) Upon discovery of oil or gas on the leased area in quantities that would appear to a reasonable and prudent operator to be sufficient to recover ordinary costs of drilling, completing, and producing an additional well in the same geologic structure at another location with a reasonable profit to the operator, the lessee must drill those wells as a reasonable and prudent operator would drill, having due regard for the interest of the state as well as the interest of the lessee.

(c) The lessee shall perform all operations under this lease in a good and workmanlike manner in accordance with the methods and practices set out in the approved plan of operations and plan of development, with due regard for the prevention of waste of oil, gas, and associated substances and the entrance of water to the oil and gas-bearing sands or strata to the destruction or injury of those sands or strata, and to the preservation and conservation of the property for future productive operations. The lessee shall carry out at the lessee's expense all orders and requirements of the State of Alaska relative to the prevention of waste and to the preservation of the leased area. If the lessee fails to carry out these orders, the state will have the right, together with any other available legal recourse, to enter the leased area to repair damage or prevent waste at the lessee's expense.

(d) The lessee shall plug and abandon any well in a manner prescribed by the Alaska Oil and Gas Conservation Commission.

14. OFFSET WELLS. The lessee shall drill such wells as a reasonable and prudent operator would drill to protect the state from loss by reason of drainage resulting from production on other land. Without limiting the generality of the foregoing sentence, if oil or gas is produced in a well on other land not owned by the State of Alaska or on which the State of Alaska receives a lower rate of royalty than under this lease, and that well is within 500 feet in the case of an oil well or 1,500 feet in the case of a gas well of lands then subject to this lease, and that well produces oil or gas for a period of 30 consecutive days in quantities that would appear to a reasonable and prudent operator to be sufficient to recover

ordinary costs of drilling, completing, and producing an additional well in the same geological structure at an offset location with a reasonable profit to the operator, and if, after notice to the lessee and an opportunity to be heard, the state finds that production from that well is draining lands then subject to this lease, the lessee shall within 30 days after written demand by the state begin in good faith and diligently prosecute drilling operations for an offset well on the leased area. In lieu of drilling any well required by this paragraph, the lessee may, with the state's consent, compensate the state in full each month for the estimated loss of royalty through drainage in the amount determined by the state.

15. UNITIZATION. (a) The lessee may unite with others, jointly or separately, in collectively adopting and operating under a cooperative or unit agreement for the exploration, development, or operation of the pool, field, or like area or part of the pool, field, or like area that includes or underlies the leased area or any part of the leased area whenever the state determines and certifies that the cooperative or unit agreement is in the public interest.

(b) The lessee agrees, within six months after demand by the state, to subscribe to a reasonable cooperative or unit agreement that will adequately protect all parties in interest, including the state. The state reserves the right to prescribe such an agreement.

(c) With the consent of the lessee, and if the leased area is committed to a unit agreement approved by the state, the state may establish, alter, change, or revoke drilling, producing, and royalty requirements of this lease as the state determines necessary or proper to secure the proper protection of the public interest.

(d) Except as otherwise provided in this subparagraph, where only a portion of the leased area is committed to a unit agreement approved or prescribed by the state, that commitment constitutes a severance of this lease as to the unitized and nonunitized portions of the leased area. The portion of the leased area not committed to the unit will be treated as a separate and distinct lease having the same effective date and term as this lease and may be maintained only in accordance with the terms and conditions of this lease, statutes, and regulations. Any portion of the leased area not committed to the unit agreement will not be affected by the unitization or pooling of any other portion of the leased area, by operations in the unit, or by suspension approved or ordered for the unit. If any portion of this lease is included in a participating area formed under a unit agreement, the entire leased area will remain committed to the unit and this lease will not be severed.

16. INSPECTION. The lessee shall keep open at all reasonable times, for inspection by any duly authorized representative of the State of Alaska, the leased area, all wells, improvements, machinery, and fixtures on the leased area, and all reports and records relative to operations and surveys or investigations on or with regard to the leased area or under this lease. Upon request, the lessee shall furnish the State of Alaska with copies of and extracts from any such reports and records.

17. SUSPENSION. The state may from time to time direct or approve in writing suspension of production or other operations under this lease.

18. ASSIGNMENT, PARTITION, AND CONVERSION. This lease, or an interest in this lease, may, with the approval of the state, be assigned, subleased, or otherwise transferred to any person or persons qualified to hold a lease. No assignment, sublease, or other transfer of an interest in this lease, including assignments of working or royalty interests, or subleases, will be binding upon the state unless approved by the state. The lessee shall remain liable for all obligations under this lease accruing prior to the approval by the state of any assignment, sublease, or other transfer of an interest in this lease. All provisions of this lease will extend to and be binding upon the heirs, administrators, successors, and assigns of the state and the lessee. Applications for approval of an assignment, sublease, or other transfer must comply with all applicable regulations and must be filed within 90 days after the date of final execution of the instrument of transfer. The state will approve a transfer of an undivided interest in this lease unless the transfer would adversely affect the interests of Alaska or the application does not comply with applicable regulations. The state will disapprove a transfer of a divided interest in this lease if the transfer covers only a portion of the lease or a separate and distinct zone or geological horizon unless the lessee demonstrates that the proposed transfer of a divided interest is reasonably necessary to accomplish exploration or development of the lease, the lease is committed to an approved unit agreement, the lease is allocated production within an approved participating area, or the lease has a well capable of production in paying quantities. The state will make a written finding stating the reasons for disapproval of a transfer of a divided interest. Where an assignment, sublease, or other transfer is made of all or a part of the lessee's interest in a portion of the leased area, this lease may, at the option of the state or upon request of the transferee and with the approval of the state, be severed, and a separate and distinct lease will be issued to the transferee having the same effective date and terms as this lease.

19. SURRENDER. The lessee at any time may file with the state a written surrender of all rights under this lease or any portion of the leased area comprising one or more legal subdivisions or, with the consent of the state, any separate and distinct zone or geological horizon underlying the leased area or one or more legal subdivisions of the leased

area. That surrender will be effective as of the date of filing, subject to the continued obligations of the lessee and its surety to make payment of all accrued royalties and to place all wells and surface facilities on the surrendered land or in the surrendered zones or horizons in condition satisfactory to the state for suspension or abandonment. After that, the lessee will be released from all obligations under this lease with respect to the surrendered lands, zones, or horizons.

20. **DEFAULT AND TERMINATION; CANCELLATION.** (a) The failure of the lessee to perform timely its obligations under this lease, or the failure of the lessee otherwise to abide by all express and implied provisions of this lease, is a default of the lessee's obligations under this lease. Whenever the lessee fails to comply with any of the provisions of this lease (other than a provision which, by its terms, provides for automatic termination), and fails to comply within 60 days after written notice of that default, the state may terminate this lease if at the time of termination there is no well on the leased area capable of producing oil or gas in paying quantities. If there is a well on the leased area capable of producing oil or gas in paying quantities, this lease may be terminated by an appropriate judicial proceeding.

(b) The state may cancel this lease at any time if the state determines, after the lessee has been given notice and a reasonable opportunity to be heard, that:

(1) continued operations pursuant to this lease probably will cause serious harm or damage to biological resources, to property, to mineral resources, or to the environment (including the human environment);

(2) the threat of harm or damage will not disappear or decrease to an acceptable extent within a reasonable period of time; and

(3) the advantages of cancellation outweigh the advantages of continuing this lease in effect. Any cancellation under this subparagraph will not occur unless and until operations under this lease have been under suspension or temporary prohibition by the state, with due extension of the term of this lease, continuously for a period of five years or for a lesser period upon request of the lessee.

(c) Any cancellation under subparagraph (b) will entitle the lessee to receive compensation as the lessee demonstrates to the state is equal to the lesser of:

(1) the value of the cancelled rights as of the date of cancellation, with due consideration being given to both anticipated revenues from this lease and anticipated costs, including costs of compliance with all applicable regulations and stipulations, liability for clean-up costs or damages, or both, in the case of an oil spill, and all other costs reasonably anticipated under this lease; or

(2) the excess, if any, over the lessee's revenues from this lease (plus interest on the excess from the date of receipt to date of reimbursement) of all consideration paid for this lease and all direct expenditures made by the lessee after the effective date of this lease and in connection with exploration or development, or both, under this lease, plus interest on that consideration and those expenditures from the date of payment to the date of reimbursement.

21. **RIGHTS UPON TERMINATION.** (a) Upon the expiration or earlier termination of this lease as to all or any portion of the leased area, the lessee will be directed in writing by the state and will have the right at any time within a period of one year after the termination, or any extension of that period as may be granted by the state, to remove from the leased area or portion of the leased area all machinery, equipment, tools, and materials. Upon the expiration of that period or extension of that period and at the option of the state, any machinery, equipment, tools, and materials that the lessee has not removed from the leased area or portion of the leased area become the property of the state or may be removed by the state at the lessee's expense. At the option of the state, all improvements such as roads, pads, and wells must either be abandoned and the sites rehabilitated by the lessee to the satisfaction of the state, or be left intact and the lessee absolved of all further responsibility as to their maintenance, repair, and eventual abandonment and rehabilitation. Subject to the above conditions, the lessee shall deliver up the leased area or those portions of the leased area in good condition.

(b) The state may require such financial assurances as the commissioner determines necessary to ensure the lessee's ability to meet its obligations under this paragraph. If at any time the commissioner determines that existing financial assurances are insufficient to satisfactorily guarantee the performance of all the lessee's obligations under this paragraph, the commissioner may require the delivery of such substitute or supplemental financial assurances as the commissioner determines necessary.

22. **DAMAGES AND INDEMNIFICATION.** (a) No rights under the AS 38.05.125 reservation may be exercised by the lessee until the lessee has provided to pay the owner of the land, his lessees and permittees, upon which the AS 38.05.125 reserved rights are sought to be exercised, full payment for all damage sustained by the owner by reason of entering the land. If the owner for any reason does not settle the damages, the lessee may enter the land after posting a surety bond determined by the state, after notice and an opportunity to be heard, to be sufficient as to form, amount, and security to secure to the owner, his lessees and permittees, payment for damages, and may institute legal proceedings in a court of competent jurisdiction where the land is located to determine the damages which the owner of the land may suffer. The lessee agrees to pay for any damages that may become payable under AS 38.05.130 and to indemnify the

state and hold it harmless from and against any claims, demands, liabilities, and expenses arising from or in connection with such damages. The furnishing of a bond in compliance with this paragraph will be regarded by the state as sufficient provision for the payment of all damages that may become payable under AS 38.05.130 by virtue of this lease.

(b) The lessee shall indemnify the state for, and hold it harmless from, any claim, including claims for loss or damage to property or injury to any person caused by or resulting from any act or omission committed under this lease by or on behalf of the lessee. The lessee is not responsible to the state under this subparagraph for any loss, damage, or injury caused by or resulting from the sole negligence of the state.

(c) The lessee expressly waives any defense to an action for breach of a provision of this lease or for damages resulting from an oil spill or other harm to the environment that is based on an act or omission committed by an independent contractor in the lessee's employ. The lessee expressly agrees to assume responsibility for all actions of its independent contractors.

23. BONDS. (a) The lessee shall furnish a bond before lease operations commence in an amount equal to at least \$10,000, and must maintain that bond as long as required by the state.

(b) The lessee may, in lieu of the bond required under (a) above, furnish and maintain a statewide bond in accordance with applicable regulations.

(c) The state may, after notice to the lessee and a reasonable opportunity to be heard, require a bond in a reasonable amount greater than the amount specified in (a) above where a greater amount is justified by the nature of the surface and its uses and the degree of risk involved in the types of operations being or to be carried out under this lease. A statewide bond will not satisfy any requirement of a bond imposed under this subparagraph, but will be considered by the state in determining the need for and the amount of any additional bond under this subparagraph.

(d) If the leased area is committed in whole or in part to a cooperative or unit agreement approved or prescribed by the state the unit operator will furnish and maintain a statewide bond in accordance with applicable regulations.

24. AUTHORIZED REPRESENTATIVES. The Director of the Division of Oil and Gas, Department of Natural Resources, State of Alaska, and the person executing this lease on behalf of the lessee shall be authorized representatives for their respective principals for the purposes of administering this lease. The state or the lessee may change the designation of its authorized representative or the address to which notices to that representative are to be sent by a notice given in accordance with Paragraph 25 below. Where activities pursuant to a plan of operations are underway, the lessee shall also designate, pursuant to a notice under Paragraph 25 below, by name, job title, and address, an agent who will be present in the state during all lease activities.

25. NOTICES; PROTEST. (a) Any notices required or permitted under this lease must be by electronic media producing a permanent record or in writing and must be given personally or by registered or certified mail, return receipt requested, addressed as follows:

TO THE STATE:

DIRECTOR, DIVISION OF OIL AND GAS  
DEPARTMENT OF NATURAL RESOURCES  
550 WEST 7TH AVENUE, SUITE 1100  
ANCHORAGE, ALASKA 99501-3563

TO THE LESSEE:

(b) Any notice given under this paragraph will be effective when delivered to the above authorized representative

(c) A lessee who wishes to protest the amount of money due the state under the lease or any action of the state regarding a provision of this lease must file a written protest with the Division of Oil and Gas within 30 days after the mailing date of the state's notice or bill. A lessee who fails to file a protest within the required time waives any further right to protest. The state will establish the administrative appeal procedure to be followed and will inform the lessee of the procedure no later than 30 days after the filing of the written protest.

26. **STATUTES AND REGULATIONS.** This lease is subject to all applicable state and federal statutes and regulations in effect on the effective date of this lease, and insofar as is constitutionally permissible, to all statutes and regulations placed in effect after the effective date of this lease. A reference to a statute or regulation in this lease includes any change in that statute or regulation whether by amendment, repeal and replacement, or other means. This lease does not limit the power of the State of Alaska or the United States of America to enact and enforce legislation or to promulgate and enforce regulations affecting, directly or indirectly, the activities of the lessee or its agents in connection with this lease or the value of the interest held under this lease. In case of conflicting provisions, statutes and regulations take precedence over this lease.

27. **INTERPRETATION.** This lease is to be interpreted in accordance with the rules applicable to the interpretation of contracts made in the State of Alaska. The paragraph headings are not part of this lease and are inserted only for convenience. The state and the lessee expressly agree that the law of the State of Alaska will apply in any judicial proceeding affecting this lease.

28. **INTEREST IN REAL PROPERTY.** It is the intention of the parties that the rights granted to the lessee by this lease constitute an interest in real property in the leased area.

29. **WAIVER OF CONDITIONS.** The state reserves the right to waive any breach of a provision of this lease, but any such waiver extends only to the particular breach so waived and does not limit the rights of the state with respect to any future breach; nor will the waiver of a particular breach prevent cancellation of this lease for any other cause or for the same cause occurring at another time. Notwithstanding the foregoing, the state will not be deemed to have waived a provision of this lease unless it does so in writing.

30. **SEVERABILITY.** If it is finally determined in any judicial proceeding that any provision of this lease is invalid, the state and the lessee may jointly agree by a written amendment to this lease that, in consideration of the provisions in that written amendment, the invalid portion will be treated as severed from this lease and that the remainder of this lease, as amended, will remain in effect.

31. **LOCAL HIRE.** The lessee is encouraged to hire and employ local and Alaska residents and companies, to the extent they are available and qualified, for work performed on the leased area. Lessees shall submit, with the plans of operations, a proposal detailing the means by which the lessee will comply with this measure. The lessee is encouraged to coordinate with employment services offered by the State of Alaska and local communities to employ apprentices to perform work in the leased area and to recruit employees from local communities.

32. **CONDITIONAL LEASE.** If all or a part of the leased area is land that has been selected by the state under laws of the United States granting lands to the state, but the land has not been patented to the state by the United States, then this lease is a conditional lease as provided by law until the patent becomes effective. If for any reason the selection is not finally approved, or the patent does not become effective, any rental, royalty, or other production or profit-based payments made to the state under this lease will not be refunded.

33. **NONDISCRIMINATION.** The lessee and the lessee's contractors and subcontractors may not discriminate against any employee or applicant because of race, religion, marital status, change in marital status, pregnancy, parenthood, physical handicap, color, sex, age, or national origin as set out in AS 18.80.220. The lessee and its contractors and subcontractors must, on beginning any operations under this lease, post in a conspicuous place notices setting out this nondiscrimination provision.

34. **DEFINITIONS.** All words and phrases used in this lease are to be interpreted where possible in the manner required in respect to the interpretation of statutes by AS 01.10.040. However, the following words have the following meanings unless the context unavoidably requires otherwise:

(1) "oil" means crude petroleum oil and other hydrocarbons, regardless of gravity, that are produced in liquid form by ordinary production methods, including liquid hydrocarbons known as distillate or condensate recovered by separation from gas other than at a gas processing plant;

(2) "gas" means all natural gas (except helium gas) and all other hydrocarbons produced that are not defined in this lease as oil;

(3) "associated substances" means all substances except helium produced as an incident of production of oil or gas by ordinary production methods and not defined in this lease as oil or gas;

(4) "drilling" means the act of boring a hole to reach a proposed bottom hole location through which oil or gas may be produced if encountered in paying quantities, and includes redrilling, sidetracking, deepening, or other means necessary to reach the proposed bottom hole location, testing, logging, plugging, and other operations necessary and incidental to the actual boring of the hole;

(5) "reworking operations" means all operations designed to secure, restore, or improve production through some use of a hole previously drilled, including, but not limited to, mechanical or chemical treatment of any horizon, plugging back to test higher strata, etc.;

(6) "paying quantities" means production in quantities sufficient to yield a return in excess of operating costs, even though drilling and equipment costs may never be repaid and the undertaking considered as a whole may ultimately result in a loss; and

(7) "force majeure" means war, riots, acts of God, unusually severe weather, or any other cause beyond the lessee's reasonable ability to foresee or control and includes operational failure of existing transportation facilities and delays caused by judicial decisions or lack of them.

35. ROYALTY ON PRODUCTION. Except for oil, gas, and associated substances used on the leased area for development and production or unavoidably lost, the lessee shall pay to the state as a royalty \_\_\_\_\_ percent in amount or value of the oil, gas, and associated substances saved, removed, or sold from the leased area and of the gas from the leased area used on the leased area for extraction of natural gasoline or other products.

36. VALUE. (a) For the purposes of computing royalties due under this lease, the value of royalty oil, gas, or associated substances shall not be less than the highest of:

(1) the field price received by the lessee for the oil, gas, or associated substances;

(2) the volume-weighted average of the three highest field prices received by other producers in the same field or area for oil of like grade and gravity, gas of like kind and quality, or associated substances of like kind and quality at the time the oil, gas, or associated substances are sold or removed from the leased or unit area or the gas is delivered to an extraction plant if that plant is located on the leased or unit area; if there are less than three prices reported by other producers, the volume-weighted average will be calculated using the lesser number of prices received by other producers in the field or area;

(3) the lessee's posted price in the field or area for the oil, gas, or associated substances; or

(4) the volume-weighted average of the three highest posted prices in the same field or area of the other producers in the same field or area for oil of like grade and gravity, gas of like kind and quality, or associated substances of like kind and quality at the time the oil, gas, or associated substances are sold or removed from the leased or unit area or the gas is delivered to an extraction plant if that plant is located on the leased or unit area; if there are less than three prices posted by other producers, the volume-weighted average will be calculated using the lesser number of prices posted by other producers in the field or area.

(b) If oil, gas, or associated substances are sold away from the leased or unit area, the term "field price" in subparagraph (a) above will be the cash value of all consideration received by the lessee or other producer from the purchaser of the oil, gas, or associated substances, less the lessee's actual and reasonable costs of transportation away from the leased or unit area to the point of sale. The "actual and reasonable costs of transportation" for marine transportation are as defined in 11 AAC 83.229(a), (b)(2), and (c) - (f).

(c) In the event the lessee does not sell in an arm's-length transaction the oil, gas, or associated substances, the term "field price" in subparagraphs (a) and (b) above will mean the price the lessee would expect to receive for the oil, gas, or associated substances if the lessee did sell the oil, gas, or associated substances in an arm's-length transaction, minus reasonable costs of transportation away from the leased or unit area to the point of sale or other disposition. The lessee must determine this price in a consistent and logical manner using information available to the lessee and report that price to the state.

(d) The state may establish minimum values for the purposes of computing royalties on oil, gas, or associated substances obtained from this lease, with consideration being given to the price actually received by the lessee, to the price or prices paid in the same field or area for production of like quality, to posted prices, to prices received by the lessee and/or other producers from sales occurring away from the leased area, and/or to other relevant matters. In establishing minimum values, the state may use, but is not limited to, the methodology for determining "prevailing value" as defined in 11 AAC 83.227. Each minimum value determination will be made only after the lessee has been given notice and a reasonable opportunity to be heard. Under this provision, it is expressly agreed that the minimum value of royalty

oil, gas, or associated substances under this lease may not necessarily equal, and may exceed, the price of the oil, gas, or associated substances.

37. **LESSEE SALES INFORMATION.** Lessee acknowledges that sales information, including but not limited to confidential sales pricing terms, of the lessee for the production and sale of hydrocarbons from the lease may be used by the Department to administer the lease, and other leases in the field or area, including valuation for royalty purposes and the Department may disclose such confidential sales information to other producer/lessees in the same field or area in the administration, collection, and/or audit of royalties and net profit share payments. The Department also reserves the right to utilize information filed by the lessee with the Department of Revenue in the administration, collection, and/or audit of royalties and net profit share payments.

38. **ROYALTY IN VALUE.** Except to the extent that the state elects to receive all or a portion of its royalty in kind as provided in Paragraph 39 below, the lessee shall pay to the state that value of all royalty oil, gas, and associated substances as determined under Paragraph 36 above. Royalty paid in value will be free and clear of all lease expenses (and any portion of those expenses that is incurred away from the leased area), including, but not limited to, expenses for separating, cleaning, dehydration, gathering, saltwater disposal, and preparing the oil, gas, or associated substances for transportation off the leased area. All royalty that may become payable in money to the State of Alaska must be paid on or before the last federal banking day of the calendar month following the month in which the oil, gas, or associated substances are produced. The amount of all royalty in value payments which are not paid when due under this lease or the amount which is subsequently determined to be due to the state or the lessee as the result of a redetermination will bear interest from the last federal banking day of the calendar month following the month in which the oil, gas, or associated substances were produced, until the obligation is paid in full. Interest shall accrue at the rate provided in AS 38.05.135(d) or as may later be amended. Royalty payments must be accompanied by such information relating to valuation of royalty as the state may require which may include, but is not limited to, run tickets, evidence of sales, shipments, and amounts of gross oil, gas, and associated substances produced.

39. **ROYALTY IN KIND.** (a) At the state's option, which may be exercised from time to time upon not less than 50 days' notice to the lessee, the lessee shall deliver all or a portion of the state's royalty oil, gas, or associated substances produced from the leased area in kind. Delivery will be on the leased area, unit area, or at a place mutually agreed to by the state and the lessee, and must be delivered to the State of Alaska or to any individual, firm, or corporation designated by the state.

(b) Royalty oil, gas, or associated substances delivered in kind must be delivered in good and merchantable condition, of pipeline quality, and free and clear of all lease expenses (and any portion of those expenses incurred away from the leased area), including, but not limited to, expenses for separating, cleaning, dehydration, gathering, saltwater disposal, and preparing the oil, gas, or associated substances for transportation off the leased area.

(c) After having given notice of its intention to take, or after having taken its royalty oil, gas, or associated substances in kind, the state, at its option, may elect to receive a different portion or none of its royalty in kind. If, under federal regulations, the taking of royalty oil, gas, or associated substances in value by the state creates a supplier-purchaser relationship, the lessee hereby waives its right to continue to receive royalty oil, gas, or associated substances under that relationship, and further agrees that it will require any purchasers of the royalty oil, gas, or associated substances likewise to waive any supplier-purchaser rights.

(d) The lessee shall furnish storage for royalty oil, gas, and associated substances produced from the leased or unit area to the same extent that the lessee provides storage for the lessee's share of oil, gas, and associated substances. The lessee shall not be liable for the loss or destruction of stored royalty oil, gas and associated substances from causes beyond the lessee's ability to control.

(e) If a state royalty purchaser refuses or for any reason fails to take delivery of oil, gas, or associated substances, or in an emergency, and with as much notice to the lessee as is practical or reasonable under the circumstances, the state may elect without penalty to underlift for up to six months all or a portion of the state's royalty on oil, gas, or associated substances produced from the leased or unit area and taken in kind. The state's right to underlift is limited to the portion of royalty oil, gas, or associated substances that the royalty purchaser refused or failed to take delivery of, or the portion necessary to meet the emergency condition. Underlifted oil, gas, or associated substances may be recovered by the state at a daily rate not to exceed 100 percent of its royalty interest share of daily production at the time of the underlift recovery.

40. **REDUCTION OF ROYALTY.** Lessee may request a reduction of royalty in accordance with the applicable statutes and regulations in effect on the date of application for the reduction.

41. **EFFECTIVE DATE.** This lease takes effect on

BY SIGNING THIS LEASE, the state as lessor and the lessee agree to be bound by its provisions.

STATE OF ALASKA

By: \_\_\_\_\_

Director, Division of Oil and Gas

STATE OF ALASKA        )  
                                  ) ss.  
Third Judicial District    )

On \_\_\_\_\_, before me appeared \_\_\_\_\_ of the Division of Oil and Gas of the State of Alaska, Department of Natural Resources, and who executed this lease and acknowledged voluntarily signing it on behalf of the State of Alaska as lessor.

\_\_\_\_\_  
Notary public in and for the State of Alaska  
My commission expires \_\_\_\_\_

LESSEE: \_\_\_\_\_

Signature: \_\_\_\_\_

Printed Name/Title: \_\_\_\_\_

INSERT NOTARY ACKNOWLEDGMENT OF LESSEE'S SIGNATURE HERE.

LESSEE: \_\_\_\_\_

Signature: \_\_\_\_\_

Printed Name/Title: \_\_\_\_\_

INSERT NOTARY ACKNOWLEDGMENT OF LESSEE'S SIGNATURE HERE.

LESSEE: \_\_\_\_\_

Signature: \_\_\_\_\_

Printed Name/Title: \_\_\_\_\_

INSERT NOTARY ACKNOWLEDGMENT OF LESSEE'S SIGNATURE HERE.

Attachment 1. Alaska Department of Natural Resources, Division of Oil & Gas  
Submittal of Well Data Required by DNR Lease

Data shall be submitted to the Division in a digital format, generally in PDF. For spreadsheets, include the original Excel document. For images such as maps or charts, include a high-resolution TIFF or JPEG. For logs, see formats specified below, but include a graphical image file of the logs as a PDF or TIFF in addition to the final merged data file of the log curves. Data may be submitted on CD, DVD or USB mass storage device (include any necessary cables). Required data shall include any and all of the following:

1. A copy of the well completion report (AOGCC Form 10-407) for each well bore.
2. Daily drilling reports or a summary report of daily drilling.
3. Latitudinal and longitudinal coordinates for each well, pilot hole, and plugged back well bore with completed surface and bottom hole locations. Coordinates can be based upon either the NAD 83 or NAD 27 geodetic datum as long as the datum used is clearly specified.
4. Directional survey for each well, pilot hole, and plugged back well bore.
5. A list of all logs run and the depth interval covered for each well, pilot hole, and plugged back well bore.
6. A list of formations and other geologic markers encountered and the measured depths (MD) and true vertical depths (TVD) of each, for each well, pilot hole, and plugged back well bore.
7. Summary of cored intervals (conventional and sidewall), including depth, formation name, lithology, presence of oil, gas, gas hydrates, and water, porosity, fractures and apparent dips; indicate "none" on completion report or in an attachment if no cores were taken.
8. Core reports including lab analyses of lithology, porosity, permeability (vertical and horizontal, air and liquid), density, capillary pressure, and fluid saturation, if available.
9. Conventional and sidewall core photos (plain light and ultraviolet), if applicable.
10. Identified formation names and corresponding depths for oil, gas, and gas hydrate shows. Indicate "none" on the completion report or in an attachment if no shows were observed.
11. Identified depth zones of abnormal pressure. Indicate "none" on the completion report or in an attachment if none were observed.
12. A synopsis or summary of testing and all fluid recovery efforts, including production tests (IP), drill stem tests (DST), wireline formation tests (i.e. repeat formation tests (RFT) and modular dynamics tests (MDT)), and any other production and formation testing data; the summary should include test date, time, depth, formation name, method of operation, recovered fluid type(s) and amount(s), fluid rate, gas-oil ratio (GOR), oil gravity, pressure, and choke size, when available. If no tests were undertaken, indicate "none" where appropriate on the completion report or in an attachment, if tests were undertaken but failed to recover fluids indicate "no recovery".
13. Pressure build-up and fluid PVT analyses, if applicable.
14. Open flow potential test reports and report attachments to AOGCC Forms 10-421.
15. Well test procedures, field chronologies, and field data; including details necessary for evaluation (intervals open to test; volumes of oil, gas, water, mud, and other borehole substances; API gravity; gas density; wellhead and down hole pressure; and formation and wellhead temperature).
16. Geochemical and formation fluid analyses and reports, if applicable.
17. Down hole and surface fluid sampling procedures, field chronologies, raw data, and laboratory test results for all water and hydrocarbon-bearing zones (oil, gas, gas hydrates) sampled; including details sufficient to fully evaluate quality of sample data.
18. Permit to drill (AOGCC form 10-401) and the survey as-built of the well location.
19. LAS Version 2, TAP, TIF, LIS and DLIS (if available) files of final merged open-and cased-hole log data, including specialty logs (such as Schlumberger's cyberlook, formation microscanners and dipmeter logs), measured-while-drilling (MWD) and logged-while-drilling (LWD) logs. Include a graphical image file of the 2-inch MD & TVD logs as a PDF or TIFF in addition to the log data file.
20. LAS Version 2 of final composite mudlog or lithology log curves. Include a graphical image file of the final 2-inch MD & TVD logs, with lithology display, oil, gas, and gas hydrate show indicators, mud properties, and cuttings descriptions and report as a PDF or TIFF in addition to the log data file.
21. Clear, legible files of all well data and reports including, but not limited to, paleontology, palynology, petrography (including point-count analyses), X-ray diffraction analyses, SEM micrographs, thermal maturity, vitrinite reflectance, total organic carbon, RockEval pyrolysis, geochronology, fission track analyses, fluid inclusion analyses, Mercury injection capillary pressure analyses, chemical analyses (EPMA, XRF, ICP, etc.), isotope analyses, water chemistry, burial and temperature history analyses, strain analyses, acoustic analyses, gas hydrate analyses and well pressure and temperature survey analyses.

22. Final reports of velocity, checkshot or VSP surveys (an ASCII format digital version of the above data shall also be submitted), including seismic profile data in SEG-Y format. Indicate "none" in your response to this request if no velocity, checkshot or VSP surveys were undertaken. Submission of velocity, checkshot, and VSP surveys is always required by DNR under the operator surface-use permit obligations.
23. All coalbed core, gas, and water quality reports including lab analyses of core lithology, coal rank, vitrinite reflectance, maceral composition, total organic carbon, ash, sulfur and BTU content, moisture content, cleating, adsorption/desorption data, residual gas measurements, porosity and permeability analyses, core photos, if available.
24. Any other geoscience- and engineering-related data sets from the well(s).

Please note: Physical samples of well cuttings or cores specified in 20 AAC 25.071(b)(2) and 20 AAC 25.071(b)(4) should be sent to AOGCC, not to the Division.

All material should be either hand-carried by bonded courier or mailed by registered mail to:

Resource Evaluation Section  
Alaska Department of Natural Resources, Division of Oil & Gas  
550 West 7th Avenue, Suite 1100  
Anchorage, AK 99501-3510  
Email: [DOG.REdata@alaska.gov](mailto:DOG.REdata@alaska.gov)





THE STATE  
*of* **ALASKA**  
GOVERNOR BILL WALKER

Department of Natural Resources

COMMISSIONER'S OFFICE

550 W. 7<sup>th</sup> #1400  
Anchorage, AK 99501  
Main: 907.269.8431  
Fax: 907.269.8918

January 24, 2018

Honorable Chair Giessel and Members of the Senate Resources Committee:

During our department presentation to your committee on January 22, 2018, a member requested additional information related to two issues. This letter is intended to provide answers to those questions.

1. **What is the average bonus bid on the North Slope?**

*During the 2017 lease sale, the average winning bid was \$121.37 per acre.*

2. **What will the royalty rate in ANWR be?**

*The royalty rate will be 16.67%*

Sincerely,

A handwritten signature in black ink, appearing to read "Ed King".

Ed King  
Special Assistant  
Department of Natural Resources



THE STATE  
of **ALASKA**  
GOVERNOR BILL WALKER

Department of Natural Resources

DIVISION OF OIL & GAS  
550 WEST 7<sup>TH</sup> AVENUE, SUITE 1100  
ANCHORAGE, ALASKA 99501-3563  
Mail: 907-269-8800  
Fax: 907-269-8939

October 6, 2017

**NOTICE OF SALE  
BEAUFORT SEA AREAWIDE 2017W  
NORTH SLOPE AREAWIDE 2017W and  
NORTH SLOPE FOOTHILLS AREAWIDE 2017  
COMPETITIVE OIL AND GAS LEASE SALES**

The Alaska Department of Natural Resources (DNR), Division of Oil and Gas (DO&G), is giving notice pursuant to AS 38.05.945(a)(4) that it is offering State lands for competitive oil and gas leasing in the Beaufort Sea Areawide 2017W (BSA 2017W), the North Slope Areawide 2017W (NSA 2017W), and the North Slope Foothills Areawide 2017 (FHA 2017) Competitive Oil and Gas Lease Sales. This notice is available on the State of Alaska Online Public Notice System at <http://aws.state.ak.us/OnlinePublicNotices/>.

In-person bid submission – Monday, December 4, 2017 from 9:00 a.m. to 4:00 p.m. at Suite 800 of the Atwood Building, 550 West 7<sup>th</sup> Avenue, Anchorage, Alaska or by mail to DNR Division of Oil & Gas, Attn: Lease Sale, 550 W 7th Avenue, Suite 1100, Anchorage, Alaska 99501-3563.

Public bid opening – Wednesday, December 6, 2017 from 9:00 a.m. until all bids are read at the Tubughnenq' (Tyonek) Meeting Room, Dena'ina Center, 600 West 7<sup>th</sup> Avenue, Anchorage, Alaska.

**Areawide Lease Sale Locations**

The Beaufort Sea Areawide is divided into 591 tracts ranging in size from 530 to 5,760 acres. These tracts are within the North Slope Borough and consist of state-owned tide and submerged lands in the Beaufort Sea between the Canadian border and Point Barrow. The northern boundary of the Areawide is along the federal Alaska Outer Continental Shelf. The southern fringe of the sale area includes some state-owned uplands lying between the National Petroleum Reserve – Alaska (NPR-A) and the Arctic National Wildlife Refuge (ANWR). Some tracts are jointly owned by the State of Alaska and Arctic Slope Regional Corporation (ASRC).

The North Slope Areawide is divided into 3,137 tracts, ranging in size from 640 to 5,760 acres. Tracts in this sale area are within the North Slope Borough between the Canning River and ANWR on the east and the Colville River and NPR-A on the west. The southern boundary of the sale area is the Umiat Meridian baseline. The Areawide is divided into North and South Sub-regions. Some tracts are jointly owned by the State of Alaska and ASRC.

The North Slope Foothills Areawide is divided into 1,347 tracts ranging in size from 480 to 5,760 acres. These tracts are located between ANWR and NPR-A. The northern boundary of the sale area is the Umiat Meridian baseline and the southern boundary is the Gates of the Arctic National Park and Preserve.

**Sale Documents**

Complete details regarding these lease sales are on the DO&G website at <http://dog.dnr.alaska.gov/Services/LeaseSale> under Current Lease Sales. Sale documents include this Notice of Sale, Sale Announcement and Instructions to Bidders, Attachment A with estimated acreages and deferred tracts, lease forms, mitigation measures, Bid Form for DNR Areawide Oil & Gas Lease Sale, and tract map. These documents are also available in the following locations:

Nuiqsut Trapper School Library, Nunamiut School Library in Anaktuvuk Pass, Harold Kaveolook School Library in Kaktovik, Meade River School Library in Atkasuk, Tuzzy Consortium Library in Barrow, Alaska Resource Library & Information Services, Z.J. Loussac Public Library in Anchorage, and the Alaska State Library in Juneau.

If you are unable to access this information, call the Leasing Section at (907) 269-8800 or email [dog.leasing@alaska.gov](mailto:dog.leasing@alaska.gov). You may subscribe to lease sale email announcements at <http://list.state.ak.us/mailman/listinfo/DOG.Licensing>.

**Sale Terms and Conditions**

Beaufort Sea Areawide 2017W						
Lease Sale Tracts	Bid Variable	Minimum Bid	Royalty Rate	Primary Lease Term	Annual Rental Rate	Lease Form
State/ASRC Tracts	Cash Bonus	\$25.00 per acre	16.66667% Fixed	10 Years	Years 1 – 7: \$10.00 per acre Years 8 – 10: \$250.00 per acre**	DOG 201503W AS
BSA 2017W Tracts	Cash Bonus	\$25.00 per acre	16.66667% Fixed	8 Years*	Years 1 – 8: \$10.00 per acre	DOG 201710W
*Under provisions of AS 38.05.180(m), state oil and gas leases may receive a one-time lease extension under certain conditions, upon request.						
**Annual rental will be as listed above; except that beginning in the year after the year in which sustained production commences on the lease or the state otherwise determines in its sole discretion, upon request, that the lessee has exercised reasonable diligence in exploring and developing the lease, the annual rental will be \$10.00 per acre or fraction of an acre. In evaluating a request to decrease rental based on the exercise of reasonable diligence, the state will consider the funds expended by the lessee to explore and develop the lease and the types of work completed by or on behalf of the lessee on this lease.						

North Slope Areawide 2017W						
Lease Sale Tracts	Bid Variable	Minimum Bid	Royalty Rate	Primary Lease Term	Annual Rental Rate	Lease Form
State/ASRC Tracts	Cash Bonus	\$25.00 per acre	16.66667% Fixed	10 Years	Years 1 – 7: \$10.00 per acre Years 8 – 10: \$250.00 per acre**	DOG 201503W AS
North Sub-Region Tracts	Cash Bonus	\$25.00 per acre	16.66667% Fixed	8 Years*	Years 1 – 8: \$10.00 per acre	DOG 201710W
South Sub-Region Tracts	Cash Bonus	\$25.00 per acre	12.5% Fixed	8 Years*	Years 1 – 8: \$10.00 per acre	DOG 201710W
*Under provisions of AS 38.05.180(m), state oil and gas leases may receive a one-time lease extension under certain conditions, upon request.						
**Annual rental will be as listed above; except that beginning in the year after the year in which sustained production commences on the lease or the state otherwise determines in its sole discretion, upon request, that the lessee has exercised reasonable diligence in exploring and developing the lease, the annual rental will be \$10.00 per acre or fraction of an acre. In evaluating a request to decrease rental based on the exercise of reasonable diligence, the state will consider the funds expended by the lessee to explore and develop the lease and the types of work completed by or on behalf of the lessee on this lease.						

North Slope Foothills Areawide 2017						
Lease Sale Tracts	Bid Variable	Minimum Bid	Royalty Rate	Primary Lease Term	Annual Rental Rate	Lease Form
FHA 2017 Tracts	Cash Bonus	\$10.00 per acre	12.5% Fixed	10 Years	Year 1: \$1.00 per acre Year 2: \$1.50 per acre Year 3: \$2.00 per acre Year 4: \$2.50 per acre Years 5+: \$3.00/acre	DOG 201710

### New Lease Provisions

Lease forms DOG 201710 and DOG 201710W listed in the Sale Terms and Conditions section of this document include changes from lease forms DOG 201503 and DOG 201509W most recently used by the Division for Beaufort Sea, North Slope, and North Slope Foothills Area-wide lease sales.

The changes include the following new lease provision with re-numbering of subsequent paragraphs.

#### 37. LESSEE SALES INFORMATION

The following lease paragraphs have been changed:

4. EXTENSION (d)
5. RENTALS (a)
6. RECORDS (a) and (b)
7. APPORTIONMENT OF ROYALTY FROM APPROVED UNIT
10. PLAN OF DEVELOPMENT (a) and (b)
13. DILIGENCE AND PREVENTION OF WASTE (d)
15. UNITIZATION (d)
20. DEFAULT AND TERMINATION; CANCELLATION (a)
23. BONDS (a) and (d)
31. LOCAL HIRE
38. ROYALTY IN VALUE (re-numbered paragraph)

In addition, there are deletions in the following lease paragraphs:

9. PLAN OF OPERATIONS (h)

### Tracts Deferred or Deleted from Sale

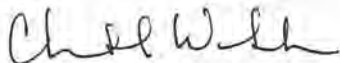
Deferred or deleted lease sale tracts will not be offered for lease in this sale, but may be included in future lease sales. DO&G reserves the right to delete or defer any additional acreage or tracts from the sale at any time prior to issuance of the lease. Currently, deferred or deleted lease sale tracts are listed on Attachment A of the Sale Announcement and Instructions to Bidders. Check <http://dog.dnr.alaska.gov/Services/LeaseSale> for updated Attachment A documents.

### Best Interest Findings to Offer Oil and Gas Leases in Area-wide Sales

These lease sales are being held according to AS 38.05.035(e) and AS 38.05.180. Under these statutes, land that is subject to a best interest finding issued within the previous 10 years may be offered for oil and gas leasing. The finding sets forth the facts, policies, and applicable laws and regulations upon which the Director based his determination that oil and gas lease sales in an Area-wide sale will best serve the interests of the State. Every year, the Director makes a request for substantial new information that may justify a supplement to the finding and issues a response to information received. Best interest finding documents and supplements for these sales can be found by searching with filters for Name and Region at <http://dog.dnr.alaska.gov/Information/DocumentLibrary>. If you are unable to access this information, call the Leasing Section at (907) 269-8800 or email [dog.bif@alaska.gov](mailto:dog.bif@alaska.gov).

### Americans with Disabilities Act Compliance

The State of Alaska, DNR, DO&G complies with Title I of the Americans with Disabilities Act 1990. This publication will be made available in alternative communication formats upon request. Please call (907) 269-8800 or email [dog.leasing@alaska.gov](mailto:dog.leasing@alaska.gov) to make any necessary arrangements.



Chantal Walsh  
Director  
Division of Oil and Gas