

SCOMM

#46:14

DELIVER TO: <u>SAP Ned Farguhar</u>	LOCATION: <u>465-240d586-</u>
FROM: <u>Betty Harrison</u>	LOCATION: <u>265-4244</u>
TELEPHONE/TELECOPIER # _____	TOTAL NUMBER OF PAGES: <u>37</u>
TRANSMITTING ON/SPEED _____	DATE: <u>9/7</u> TIME: <u>12:05</u>
PHONE FOR PROBLEMS-NAME/NUMBER: <u>265-4244</u>	<u>and see King's Room</u>
COMMENTS: <u>Per Call, pls make necessary changes. Thanks.</u>	

1985 LEGISLATIVE PROPOSAL REQUEST FORM

DATE: August 30, 1984

DEPARTMENT: Department of Natural Resources (Oil and Gas)

SUBJECT OF PROPOSED BILL:

Royalty oil sales statewide change.

SUMMARY/EXPLANATION OF INTENT: (Why is legislation requested. Explain need. Attach additional sheet, if necessary.)

The proposed bill would 1) clarify and streamline procedural requirements for royalty oil sales by eliminating the best interest finding required by AS 38.05.035(e); and 2) enable the department to establish a regular program of short-term competitive royalty oil sales. The department proposes to conduct a competitive royalty oil (continued on attachment)
ESTIMATED FISCAL IMPACT: 0

Capital: 0

Operating: 0

Has this or a substantially similar bill been introduced (and not passed) in the Legislature in previous session? No
Has it been drafted and but not introduced: (If so, please attach copy of approved draft and give Department of Law file no.: 377-_____-_____.)

Why wasn't it passed?

Rate the bill's importance to the department by priority number (in relationship to your department's other requests if any).

COMMISSIONER'S SIGNATURE: _____
DATE: _____

Governor's Office Recommendation:

red: this should read "similar"

Continuation of Summary/Explanation of Intent:

sale in December, and it may wish to conduct similar competitive sales in the future. The statute requires legislative approval of royalty contracts except for small volume sales and sales of one year or less to relieve storage or market conditions. The statute further provides that a short-term sale to relieve storage or market conditions may not be continued after the end of one year or renewed with the same party without prior approval of the legislature.

The Department of Law has advised the department that if a second competitive sale were to be held in 1985 (assuming the 1984 proposed competitive sale proceeds as planned), successful bidders in the 1984 sale would not be able to participate in the 1985 sale due to the provision prohibiting continuation of a contract with the same party beyond one year without approval of the legislature. Thus, without the proposed statutory change, competition in any subsequent sales would be severely limited. The proposed legislation would allow companies that are successful bidders in the December competitive sale to participate in succeeding competitive sales for short-term contracts without requiring legislative approval of those contracts.

Regarding clarification of procedural requirements for royalty sales, AS 38.05.035 ~~(a)(1)~~ arguably applies to royalty sales even though the finding and related notice requirements are duplicative of the extensive royalty oil sale procedures in AS 38.05.182, .183, and AS 38.06. (Draft legislation attached.)

(e) . 1c

red: AS 38.05.035(a)(1)
Should read:
AS 38.05.035(e)

Offered:

Referred:

Original sponsors:

1 IN THE HOUSE

2

HOUSE BILL NO.

3

IN THE LEGISLATURE OF THE STATE OF ALASKA

4

FOURTEENTH LEGISLATURE - FIRST SESSION

5

A BILL

6 For an Act entitled: "An Act relating to royalty oil; and providing
7 for an effective date."

8 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

9 *Section 1. As 38.05.183 is amended by adding a new subsection to
10 read:

11 (f) AS 38.05.035^(e)~~(a)(1)~~ does not apply to a sale,
12 exchange or other disposal of oil or gas under this section.

13 *Section 2. AS 38.06.055(c) is amended to read:

14 (c) A sale, exchange, or other disposition of oil or gas made
15 other than by competitive bid under (b)(1) of this section may not
16 be continued after the end of one year or renewed with the same
17 party to provide relief for market or storage conditions without
18 the prior approval of the legislature under (a) of this section.

19 *Section 3. This act takes effect immediately in accordance with
20 AS 01.10.070(c).

telecopy → Kay
draft transmitted let
no fiscal impact?

D R A F T

Under the authority of art. III, sec. 18, of the Alaska Constitution, I am transmitting a bill relating to royalty oil. The bill would (1) clarify and streamline procedural requirements for royalty oil and gas sales by expressly providing that the best-interest finding set out in AS 38.05.035(e) does not apply to those sales; and (2) enable the Department of Natural Resources to establish a regular program of short-term competitive royalty oil sales.

It is unclear whether AS 38.05.035(e) applies to royalty oil and gas sales. Royalty oil and gas sales have detailed finding and notice requirements set out in AS 38.05.182, 38.05.183, and AS 38.06, and are expressly committed to commissioner actions. AS 38.05.035(e), on the other hand, is essentially duplicative of those other processes and concerns actions taken by the director of the division of lands. Although we believe that the provisions of AS 38.05.035(e) are not presently applicable to oil and gas sales, such confusion does cast a cloud over royalty oil sales (particularly those that are entered into because of an emergency situation). The amendment in sec. 1 of the bill resolves the issue.

The second change, in sec. 2 of the bill, would allow competitive royalty oil sales for terms of less than

DELIVER TO: Kay Beatty	LOCATION: Bill 182
FROM: Ted Egan	LOCATION: Bill - Sec. 1
TELEPHONE/TELETYPE: N	TOTAL NUMBER OF PAGES: 2
TRANSMITTING ON/SPEED: 9	DATE: 10/15
PHONE FOR PROBLEMS/NUMBER: Alaska 465-2400	TIME: 9:50A
COMMENTS	

one year to be conducted without legislative approval of those sales. To await legislative approval under a competitive bid situation for contracts of one year or less would defeat the entire purpose of that type of short-term competitive sales. Under the present statutory scheme, however, there is a serious question as to whether a party who gained royalty oil under one competitive sale could re-bid in a subsequent royalty oil sale if the combination of the two sales would lead to that particular buyer receiving oil for more than a one year period. Although it has been the consistent position of this and previous administrations that the requirement of legislative approval is unconstitutional, administrations have always, as a matter of comity, respected the legislature's desire to be consulted in long-term or negotiated royalty oil contracts. Further, the presence of the statute, whether or not constitutional, would cast a cloud on any sale. Thus we believe that a clarification to allow short-term competitive royalty oil sales would be in the best interests of all.

Sincerely,

Bill Sheffield
Governor

DRAFT

November 19, 1984

DISCUSSION OUTLINE PROPOSED ROYALTY OIL STATUTE REVISION

Summary

The royalty oil statute needs revision in order to establish a program of regular competitive sales, a policy option the Sheffield administration may wish to pursue in 1986 after analyzing results from the December sale. In addition, other revisions are needed to clarify overall policy goals and streamline procedures.

Statement of Problem

1. The statute does not clearly define the purpose and policy goals of royalty oil sales. The statute does not provide effective guidance for assessing in-kind versus in-value taking, or competitive versus negotiated sales.
2. The prescribed procedures are cumbersome.
3. The statute as written arguably would not allow continuing, short-term competitive sales without legislative approval.
4. There is uncertainty over the division of responsibilities between the legislative and executive branches.
5. The result of these problems is that the state does not project a business-like atmosphere in conducting royalty oil sales. In past years we have seen extended arguments between the executive and legislative branches, and within the legislature itself, over proposed royalty oil contracts. Lawsuits have been filed. A proposed refinery and petrochemical complex based on a royalty oil contract failed to materialize. These problems cause uncertainty and delay for royalty oil purchasers, as well as administrative difficulties for the agency. Most important, failure to clearly define the purpose of the program may jeopardize our ability to maximize the state's income from royalty oil sales.

Recommendations for Statute Revision

1. Clarify policy criteria for sales.
 - a. The primary policy goal for royalty oil sales should be to maximize the state's income.
 - b. To the extent they are consistent with the primary objective of maximizing income, secondary policy goals should be to:

DRAFT

- Supply existing in-state refiners and utilities at market prices.
- Promote new in-state projects based on royalty oil and gas to the extent they are economically feasible at market prices in the absence of a royalty oil contract.
- Promote expansion of foreign markets for Alaska resources.
- Promote competition in the in-state market by giving preferences to in-state suppliers of petroleum products in competitive sales.

2. Clarify and Streamline Procedural Requirements.

- a. Establish presumption for short-term (up to two years), competitive bid contracts which would not be approved by the legislature.
- b. All long-term, negotiated contracts would require legislative approval.

Negotiated contracts would be allowed to achieve the first three secondary policy goals described above.
- c. Short-term negotiated contracts (one year or less) could be allowed without legislative approval in specific, defined circumstances (such as emergency shortages and storage conditions).
- d. Add requirement for an annual royalty report to be submitted to the legislature. Establish a schedule for contract submission and, if possible, for review by the legislature.
- e. Clarify the role of the royalty oil and gas development advisory board.

Specific Proposed Revisions

- Consolidate and clarify procedural requirements of AS 38.05.182 - .183, AS 38.05.035(e), 38.05.345 and 38.06.
- Adopt general procedures to cover all royalties taken in-kind under AS 38.05.135-.181 (energy minerals including oil, gas, coal, geothermal, phosphates, oil shale, sodium, sulphur and potassium), and more specific procedures to cover only oil and gas.

DRAFT

- Add a provision requiring the Commissioner to reserve in-kind taking rights in all leases issued under 38.05.135-.181.
- Retain (or clarify) the present in-kind presumption in 38.05.182(a) (applies only to oil and gas). Eliminate the present opportunity for the Legislature to revoke a determination to take in-value in 38-.05.182(b).
- Add a requirement that the Commissioner submit an annual report on the royalty status of all producing leases to the Legislature within 10 days of the convening of a regular legislative session. The report would be similar in format and content to the Five-Year Oil and Gas Leasing Program document, and would include the percentages of royalties taken in-kind and in-value for each resource; the percentage of royalties purchased by in-state refiners/processors and the percentage of royalty oil or other resource actually processed in the state; proposed royalty contracts (if any) and .035 findings to support them.
- Generally, eliminate all requirements for separate procedures in 38.06 and 38.05.182-.183, and rely on the general disposition procedures in 38.05.035 and .345.

Incorporate all findings for specific items (such as determination of projected in-state hydrocarbon needs; determination to waive competitive bidding; etc.) into best interest findings under 38.05.035(e).

- Repeal most of AS 38.06 (Royalty Board).

Reestablish the board under .183 as an advisory group to the Commissioner of Natural Resources. Require the board to hold a hearing and make a written recommendation to the Commissioner on proposed sales which require legislative approval.

- Transfer 38.06.055 to .183 (legislative approval requirement and exemptions for short-term and small volume sales). Expand exemptions to include competitively bid contracts with terms of two years or less. (The requirements of .055 would continue to apply only to oil and gas.)
- Transfer the confidentiality provisions in 38.06.060 to .183.

MEMORANDUM

To: Senator Jay Kertulla

From: Jonathan Sperber, Committee Aide
House Special Committee on Oil and Gas

Date: May 9, 1985

Re: Underlift Amendment

Attached is a copy of the proposed amendment to CSHB 103, incorporating language changes suggested by Senator Halford and approved by Director Kay Brown and Commissioner Wunnicke.

I have also attached an opinion by Legislative Counsel Randall Moen stating that this amendment does not fall within the scope of the title of CSHB 103. It is the belief of both the Department of Law and the Department of Natural Resources, however, that underlifting is a form of disposal and that there is therefore no problem in attaching this amendment to the bill.

The purpose of this amendment is to allow the commissioner to defer disposing of royalty natural gas in the Southcentral marketplace until a later date. The state must dispose of its natural gas at the time of receipt, and the date of receipt and disposal is directly affected by underlifting of the gas.

As mentioned in 38.05.183(a), there may be a "disposal in whole or in part of a right to receive future mineral production under a state lease under this chapter." In this case, the state is giving up its right to receive royalty natural gas at this time, in order to exercise its right to receive royalty natural gas at a later date.

Please call me at 465-4930/4941 if I can be of assistance to you or your staff in this matter.

REMARKS

by

KAY BROWN, DIRECTOR, DIVISION OF OIL & GAS

on

CS HB 103 (Oil and Gas)

to

HOUSE RESOURCES COMMITTEE

February 25, 1985

Thank you Mr. Chairman. For the record, I'm Kay Brown, Director of the Division of Oil and Gas for the Alaska Department of Natural Resources. I appreciate the opportunity to address the committee on CS HB 103.

This bill makes two technical changes to the royalty oil and gas disposal statute.

SECTION 1 of the bill would remove royalty oil and gas disposals from the procedures that govern all disposals of interest in state land or resources under AS 38. It is unclear whether AS 38.05.035(e) applies to royalty oil and gas sales. Royalty oil and gas sales have detailed finding and notice requirements under AS 38.05.182, 183 and AS 38.06. Although we believe that .035 is not presently applicable to royalty oil and gas sales, the possibility that it does apply would cast a cloud over sales that had to be entered into because of an emergency situation. Further, elimination of the .035 requirement streamlines the procedural requirements by removing conflicting timelines for disposal.

SECTION 2 of the bill would allow continuing competitive royalty oil sales

for terms of less than one year to be conducted without legislative approval of those sales. AS 38.06.055(a) provides that the legislature will approve all royalty oil and gas sales. Subsection (b) of that section sets out several exceptions for short-term and small volume sales which do not require legislative approval. Subsection (b)(1) makes an exception for sales of one year or less to relieve storage or market conditions, and this is the section under which we held the competitive sale in December 1984. Subsection (c), which is the section being amended in CS HB 103, goes on to say that a sale made under (b)(1) may not be continued after the end of one year or renewed with the same party without the prior approval of the legislature under (a) of the statute.

The Department of Law has advised us that there is a serious question as to whether a party who gained royalty oil under one competitive sale could re-bid in a subsequent royalty oil sale if the combination of the two sales would lead to that particular buyer receiving oil for more than a one-year period.

We see no reason why a company which bids and wins in one competitive sale should not be able to bid again the next year and again win the right to receive oil if it bids the highest price.

To await legislative approval under a competitive bid situation for contracts of one year or less would defeat the entire purpose of that type of short-term competitive sale.

Although it has been the consistent position of this and previous

administrations that the requirement of legislative approval is unconstitutional, administrations have always, as a matter of comity, respected the legislature's desire to be consulted in long-term or negotiated royalty oil contracts. Further, the presence of the statute, whether constitutional or not, could cast a cloud on any subsequent competitive sale.

Mr. Chairman, while we have not yet made a firm decision on whether continuing competitive sales would be beneficial to the state, we would like to have that option available for consideration at the same time we are considering the new proposals for in-state use.

That concludes my remarks Mr. Chairman. Thank you very much for your time.

1585K

STATE OF ALASKA
THE LEGISLATURE

POUCH Y - STATE CAPITOL
JUNEAU, ALASKA 99811
907 465 3800

LEGISLATIVE AFFAIRS AGENCY

MEMORANDUM

May 9, 1985

SUBJECT: Constitutionality of amendment to
 CSHB 103(Fin)

TO: Representative Mike Davis

FROM: Randall J. Moen *RJM*
 Legislative Counsel

You have requested an amendment to CSHB 103(Fin), "An Act relating to prerequisites for the disposal of royalty oil and gas;", that, among other things, authorizes the commissioner of natural resources to enter into an agreement with affected field lease holders to store all or part of the state's royalty share of oil and gas before the end of 80 percent of the estimated field life.

In my opinion the amendment to CSHB 103(Fin) violates Article II, sec. 13, Constitution of the State of Alaska, which requires that "the subject of each bill shall be expressed in the title". The subject of the amendment relates to the storage of royalty oil and gas, whereas, the title addresses the disposal of royalty oil and gas. Storage is not a disposal. Storage relates to the safekeeping of one's goods and not the consumption or sale. O'Niel v. Buffalo F. Ins. Co., 3 N.Y. 122. Disposal pertains to the sale, pledge, giving away, use, consumption or any other disposition of a thing. C.B. Norton Jewelry Co. v. Maddock, 115 Kan. 108, 222 P.113, 114.

Because storage of royalty oil and gas and the disposal of royalty oil and gas are two distinct subjects, I conclude that the subject of the amendment to CSHB 103(Fin) is not expressed in the title of CSHB 103(Fin), and therefore is in violation of Article II, sec. 13 of the Alaska Constitution.

RJM:ojb
J14/108

Possible Amendment to AS 38.05.183(d)

(d) Except for sales of one year or less to relieve storage or market conditions, oil or gas taken in-kind by the state as its royalty share may not be sold or otherwise disposed of for export from the state until the commissioner determines that the royalty in-kind oil or gas is surplus to the present and projected intrastate domestic and industrial needs. The commissioner shall make public, in writing, the specific findings and reasons on which ~~his~~^{THE} determination is based and shall, within 10 days of the convening of a regular session of the legislature, submit a report showing the immediate and long-range domestic and industrial needs of the state for oil and gas and an analysis of how these needs are to be met.



Official Business

Alaska State Legislature

House

Pouch V
State Capitol
Juneau, Alaska 99811

MEMORANDUM

DATE: February 28, 1985

TO: Representative Davis
Representative Cotten
Representative Shultz
Representative Adams

FROM: Representative Marco Pignalberi *MAR (mk)*

SUBJECT: CSHB 103

I didn't have time to do homework on HB103 while it was in Oil & Gas Committee. However, subsequent review indicates to me that it has a serious flaw. Namely, that there is no limit on the frequency or duration of the renewals and continuations that DNR may award to a "short-term royalty oil contract holder.

I'd appreciate it if you would address this in your committee.

CSHB 103
ANALYSIS
REPRESENTATIVE MARCO A. PIGNALBERI

SECTION 1

- AS 38.05.183 (a) Oil and gas royalties shall be by competitive bid.
- (c) If oil and gas royalty sale is by other than competitive bid, then Commissioner shall make public, written justification.
- (e) If oil and gas royalty sale is other than competitive bid, Commissioner shall award to buyer who proposes maximum benefits to state.

HB103 would add new section, (g), as follows:

- (g) AS 38.05.035(e) does not apply to a sale of oil and gas under this section.

AS 38.05.035(e) Director may approve contracts for sale of land and resources with consent of Commissioner.

Analysis: This is a housekeeping amendment. It is not clear that 38.05.035(e) applies to royalty oil and gas. Its thrust is definitely land sales. In order to eliminate confusion, this section specifically excludes oil & gas.

SECTION 2

- AS 38.06.055 (a) Requires legislative approval for royalty oil and gas contracts by enactment of legislation.
- (b) Exceptions to legislative approval
- (1) if sale is less than one year to relieve storage or market conditions
- (2) "small amounts"
- AS 38.06.055 (c) Present language says contracts that are exempt from legislative approval because they're for less than one year to relieve storage or market conditions, may not be continued or renewed beyond one year.

The proposed AS 38.06.055 (c) would allow a competitive bid sale that is less than one year to be continued or renewed without legislative approval. But it would not allow a negotiated sale to be renewed without legislative approval.

Analysis: Summarily, the protection of the public interest afforded by legislative review and approval is replaced by competitive bid procedures. However, the proposed change in AS 38.06.055 (c) does not limit the frequency or duration of renewals and continuances that may be made without the legislature's approval.

Conclusion: This amendment may have the effect of circumventing the legislature by transitioning all short-term, "market conditions" contracts to long-term contracts. I believe this flaw is serious, especially in light of DNR's position that legislative approval is an unconstitutional burden.

In addition, I suggest you delete the phrase beginning on line 17 and ending on line 18 that says [to provide relief for market or storage conditions].



Official Business

Alaska State Legislature

House

Pouch V
State Capitol
Juneau, Alaska 99811

February 28, 1985

Kay Brown, Director
Division of Oil and Gas
Department of Natural Resources
Pouch 7-034
Anchorage, Alaska 99510

Dear Kay:

During your testimony on HB 103, before the House Oil and Gas Committee, it was not made clear what time savings would accrue or deadline conflicts would be averted with enactment of the bill. Would you please explicate these matters in writing and copy the members shown below.

Thank you.

Yours truly,

Marco A. Pignalberi
State Representative

MAP:mk

cc: Representative Mike Davis
Representative Dick Shultz
Representative Al Adams
Representative Terry Martin

STATE OF ALASKA

DEPARTMENT OF NATURAL RESOURCES

BILL SHEFFIELD, GOVERNOR

POUCH 7-034
ANCHORAGE, ALASKA 99510

DIVISION OF OIL AND GAS

March 5, 1985

The Honorable Al Adams, Chairman
House Finance Committee
Alaska State House of Representatives
Juneau, AK 99811

Dear Representative Adams:

CSHB 103 (Oil and Gas), which relates to prerequisites for disposal of royalty oil and gas, is scheduled for a hearing tomorrow in your committee.

At the House Resources Committee hearing on February 25, 1985, the question was raised as to whether the proposed amendment in Section 2 of the bill would allow a competitive bid sale of one year or less to be continued or renewed beyond one year without legislative approval and without going to competitive bid.

While the language could possibly be interpreted to allow that outcome, I am informed by the Attorney General's Office that the case law on competitive bidding would preclude it, since a competitively-bid contract cannot be materially amended after it is awarded.

Nevertheless, we believe the bill could be improved and an unintended construction could be prevented by adoption of the following language for Section 2 of the bill (substitute beginning on line 14):

*Sec. 2. AS 38.06.055(c) is amended to read:

(c) A sale, exchange, or other disposition of oil or gas [MADE] under (b)(1) of this section may not be continued after the end of one year or renewed with the same party [TO PROVIDE RELIEF FOR MARKET OR STORAGE CONDITIONS] without the prior approval of the legislature under (a) of this section. This subsection does not apply to contracts awarded to the same party in sequential competitive sales of oil or gas under (b)(1) of this section.

Thank you for your consideration.

Sincerely,


Kay Brown
Director

cc: House Finance Committee Members
Commissioner Esther C. Wunnicke

Mike --

You asked for comments regarding Marco's analysis of HB 103:

As you know from conversations we had prior to the bill's introduction, there is no limit to the number of times that a company would be eligible to receive consecutive short-term competitive bid contracts under HB 103. You will recall that we discussed the possibility of proposing amendments that would either limit the number of times that such a contract could be renewed, or that would extend the maximum duration of a short-term contract while disallowing renewal.

Marco is also correct in noting that 'NR regards the need for legislative approval of long-term royalty oil contracts as unconstitutional, as this was directly stated in the Governor's letter of transmittal. We are also aware from repeated conversations with Kay Brown that 'NR is a proponent of competitive bid sales and, in large degree, an opponent of negotiated sales.

As was discussed in committee, language allowing for the sale of royalty oil to meet market or storage conditions does provide an effective means of circumventing statutory requirements for legislative approval of long-term sales. Although definitions of market and storage conditions are present in 11 AAC 03.080 and .090, these terms are not defined in the statutes themselves. 'NR has pointed out that this lack of definition presents problems from their perspective as well.

Please advise as to what you would like done at this point.

Jim

0:9

Introduced: 1/23/85
Referred: House Special Committee on
Oil & Gas, Resources and Finance

1 IN THE HOUSE

BY THE RULES COMMITTEE BY
REQUEST OF THE GOVERNOR

2

HOUSE BILL NO. 103

3

IN THE LEGISLATURE OF THE STATE OF ALASKA

4

FOURTEENTH LEGISLATURE - FIRST SESSION

5

A BILL

6

For an Act entitled: "An Act relating to royalty oil; and providing for an
effective date."

7

8

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

9

* Section 1. AS 38.05.183 is amended by adding a new subsection to

10 read:

11

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

12

13

* Sec. 2. AS 38.06.055(c) is amended to read:

14

(c) A sale, exchange, or other disposition of oil or gas, ~~other~~

15

~~than by competitive bid~~, made under (b)(1) of this section may not be

16

continued after the end of one year or renewed with the same party ^① to

17

provide relief for market or storage conditions without the prior

18

approval of the legislature under (a) of this section. ^②

19

* Sec. 3. This Act takes effect immediately in accordance with AS 01.-

20

10.070(c).

① add ", other than by competitive bid,"

OR

② add a new sentence "This subsection does not apply to contracts awarded for the same party in sequential competitive sales of oil or gas under (b) (1) of this section."

1 IN THE HOUSE

BY THE FINANCE COMMITTEE

2 CS FOR HOUSE BILL NO. 103 (Finance)

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 FOURTEENTH LEGISLATURE - FIRST SESSION

5 A BILL

6 For an Act entitled: "An Act relating to prerequisites for the disposal of
7 royalty oil and gas; and providing for an effective
8 date."

9 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

10 * Section 1. AS 38.05.183 is amended by adding a new subsection to
11 read:

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

14 * Sec. 2. AS 38.06.055(c) is amended to read:

15 (c) A sale, exchange, or other disposition of oil or gas [MADE]
16 under (b)(1) of this section may not be continued after the end of one
17 year or renewed with the same party [TO PROVIDE RELIEF FOR MARKET OR
18 STORAGE CONDITIONS] without the prior approval of the legislature
19 under (a) of this section. This subsection does not apply to a se-
20 quential competitively bid sale of oil or gas made with the same party
21 under (b)(1) of this section.

22 * Sec. 3. This Act takes effect immediately in accordance with AS 01.-
23 10.070(c).

A M E N D M E N T

Offered in the SENATE

TO: CSHB 103 (Finance)

Page 1, after line 9 insert a new bill section to read:

"* Section 1. AS 38.05.180(1) is amended to read:

(1) Subject to the provisions of AS 31.05, the commissioner has discretion to enter into an agreement whereby, with the consent of the lessee, the state's royalty share of oil and gas production may be stored or retained in storage by the lessee, or the commissioner may enter into an agreement with one or more of the affected field lease holders to trade current royalty production from a field for a like amount, kind, and quality of future production. An agreement for storage may be made only [,] on the condition that the state receives back its stored [OR TRADED] royalty share during the first half of the estimated field life or no later than 15 years after start of production, whichever is sooner. An agreement to trade all or part of current royalty production for future production may be made only if the commissioner makes a written finding that the state will receive back its traded royalty share before 80 percent of the estimated field reserves are depleted, considering engineering constraints, whether reserves from other producing fields are pledged to protect the traded royalty share, and other relevant factors. An agreement to trade current production for future production entered into under this subsection must contain a provision holding the lessee harmless in the

event that, without the fault of the lessee, the state is unable to receive its traded royalty share because of unanticipated depletion of the field and any other pledged producing fields."

Page 1, line 10, delete "* Section 1." and insert "* Sec. 2."

Renumber remaining bill section accordingly.

J

A M E N D M E N T

Offered in the SENATE

TO: CSHB 103 (Finance)

Page 1, after line 9 insert a new bill section to read:

"* Section 1. AS 38.05.180(1) is amended to read:

(1) Subject to the provisions of AS 31.05, the commissioner has discretion to enter into an agreement whereby, with the consent of the lessee, all or part of the state's royalty share of oil and gas production may be stored or retained in storage by the lessee, or the commissioner may enter into an agreement with one or more of the affected field lease holders to trade all or part of current royalty production from a field for a like amount, kind, and quality of future production, if the commissioner makes a written finding [ON THE CONDITION] that the state receives back its stored or traded royalty share before 80 percent of the estimated field life is depleted, considering engineering constraints, whether reserves from other producing fields are pledged to protect the stored or traded royalty share, and other relevant factors [DURING THE FIRST HALF OF THE ESTIMATED FIELD LIFE OR NO LATER THAN 15 YEARS AFTER START OF PRODUCTION, WHICHEVER IS SOONER]."

Page 1, line 10, delete "* Section 1." and insert "* Sec. 2."

Renumber remaining bill section accordingly.

20090V Perdue

MEMORANDUM

DEPARTMENT OF NATURAL RESOURCES
DIVISION OF OIL AND GAS

TO: Senator Jalmar Karttula

State of Alaska

DATE: May 9, 1989

FILE NO:

TELEPHONE NO: 276-2653

FROM: Kay Brown, Director

SUBJECT: Underlift Amendment

Here is some additional background for your information.

	<u>Kenai gas field</u>	<u>Beluga gas field</u>
Date of first production	1962	1968
Years produced	23	17
Total recoverable gas	2410 BCF	985 BCF
Total production to date	1560 BCF	185 BCF
Percent of total recoverable gas produced to date	65	19
Average annual production	108 BCF	19 BCF
Years of production remaining (at current rates)	8	42
Year that 80% of recoverable gas will have been produced (at current rates)	1989	2016

1637K

Handle ASAP. per Comments

DELIVER TO: <u>Ned Farquhar</u>	LOCATION: <u>465-2400</u>
FROM: <u>Kay Brown</u>	LOCATION: <u>265-4241</u>
TELEPHONE/TELECOPIER # _____	TOTAL NUMBER OF PAGES: <u>4</u>
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NAME AND PHONE NUMBER: <u>265-4244 - 1327</u>	

STATE OF ALASKA



POUCH V
JUNEAU, ALASKA 99811
(907) 465-4941

HOUSE SPECIAL COMMITTEE ON OIL AND GAS

MEMORANDUM

To: Legislative Drafting
From: Rep. Mike Davis, Chairman
Date: Feb. 14, 1985
Re: CSHB 103

On Feb. 13 the House Special Committee on Oil and Gas passed out CSHB 103 with the following amendment:

The title has been changed to "An Act relating to prerequisites for the disposal of royalty oil and gas; and providing for an effective date."

Please send a final draft of CSHB 103 incorporating this amendment to my office.

Thank you for your assistance.

STATE OF ALASKA

DEPARTMENT OF NATURAL RESOURCES

OFFICE OF THE COMMISSIONER

BILL SHEFFIELD, GOVERNOR 

POUCH M
JUNEAU, ALASKA 99811
PHONE: 907-485-2400

May 8, 1985

The Honorable Mike Davis
Alaska State House
Pouch V
Juneau, AK 99811

Dear Representative Davis:

The Department of Natural Resources has proposed an amendment to AS 38.05.180(1) that I believe deserves your support. The proposed amendment is needed to give the State more flexibility to resolve a dispute over the value of Cook Inlet royalty gas.

The Department of Natural Resources recently informed Cook Inlet gas lessees that it would no longer accept long-term contract prices as the value for royalty gas taken in-value. Under the leases, the State is entitled to get current market value for the royalties. The department took the action to fulfill its responsibility under the law and the leases to obtain full value for the State's resources.

One consequence of the lease enforcement action is that consumer prices for electricity and gas in Southcentral will go up by a small amount (no more than 4 percent).

One lessee -- ARCO -- recently sued the State over the action, and the other lessees have indicated they also will fight the action in court.

A representative of one of the Beluga gas field lessees suggested a few days ago that the State consider an "underlift" of its royalty share as a possible way to resolve the dispute. Under this approach, the State's gas could be kept in the ground and recovered at a later date.

The current statute authorizes trades of current royalty production for future production, but provides that the traded royalty share must be recovered during the first half of the field life or within 15 years from the start of production, whichever is sooner.

Both the Kenai gas field and the Beluga gas field are more than 15 years into production. The Beluga field, which began production in 1968, has about 80 percent of its recoverable reserves remaining to be produced after 17 years of production. The Kenai field, which began production in 1962, has about 34 percent of its recoverable reserves remaining, but the State's effective royalty share is only about 2 percent in that field. To ensure that the State receives its share before the end of the field life, gas from other nearby fields could be pledged as a backup mechanism.

The possibility of arranging a trade of current production for future production holds promise as a way to resolve the current dispute without compromising the State's position in other royalty litigation or the lease enforcement process. However, we cannot pursue this possibility unless the statute is amended.

We think the underlift approach could be attractive to all parties because:

- Consumer electric and gas rate increases that would otherwise occur could be avoided (or at least postponed for perhaps 5-7 years);
- The State would be banking the resources until a local or foreign export market develops for the gas;
- Lengthy litigation could be avoided;
- All future options for disposition of the gas would remain open;
- The Legislature would have more time to consider the issue of using royalties to provide consumer energy subsidies;
- If the Legislature does desire to subsidize Southcentral utility rates through in-kind royalty sales in the future, more gas would be available to offset large price increases that will occur in the early 1990s when long-term contracts expire.

The expected fiscal impact of underlifting in the Beluga and Kenai fields, if agreement could be reached by the State, lessees, and utilities to allow that arrangement, would be a loss of about \$1.5 million in FY 86.

May 8, 1985

The State's options for disposition of the gas are limited at this time. Immediate local needs appear to be satisfied by existing contracts between the utilities and gas producers. Certain contractual provisions in those contracts may make in-kind royalty gas sales unattractive to the utilities at this time. For example, the Chugach Electric contract for Beluga Gas contains a "most favored nation" provision which would jeopardize the utility's favorable long-term contract price if it purchases gas from that field at a higher price. Enstar also would have no incentive to purchase royalty gas from the Kenai field because any such purchase would reduce the volume of gas Enstar is entitled to receive under its 61¢ long-term contract with Union and Marathon.

It is our expectation that the amendment will be proposed during Senate floor debate on CSHB 103(Finance). In addition to the underlift amendment, I urge your support of that bill. The bill would remove possible legal impediments to renewing with the same purchaser short-term, competitively bid royalty oil contracts.

If you have any questions, please call.

Sincerely,



Esther C. Wunnicke
Commissioner

Attachment

May 8, 1985

DEPARTMENT OF NATURAL RESOURCES

Proposed amendment to AS 38.05.180(1).

(1) Subject to the provisions of AS 31.05, the commissioner has discretion to enter into an agreement whereby, with the consent of the lessee, all or part of the state's royalty share of oil and gas production may be stored or retained in storage by the lessee, or the commissioner may enter into an agreement with one or more of the affected field lease holders to trade all or part of current royalty production from a field for a like amount, kind, and quality of future production, [ON THE CONDITION] if the commissioner makes a written finding that the state will receive[S] back its stored or traded royalty share [DURING THE FIRST HALF OF THE ESTIMATED FIELD LIFE OR NO LATER THAN 15 YEARS AFTER THE START OF PRODUCTION, WHICHEVER IS SOONER.] before the end of the estimated field life, considering engineering constraints, whether reserves from other fields are pledged to protect the royalty amount, and other relevant factors.

BILL SHEFFIELD
GOVERNOR



STATE OF ALASKA
OFFICE OF THE GOVERNOR
JUNEAU

HB103

January 23, 1985

The Honorable Ben Grussendorf
Speaker of the House
Alaska State Legislature
Pouch V
Juneau, AK 99811

Dear Representative Grussendorf:

Under the authority of art. III, sec. 18, of the Alaska Constitution, I am transmitting a bill relating to royalty oil. The bill would (1) clarify and streamline procedural requirements for royalty oil and gas sales by expressly providing that the best-interest finding set out in AS 38.05.035(e) does not apply to those sales; and (2) enable the Department of Natural Resources to establish a regular program of short-term competitive royalty oil sales.

It is unclear whether AS 38.05.035(e) applies to royalty oil and gas sales. Royalty oil and gas sales have detailed finding and notice requirements set out in AS 38.05.182, 38.05.183, and AS 38.06, and are expressly committed to commissioner actions. AS 38.05.035(e), on the other hand, is essentially duplicative of those other processes and concerns actions taken by the director of the division of lands. Although we believe that the provisions of AS 38.05.035(e) are not presently applicable to oil and gas sales, such confusion does cast a cloud over royalty oil sales (particularly those that are entered into because of an emergency situation). The amendment in sec. 1 of the bill resolves the issue.

The second change, in sec. 2 of the bill, would allow competitive royalty oil sales for terms of less than one year to be conducted without legislative approval of those sales. To await legislative approval under a competitive bid situation for contracts of one year or less would defeat the entire purpose of that type of short-term competitive sales. Under the present statutory scheme, however, there is a serious question as to whether a party who gained royalty oil under one competitive sale could re-bid in a subsequent royalty oil sale if the combination of the two sales would lead to that particular buyer receiving oil for more than a one year period. Although it has been the

consistent position of this and previous administrations that the requirement of legislative approval is unconstitutional, administrations have always, as a matter of comity, respected the legislature's desire to be consulted in long-term or negotiated royalty oil contracts. Further, the presence of the statute, whether or not constitutional, would cast a cloud on any sale. Thus we believe that a clarification to allow short-term competitive royalty oil sales would be in the best interests of all.

Sincerely,

A handwritten signature in cursive script, appearing to read "Bill Sheffield".

Bill Sheffield
Governor

**STATE OF ALASKA 1985 LEGISLATIVE SESSION
FISCAL NOTE**

Revision Date: _____

REQUEST

Bill/Resolution No.: HB 103
Title: An Act relating to royalty

FISCAL DETAIL

Agency Affected: Natural Resources
Program Category Affected: NRMEC

Sponsor: _____
Requestor: _____
Date of Request: _____

BRU, Program or Subprogram(s) Affected: _____
Minerals and Energy Management

EXPENDITURES/REVENUES: (Thousands of Dollars)

	FY 85	FY 86	FY 87	FY 88	FY 89	FY 90
OPERATING						
100 PERSONAL SERVICES						
200 TRAVEL						
300 CONTRACTUAL						
400 SUPPLIES						
500 EQUIPMENT						
600 LAND & STRUCTURES						
700 GRANTS, CLAIMS						
800 MISCELLANEOUS						
TOTAL OPERATING	0	0	0	0	0	0

CAPITAL						
----------------	--	--	--	--	--	--

REVENUE						
----------------	--	--	--	--	--	--

FUNDING: (Thousands of Dollars)

GENERAL FUND						
FEDERAL FUNDS						
OTHER						
TOTAL						

POSITIONS:

FULL-TIME						
PART-TIME						
TEMPORARY						

ANALYSIS: Attach a separate page if necessary

No fiscal impact.

Prepared By: Kay Brown Phone: 265-4241
Division: Oil and Gas Date: December 7, 1984

Approved by Commissioner: Walter D. Amundson, Deputy Date: December 10, 1984
Agency: Natural Resources

Distribution (by Agency preparing fiscal note):

- Legislative Finance
- Legislative Sponsor
- Requestor
- Office of Management and Budget
- Impacted Agency(ies)

7/1/84

best interests determination described in 11 AAC 03.010(d). (Eff. 12/12/80, Reg. 76)

Authority: AS 38.05.020
AS 38.05.183
AS 38.06.070

11 AAC 03.070. REJECTION OF PROPOSALS. (a) If the commissioner has either (1) solicited proposals for the noncompetitive sale of royalty oil, gas, or gas liquids, (2) issued a written determination to dispose of royalty oil, gas, or gas liquids by a method other than by competitive bid, or (3) issued written procedures for the noncompetitive disposal of royalty oil, gas, or gas liquids as described in 11 AAC 03.050, and the commissioner proposes to reject any proposal or application received as a result of the solicitation, determination, or written procedures, the commissioner will notify the Alaska Royalty Oil and Gas Development Advisory Board in writing before rejecting the proposal or application.

(b) The notification required by (a) of this section will consist of a list of the names of the prospective buyers whose proposals are rejected along with their proposals and any correspondence received from the prospective buyers.

(c) The commissioner will, in his or her discretion, reject unsolicited or uninvited proposals for the noncompetitive disposal of royalty oil, gas, or gas liquids without notifying the Alaska Royalty Oil and Gas Development Advisory Board. (Eff. 12/12/80, Reg. 76; am 8/8/84, Reg. 91)

Authority: AS 38.05.020
AS 38.06.050

11 AAC 03.080. STORAGE CONDITIONS. The commissioner disposes of royalty oil, gas, or gas liquids to relieve storage conditions when

(1) the royalty oil, gas, or gas liquids have either been noticed for a taking in-kind or are being taken in-kind or are being taken in-kind by the state; and

(2) the disposition planned for the oil, gas, or gas liquids at the time of the notice to take the oil, gas, or gas liquids in-kind can no longer be effectuated for any reason, or the disposition is

no longer in the best interests of the state. (Eff. 12/12/80, Reg. 76; am 8/8/84, Reg. 91)

Authority: AS 38.05.020
AS 38.05.183
AS 38.06.055

11 AAC 03.090. MARKET CONDITIONS. The commissioner disposes of royalty oil, gas, or gas liquids to relieve market conditions when

(1) in a noncompetitive disposition of royalty oil, gas, or gas liquids the price to be received under the noncompetitive disposition is higher than the amount being received by the state, either in-value or in-kind, at the time of the disposition and the commissioner estimates that the sale price will be higher than the in-value amount throughout the term of the contract for disposition;

(2) in a disposition by competitive bid the commissioner determines, at the time of issuance of the invitation to bid, that there is a substantial probability that the state will receive more than the in-value price as a result of the disposition by competitive bid;

(3) the royalty oil, gas, or gas liquids disposed of will be used to meet in-state needs for crude oil, gas, or gas liquids or petroleum products and the sale price of that royalty oil, gas, or gas liquids is at least equal to the in-value amount which would have been received by the state during the same period; or

(4) there is or will be an emergency in-state need for crude oil, gas, or gas liquids or petroleum products, which could be alleviated by the sale of the royalty oil, gas, or gas liquids. (Eff. 12/12/80, Reg. 76; am 8/8/84, Reg. 91)

Authority: AS 38.05.020
AS 38.05.183
AS 38.06.055

11 AAC 03.091. PROVISIONS APPLICABLE TO ROYALTY CONTRACTS. (a) Within 10 days after receiving written notice from a royalty purchaser of its intent to renegotiate price, as provided for by the terms of that purchaser's state royalty contract, or within 10 days after giving a royalty purchaser written notice of the state's intent to renegotiate price, as provided for by the terms of that purchaser's state royalty contract,

or before the adoption of any material amendment to a royalty contract which appreciably reduces the consideration received by the state, the commissioner will publish notice of the intent to renegotiate price or amend the contract in a newspaper of general statewide circulation. In addition, the commissioner will, in his or her discretion, publish notice by radio, television, or other electronic media. The notice will include

(1) a summary of information pertinent to the royalty contract, including quantity, current price, and termination date;

(2) a statement indicating where copies of the contract may be obtained; and

(3) a statement that any person may file written comments on the notice with the commissioner within 30 days after publication of the notice.

(b) In establishing or renegotiating the price of a royalty contract, the commissioner will obtain a price at least equal to the price that would have been received had the oil, gas, or gas liquids been taken in-value, plus field costs incurred by the royalty share, unless the commissioner determines that a lower price for the royalty gas would best serve the state's interests.

(c) The commissioner will submit to the legislature for approval any material amendment to a royalty contract which appreciably reduces the consideration received by the state. (Eff. 8/8/84, Reg. 91)

Authority: AS 38.05.020
AS 38.05.182
AS 38.05.183

11 AAC 03.100. DISPOSITION BY COMPETITIVE BID. (a) A disposition of royalty oil, gas, or gas liquids by competitive bid will, in the commissioner's discretion, be made without a written determination by the commissioner that the disposition of royalty oil, gas, or gas liquids by competitive bidding is in the best interests of the state.

(b) A disposition of royalty oil, gas or gas liquids by competitive bid will, in the commissioner's discretion, be made by the commissioner without notice to the Alaska Roy-

alty Oil and Gas Development Advisory Board; however, the commissioner will follow the procedures set out in 11 AAC 03.210 and 11 AAC 03.240. (Eff. 12/12/80, Reg. 76; am 8/8/84, Reg. 91)

Authority: AS 38.05.020
AS 38.05.183

11 AAC 03.110. SEALED BIDS. A disposition of royalty oil, gas, or gas liquids by competitive bid will be by sealed bid. The bids must be addressed to the commissioner and must be delivered in the manner, to the place, and by the date and time specified in the invitation to bid. Bids will be opened in public at the date, time, and place specified in the invitation to bid, unless the commissioner designates a later time for opening. (Eff. 12/12/80, Reg. 76; am 8/8/84, Reg. 91)

Authority: AS 38.05.020
AS 38.05.183

11 AAC 03.120. INVITATION TO BID. A disposition of royalty oil, gas, or gas liquids by competitive bid will be initiated by the commissioner by issuance of an invitation to bid. The invitation to bid will specify the quantity of oil, gas, or gas liquids to be sold, the term of disposition, the point of delivery, and any other terms and conditions of the disposition considered necessary by the commissioner. The commissioner will, in his or her discretion, include a form contract in the invitation rather than specifying terms and conditions. The invitation will specify qualifications of bidders and, if a determination of the qualification of a bidder by the commissioner is required, an explanation of the procedure for qualification. If priorities among bidders are to be assigned, the invitation will include an explanation of the procedure for obtaining a priority designation. The invitation will specify where, when, and how bids may be submitted to the commissioner and will specify the bond or other security which must accompany the bid. The invitation will specify the date, time, and place of bid opening, and the procedures under which the royalty oil will be awarded and contracts for disposition executed. (Eff. 12/12/80, Reg. 76; am 8/8/84, Reg. 91)

Authority: AS 38.05.020
AS 38.05.183

11 AAC 03.130. SECURITY. The commissioner may require that security, which in his

State of Alaska
Department of Natural Resources
Supplemental Findings
Competitive Royalty Oil Sale
(Prudhoe Bay and Kuparuk River Units)

November 28, 1984

Supplemental Findings
Competitive Royalty Oil Sale
(Prudhoe Bay and Kuparuk River Units)

AS 38.05.183(a) states that oil and gas taken in-kind as the state's royalty share of production may not be sold or otherwise disposed of for export from the state until the Commissioner of Natural Resources determines that the royalty in-kind oil or gas is surplus to the present and projected intrastate domestic and industrial needs for oil and gas. I find that the 90,000 bpd scheduled for competitive sale on December 11, 1984 is surplus to present and projected intrastate domestic and industrial needs for oil.

AS 38.05.183 also requires the Commissioner to submit an annual report to the state legislature "showing the immediate and long-term domestic and industrial needs of the state for oil and gas and an analysis of how these needs are to be met." The Department of Natural Resources, Division of Oil & Gas (the Department) complies with that requirement by preparing a document, published each January, entitled Historical and Projected Oil and Gas Consumption (also called the Supply/Demand study). The January 1984 Supply/Demand study concluded, as it has in previous years, that in-state supplies of both oil and gas far exceeded the immediate and long-term domestic and industrial needs of the state for oil and gas.

Due to the absence of any new information concerning the immediate and long-term domestic and industrial needs of the state for oil and gas, the Department again concluded, both in the Preliminary Findings and Determination to Negotiate Backup Royalty Oil Contract(s) and Conduct a Competitive Royalty Oil Sale (July 12, 1984) and the Final Findings and Determination to Conduct a Competitive Royalty Oil Sale for In-Kind Oil from the Prudhoe Bay and Kuparuk River Units (October 10, 1984), that the 90,000 bpd of state royalty oil to be sold competitively on December 11, 1984 is surplus to in-state needs. Consequently, upon the publication of the Preliminary Finding and execution of contracts with backup purchasers, the state gave a six-month notice to the North Slope producers of its intent to take 90,000 bpd of royalty oil in-kind (as provided by procedures in the Prudhoe Bay and Kuparuk River Unit Agreements).

The Department's conclusion was and is based in part on the interpretation of AS 38.05.183 stated in each Supply/Demand study since 1982. In that year, the study first gave specific definitions to certain phrases in that statute. Since 1982, the first chapter of every Supply/Demand study has contained a list of possible definitions for some of the imprecise clauses of AS 38.05.183, such as "how these needs are to be met". The Supply/Demand study definition of that phrase specifies the Department's long-standing position that the state's present and projected intrastate domestic and industrial needs for oil and gas may be met from a variety of sources, including state royalty oil. See 1984 Supply/Demand study page 1.7.

The intent of the statute should not be regarded as complete state self-sufficiency in refined products from state royalty oil. Rather, the Department believes the legislature was aiming at ensuring adequate overall oil and gas supplies for the state. The 1984 Supply/Demand study states that, "Under reasonable assumptions about recoverable reserves and Alaskan consumption, the current inventory of both oil and gas is more than sufficient to meet the presently identifiable needs of Alaskans for the next 15 years." Presently, the Department of Revenue's most recent crude oil price forecasts remain conservative due to the continued surplus in world supplies. While unfavorable from a revenue standpoint, that surplus will likely translate into dampened crude oil prices for Alaska consumers and industrial users. Only if the cost of imported products were significantly above the cost of products which could be refined in Alaska (e.g. when oil is not available to local refiners at the market price), or if Alaska users were suffering from an absolute shortfall in petroleum products, would the Department not consider the royalty oil to be sold at the competitive sale as "surplus" to present and projected in-state needs. Neither of these was found to be the case.

The Department's view of the purpose of AS 38.05.183 stems first from the atmosphere of absolute shortage, particularly in motor fuels, which prevailed at the time the statute was written. The statute was adopted in 1974, when the worldwide oil crisis and the imposition of federal oil contract controls raised the spectre of product shortages in Alaska despite North Slope crude oil production. The Department's view stems second from the apparent paradox of continued imports into regions such as Southeast Alaska, where the landed cost of such imports from Puget Sound undercuts the cost of delivered refined products to Southeast from Railbelt refiners. Under the most constrained interpretation of the statute, the Department would be obliged to promote in-state refining with royalty oil for the sake of absolute self-sufficiency, even when this resulted in higher prices for Alaskans. Clearly, this was not the intent of the statute. Intrastate needs for oil and gas are presently being met from a variety of sources, including state royalty oil. As charged, the 1984 Supply/Demand study identifies those sources and discusses how in-state needs are to be met, given the total supply of hydrocarbons within the state. In terms of total present and projected demand vs. total present and projected supply, intrastate refined product needs can be met with ease by the unprecedented production of crude oil from the North Slope, which is available to any purchaser willing to meet the market clearing price for that oil. For these reasons, the Department determined in the 1984 Supply/Demand study that the state enjoys a surplus of hydrocarbons relative to present and foreseeable demand.

Even if AS 38.05.183(d) were interpreted to require all intrastate needs to be satisfied by royalty oil before export could occur, I would find that the competitive sale amounts are surplus to present and projected intrastate domestic and on industrial needs for two reasons. First, persons who have a demand for oil as a result of current in-state processing or supply activities are granted priority rights to purchase royalty oil at the competitive sale. Second, during the term of the competitive sale contracts, royalty oil will remain in-value and will be available for disposition in-state.

The Department has provided for satisfaction of demand for royalty oil on the part of in-state refiners and in-state suppliers by giving them priority rights to purchase oil at the competitive sale. A priority will be offered to bidders which have sold an average of at least 5,000 bpd of refined petroleum products to distributors or consumers within the State of Alaska during the twelve-month period beginning June 1, 1983 and ending May 31, 1984, and which possess the ability to process crude oil into refined petroleum products at a processing facility owned by the bidder. Priority status will enable the in-state supplier to meet the highest winning bid in each of the three categories of royalty oil to be competitively sold. That right extends to the number of lots remaining in each category after the first round award of lot(s) to the highest winning bidder(s) in each category and priority bidders who have been posted as apparent high bidders. Consequently, in the first round of awards, priority bidders enjoy the possibility of receiving oil at the lowest price posted in each category. In addition, in-state suppliers are reasonably assured of receiving the desired volume of oil in the second round of awards, provided they are willing to meet the competitively established price. 11 AAC 03.250(5) states that:

"present or projected intrastate domestic and industrial needs" means in-state domestic and industrial demand at a competitive market price for the royalty oil, gas, or gas liquids. "Competitive market price" includes, but is not limited to, a price established by competitive bid.

Thus, in-state refiners and suppliers will have the first right to royalty crude at a competitive market price so that their supply is assured.

At the present time the state leaves approximately 104,735 bpd of royalty oil in-value with the North Slope lessees. The lessees export this oil from Alaska and tender the reported netback sale proceeds to the state. During the first six months of the term of the competitive sale contracts, April 1985 to September 1985, approximately 26,013 bpd of royalty oil will remain in-value. During the following six months of the term, October 1985 to March 1986, approximately 41,013 bpd of royalty oil will remain in-value. These amounts will remain available for disposition in-state if the Department finds the disposition(s) to be in the State's best interest. (If a contract currently being negotiated with Golden Valley Electric Association is approved, future amounts available for disposition would be reduced by 5,000 bpd.)

Several parties have recently expressed an interest in purchasing royalty oil from the State. Our conclusion that the competitive sale amounts are surplus to present and projected needs was drawn with the knowledge that all in-state refiners do not have 100% of their projected capacity supplied by state royalty oil. For example, as mentioned in the Preliminary Finding, the Department has conducted negotiations for the sale of royalty oil to MAPCO Inc. to fuel a proposed refinery expansion. The successful outcome of those negotiations is not, however, regarded by the Department as prerequisite to the possible export of the state's royalty oil in the planned competitive sale. First, MAPCO representatives indicated to the Department that the proposed refinery expansion may not be built, throwing the question of MAPCO's projected needs into doubt. Second, if MAPCO had a projected demand for royalty oil at a competitive price, it could have availed itself of its

opportunity to purchase oil at the competitive sale, as a priority bidder. Since it is a current in-state refiner, MAPCO would have been entitled to all the priority rights discussed above. Third, by virtue of its proximity to the Trans Alaska Pipeline (TAPS), MAPCO has unique opportunities to supply its refinery with North Slope oil. MAPCO currently receives 35,000 bpd of royalty oil directly from the State. MAPCO also receives 5,000 bpd of royalty oil through its agreement with another state royalty oil purchaser - the Golden Valley Electric Association. In addition, about 60% of the oil run through the MAPCO refinery is, with a minor quality penalty, reinjected into TAPS to re-emerge as whole oil at Valdez. That oil, which is the property of MAPCO, may be exchanged for more oil from the North Slope and again withdrawn from TAPS at Fairbanks. One of the several advantages that MAPCO enjoys with its state royalty oil contract, relative to other in-state refiners, is this absence of any state control over the return oil. MAPCO could also purchase oil directly from the North Slope lessees to satisfy any demand not met through the purchase and exchange of royalty oil. Finally, MAPCO's location on TAPS allows it to enter into "in-transit stop" arrangements in which MAPCO "borrows" oil from other TAPS shippers. The borrowed oil is processed in MAPCO's refinery with the full amount returned to the original shipper at Valdez through a combination of return oil and quality bank payments. This in-transit stop arrangement remains feasible so long as MAPCO's current contract which does not expire until 2003, remains in effect. The Department believes that any failure by MAPCO to secure oil through these possible sources of supply indicates that MAPCO's demand may exist only so long as it believes the State is willing to supply it with oil at a price below competitive prices. As explained above, 11 AAC 03.250(5) provides that projected needs means in-state demand at a competitive price.

Since the Department made its most recent finding of ample in-state hydrocarbon supplies, published in the Final Finding of October 10, 1984, several Alaskan parties in addition to MAPCO have expressed interest in purchasing royalty oil. Chevron has requested further volumes of royalty oil to meet a possible increase in "throughput" at its 18,000 bpd Nikiski Refinery. Chevron owns and exports 12,000 bpd of North Slope production in addition to the 18,000 bpd of royalty oil which it processes at Nikiski. New parties also propose to create additional new refineries in Alaska. Because these proposals were not known to the Department at the time of the most recent determination of an in-state hydrocarbon surplus, the state has decided to reduce the one-year term of those lots offered in the Kuparuk River oil category (category A) to six months. This will enable the state to have an additional 15,000 bpd of royalty oil available in the fall of 1985 for those who offer to purchase state royalty oil at terms which lead the Department to find that the disposition(s) would be in the state's best interest.

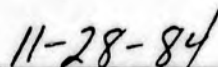
As stated, the impressive quantities of oil available within the state, which are the highest in the nation on a per-capita basis, diminish the likelihood of an actual "need" by these groups in the sense of supply availability. However, given the very recent nature of the new proposals received, the Department will further review their merits, as well as supply alternatives in addition to royalty oil. It has been the Division's experience that the term "need" is perceived differently by prospective in-state royalty oil

purchasers. Rather than the physical unavailability of oil due to world shortages or the unwillingness of North Slope producers to sell ANS crude at the market clearing price, prospective in-state royalty oil purchasers often view their feedstock needs in terms of the royalty oil price and terms they require for economic viability. While the Department recognizes that there are a host of oil-related economic activities which can be made viable should the state choose to undercut the market clearing price of Alaska North Slope oil for specific parties, this is not seen as the definition of "need" in AS 38.05.183, nor is it clearly in the State's best interest to do so.

Given the short-term nature of the proposed competitive sale, the consideration extended to in-state refiners and suppliers through the priority bidding system, the lack of demonstrated current need on the part of other potential in-state purchasers, and the amounts of oil remaining in-value available for disposition, I find pursuant to AS 38.05.183 that the royalty oil to be disposed of at the competitive sale is surplus to present and projected intrastate domestic and industrial needs.



Kay Brown, Director
Division of Oil & Gas
Department of Natural Resources


Date

HB 101

Section 2 of the bill makes the change in current law applicable to tax years beginning after December 31, 1984.

Sincerely,

/s/

Bill Sheffield
Governor"

HB 102

HOUSE BILL NO. 102 by the Rules Committee by request of the Governor, entitled:

"An Act relating to the Alaska Resources Corporation; and providing for an effective date."

was read the first time and referred to the House Special Committee on State Loans and the Finance Committee.

A zero fiscal note was attached. The Governor's transmittal letter, dated January 23, 1985, appears below:

"Dear Representative Grussendorf:

Under the authority of art. III, sec. 18, of the Alaska Constitution, I am transmitting a bill relating to the divestiture of assets and equity investments of the Alaska Resources Corporation (ARC).

Section 1 of the bill permits the board to dispose of assets, including those acquired through default or foreclosure, in any manner that serves the best interests of the state, including extended payments over time.

Section 2 of the bill permits the board to convert its equity investments into debt, which will then be treated in the same manner as the corporation's current outstanding loan portfolio.

This bill is necessary to permit the ARC board the flexibility necessary to wind up the corporation's affairs by 1989, in accordance with ch. 161, SLA 1984.

Sincerely,

/s/

Bill Sheffield
Governor"

HB 101

HOUSE BILL NO. 101 by the Rules Committee by request of the Governor, entitled:

"An Act relating to royalty oil; and providing for an effective date."

was read the first time and referred to the House Special Committee on Oil & Gas, the Resources and Finance Committees.

A zero fiscal note was attached. The Governor's transmittal letter, dated January 23, 1985, appears below:

"Dear Representative Grussendorf:

Under the authority of art. III, sec. 18, of the Alaska Constitution, I am transmitting a bill relating to royalty oil. The bill would (1) clarify and streamline procedural requirements for royalty oil and gas sales by expressly providing that the best-interest finding set out in AS 38.05.035(e) does not apply to those sales; and (2) enable the Department of Natural Resources to establish a regular program of short-term competitive royalty oil sales.

It is unclear whether AS 38.05.035(e) applies to royalty oil and gas sales. Royalty oil and gas sales have detailed finding and notice requirements set out in AS 38.05.182, 38.05.183, and AS 38.06, and are expressly committed to commissioner actions. AS 38.05.035(e), on the other hand, is essentially duplicative of those other processes and concerns actions taken by the director of the division of lands. Although we believe that the provisions of AS 38.05.035(e) are not presently applicable to oil and gas sales, such confusion does cast a cloud over royalty oil sales (particularly those that are entered into because of an emergency situation). The amendment in sec. 1 of the bill resolves the issue.

The second change, in sec. 2 of the bill, would allow competitive royalty oil sales for terms of less than one year to be conducted without legislative approval of those sales. To await legislative approval under a competitive bid situation for contracts of one year or less would defeat the entire purpose of that type of short-term competitive sales. Under the present statutory scheme, however, there is a serious question as to whether a party who gained royalty oil under one competitive sale could re-bid in a subsequent royalty oil sale if the combination of the two sales would lead to that particular buyer receiving oil for more than a one year period. Although it has been the consistent position of this and previous administrations that the requirement of legislative approval is unconstitutional, administrations have always, as a matter of comity, respected the legislature's desire to be consulted in long-term or negotiated royalty oil contracts. Further, the presence of the statute, whether or not constitutional, would cast a cloud on any sale.

HB 103

Thus we believe that a clarification to allow short-term competitive royalty oil sales would be in the best interests of all.

Sincerely,

/s/

Bill Sheffield
Governor"

HB 104

HOUSE BILL NO. 104 by the Rules Committee by request of the Governor, entitled:

"An Act relating to computation, forfeiture and restoration of statutory good time."

was read the first time and referred to the Health, Education & Social Services and Judiciary Committees.

A zero fiscal note with analysis was attached and appears in House Journal Supplement No. 7. The Governor's transmittal letter, dated January 23, 1985, appears below:

"Dear Representative Grussendorf:

Under the authority of art. III, sec. 18, of the Alaska Constitution, I am transmitting a bill relating to the computation, forfeiture, and restoration of statutory good time for state prisoners.

Good time accounting for state prisoners is currently being computed under three different systems dependent upon when a prisoner committed a criminal offense. Because of the complexities, an inordinate amount of staff time and frequent computational errors.

This bill will greatly simplify basic time accounting, and bring all Alaskan prisons under one time accounting system. For those prisoners already incarcerated on the date this bill becomes law, this bill will have the effect of changing the time accounting method from one of accruing good time at a set rate per month to one of a grant of good time in a block, the amount of which is dependent on the time remaining to be served on their sentences.

Additionally, although the primary purpose of the bill is to simplify the good time computation process, it will result in a minor reduction in the time prisoners will serve (one-twelfth of the sentence), if they observe all the rules of the institution while incarcerated.

HB 104

Finally, the bill will assist in the statewide uniform application of restoration of forfeited good time for prisoners who demonstrate good conduct during their incarceration.

Sincerely,

/s/

Bill Sheffield
Governor"

HB 105

HOUSE BILL NO. 105 by the Rules Committee by request of the Governor, entitled:

"An Act relating to the international airports revenue bonds authorization; and providing for an effective date."

was read the first time and referred to the Transportation and Finance Committees.

A fiscal note was attached and appears in House Journal Supplement No. 7. The Governor's transmittal letter, dated January 23, 1985, appears below:

"Dear Representative Grussendorf:

Under the authority of art. III, sec. 18, of the Alaska Constitution, I am transmitting a bill to raise from \$62,825,000 to \$86,525,000 the amount of international airports revenue bonds that may be issued by the state bond committee. This additional \$23,700,000 is intended to be used for the Anchorage International Airport Terminal Renovation, Phase II.

Sincerely,

/s/

Bill Sheffield
Governor"

HB 106

HOUSE BILL NO. 106 by the Rules Committee by request of the Governor, entitled:

"An Act making technical amendments relating to state taxation; and providing for an effective date."

was read the first time and referred to the Finance Committee.

not - taking adv. of a situation
storage - as per purchaser for oil

best interests determination described in 11 AAC 03.010(d). (Eff. 12/12/80, Reg. 76)

Authority: AS 38.05.020
AS 38.05.183
AS 38.06.070

11 AAC 03.070. REJECTION OF PROPOSALS. (a) If the commissioner has either (1) solicited proposals for the noncompetitive sale of royalty oil, gas, or gas liquids, (2) issued a written determination to dispose of royalty oil, gas, or gas liquids by a method other than by competitive bid, or (3) issued written procedures for the noncompetitive disposal of royalty oil, gas, or gas liquids as described in 11 AAC 03.050, and the commissioner proposes to reject any proposal or application received as a result of the solicitation, determination, or written procedures, the commissioner will notify the Alaska Royalty Oil and Gas Development Advisory Board in writing before rejecting the proposal or application.

(b) The notification required by (a) of this section will consist of a list of the names of the prospective buyers whose proposals are rejected along with their proposals and any correspondence received from the prospective buyers.

(c) The commissioner will, in his or her discretion, reject unsolicited or uninvited proposals for the noncompetitive disposal of royalty oil, gas, or gas liquids without notifying the Alaska Royalty Oil and Gas Development Advisory Board. (Eff. 12/12/80, Reg. 76; am 8/8/84, Reg. 91)

Authority: AS 38.05.020
AS 38.06.050

11 AAC 03.080. STORAGE CONDITIONS. The commissioner disposes of royalty oil, gas, or gas liquids to relieve storage conditions when

(1) the royalty oil, gas, or gas liquids have either been noticed for a taking in-kind or are being taken in-kind or are being taken in-kind by the state; and

(2) the disposition planned for the oil, gas, or gas liquids at the time of the notice to take the oil, gas, or gas liquids in-kind can no longer be effectuated for any reason, or the disposition is

no longer in the best interests of the state. (Eff. 12/12/80, Reg. 76; am 8/8/84, Reg. 91)

Authority: AS 38.05.020
AS 38.05.183
AS 38.06.055

11 AAC 03.090. MARKET CONDITIONS. The commissioner disposes of royalty oil, gas, or gas liquids to relieve market conditions when

(1) in a noncompetitive disposition of royalty oil, gas, or gas liquids the price to be received under the noncompetitive disposition is higher than the amount being received by the state, either in-value or in-kind, at the time of the disposition and the commissioner estimates that the sale price will be higher than the in-value amount throughout the term of the contract for disposition;

(2) in a disposition by competitive bid the commissioner determines, at the time of issuance of the invitation to bid, that there is a substantial probability that the state will receive more than the in-value price as a result of the disposition by competitive bid;

(3) the royalty oil, gas, or gas liquids disposed of will be used to meet in-state needs for crude oil, gas, or gas liquids or petroleum products and the sale price of that royalty oil, gas, or gas liquids is at least equal to the in-value amount which would have been received by the state during the same period; or

(4) there is or will be an emergency in-state need for crude oil, gas, or gas liquids or petroleum products, which could be alleviated by the sale of the royalty oil, gas, or gas liquids. (Eff. 12/12/80, Reg. 76; am 8/8/84, Reg. 91)

Authority: AS 38.05.020
AS 38.05.183
AS 38.06.055

11 AAC 03.091. PROVISIONS APPLICABLE TO ROYALTY CONTRACTS. (a) Within 10 days after receiving written notice from a royalty purchaser of its intent to renegotiate price, as provided for by the terms of that purchaser's state royalty contract, or within 10 days after giving a royalty purchaser written notice of the state's intent to renegotiate price, as provided for by the terms of that purchaser's state royalty contract,

or before the adoption of any material amendment to a royalty contract which appreciably reduces the consideration received by the state, the commissioner will publish notice of the intent to renegotiate price or amend the contract in a newspaper of general statewide circulation. In addition, the commissioner will, in his or her discretion, publish notice by radio, television, or other electronic media. The notice will include

(1) a summary of information pertinent to the royalty contract, including quantity, current price, and termination date;

(2) a statement indicating where copies of the contract may be obtained; and

(3) a statement that any person may file written comments on the notice with the commissioner within 30 days after publication of the notice.

(b) In establishing or renegotiating the price of a royalty contract, the commissioner will obtain a price at least equal to the price that would have been received had the oil, gas, or gas liquids been taken in-value, plus field costs incurred by the royalty share, unless the commissioner determines that a lower price for the royalty gas would best serve the state's interests.

(c) The commissioner will submit to the legislature for approval any material amendment to a royalty contract which appreciably reduces the consideration received by the state. (Eff. 8/8/84, Reg. 91)

Authority: AS 38.05.020
AS 38.05.182
AS 38.05.183

11 AAC 03.100. DISPOSITION BY COMPETITIVE BID. (a) A disposition of royalty oil, gas, or gas liquids by competitive bid will, in the commissioner's discretion, be made without a written determination by the commissioner that the disposition of royalty oil, gas, or gas liquids by competitive bidding is in the best interests of the state.

(b) A disposition of royalty oil, gas or gas liquids by competitive bid will, in the commissioner's discretion, be made by the commissioner without notice to the Alaska Roy-

alty Oil and Gas Development Advisory Board; however, the commissioner will follow the procedures set out in 11 AAC 03.210 and 11 AAC 03.240. (Eff. 12/12/80, Reg. 76; am 8/8/84, Reg. 91)

Authority: AS 38.05.020
AS 38.05.183

11 AAC 03.110. SEALED BIDS. A disposition of royalty oil, gas, or gas liquids by competitive bid will be by sealed bid. The bids must be addressed to the commissioner and must be delivered in the manner, to the place, and by the date and time specified in the invitation to bid. Bids will be opened in public at the date, time, and place specified in the invitation to bid, unless the commissioner designates a later time for opening. (Eff. 12/12/80, Reg. 76; am 8/8/84, Reg. 91)

Authority: AS 38.05.020
AS 38.05.183

11 AAC 03.120. INVITATION TO BID. A disposition of royalty oil, gas, or gas liquids by competitive bid will be initiated by the commissioner by issuance of an invitation to bid. The invitation to bid will specify the quantity of oil, gas, or gas liquids to be sold, the term of disposition, the point of delivery, and any other terms and conditions of the disposition considered necessary by the commissioner. The commissioner will, in his or her discretion, include a form contract in the invitation rather than specifying terms and conditions. The invitation will specify qualifications of bidders and, if a determination of the qualification of a bidder by the commissioner is required, an explanation of the procedure for qualification. If priorities among bidders are to be assigned, the invitation will include an explanation of the procedure for obtaining a priority designation. The invitation will specify where, when, and how bids may be submitted to the commissioner and will specify the bond or other security which must accompany the bid. The invitation will specify the date, time, and place of bid opening, and the procedures under which the royalty oil will be awarded and contracts for disposition executed. (Eff. 12/12/80, Reg. 76; am 8/8/84, Reg. 91)

Authority: AS 38.05.020
AS 38.05.183

11 AAC 03.130. SECURITY. The commissioner may require that security, which in his



Official Business

Alaska State Legislature

Senate Finance Committee

Pouch V
State Capitol
Juneau, Alaska 99811

JAN FAIKS
CO-CHAIRMAN

January 29, 1985

MEMORANDUM

TO: Representative Mike Davis
FROM: Senator Jan Faiks
SUBJECT: Special Committee on Oil and Gas

Thank you for putting me on your notification list with regard to upcoming meetings of the House Special Committee on Oil and Gas. I appreciate being kept informed of your agendas.

In fact, House Bill 103, which is scheduled for this coming Thursday really caught my eye. Not so much the specifics of the bill but its title, "An Act relating to royalty oil".

You might want to consider being more specific because as you know, a broad title allows all sorts of amendments to be added as the bill winds its way through the legislative process. Again, this is not a specific request on my part, more of a suggestion. If you have any comments, please feel free to give me a call.

Senator Faiks put this on the agenda