

SCOMM

62:29

Alaska State Legislature

Senator Drue Pearce, Chair
Senator Tim Kelly
Senator Rick Halford
Senator Paul Fischer
Senator Al Adams



WHILE IN JUNEAU:
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ANCHORAGE, ALASKA 99503
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SENATE SPECIAL COMMITTEE ON OIL AND GAS

AGENDA

THURSDAY, FEBRUARY 8, 9:00 A.M.

SENATE FINANCE -- ROOM (528)

HB 128 -- OIL & GAS LEASES & ROYALTY REDUCTION

SPONSOR: REPRESENTATIVE KAY BROWN

FIRST HEARING

SSSB 359 -- MUNICIPAL ASSISTANCE: OIL RESPONSE FUND

CONTINUATION OF BILL

Kay Brown

Alaska State Legislature House of Representatives

TO: Senator Drue Pearce, Chair
Senate Special Committee on Oil and Gas

FROM: Representative Kay Brown

DATE: February 7, 1990

SUBJ: CS HB 128 (Finance) Oil and Gas Leasing Practices and
State Royalties

Thank you for scheduling a hearing on CS HB 128 (Finance). As indicated in the enclosed sectional analysis, the proposed legislation has several different provisions that collectively will:

- o improve the efficiency of the state's oil and gas leasing program;
- o encourage production from marginal oil and gas fields;
- o provide for a written finding by the Commissioner of the Department of Natural Resources to the President of the Senate and the Speaker of the House of Representatives before granting a royalty reduction; and
- o strengthen the Public Notice requirements for proposed state oil and gas lease sales.

I look forward to the opportunity to discuss this legislation with the Senate Special Committee on Oil and Gas.

FISCAL NOTE

REQUEST:

Revision Date: 30-Jan-90

Title: An Act relating to oil & gas & geothermal leasing practices.

Sponsor: Brown, M. Davis, Gruenberg, Ellis

Requestor: Senate Oil & Gas Committee

Agency Affected: Natural Resources

BRU: Petroleum Management

Components: Petroleum Mgmt

EXPENDITURES/REVENUES:

(Thousands of Dollars)

OPERATING	FY 91	FY 92	FY 93	FY 94	FY 95	FY 96
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0

CAPITAL						
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REVENUE						
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FUNDING: (Thousands of Dollars)

GENERAL FUND						
FEDERAL FUNDS						
OTHER						
TOTAL	0.0					

POSITIONS:

FULL-TIME						
PART-TIME						
TEMPORARY						

ANALYSIS: (Attach a separate page if necessary)

Prepared by: Carol Wilson
Division: Commissioner's Office

Phone: 465-2400
Date: 30-Jan-90

Approved by Commissioner: Lennie Gorsuch
Agency: Department of Natural Resources

Date: 30-Jan-90

Distribution (by preparer) :
Legislative Finance
Legislative Sponsor
Requestor
Office of Management and Budget
Impacted Agency(ies)

March 16, 1989

The Honorable Kay Brown
Alaska House of Representatives
P. O. Box V
Juneau, Alaska 99811

Dear Representative Brown:

RE: HB 128

We have reviewed with much interest the provisions of HB 128. Conoco believes enactment of this legislation would send a strong signal that the State of Alaska recognizes the current economic dilemma we all are in and is willing to make provisions to ensure the continued economic development and production of its oil resources in times of volatile crude prices. Conoco foresees crude price volatility remaining the dominant factor affecting oil and gas investment decisions for some time to come. The following statement is offered in support of HB 128:

Section 1. Amendment to AS 38.05.035(e).

The proposed amendments to this statute will enable tracts offered for lease during the previous five years to be reoffered for lease through an expedited process. Removing both the two year scheduling requirement and a repeat best interest finding will remove some of the cumbersome detail currently necessary for leasing reoffered tracts. Continued effort to further streamline the present leasing system is needed and encouraged.

Section 2. Amendment to AS 38.05.180(j).

Conoco has been involved both legislatively and administratively with the interpretation of AS 38.05.180(j) for the past several years. We believe the changes proposed in HB 128 will clarify much of the confusion with the existing statute.

When Title 38 was rewritten in 1978, the legislature authorized royalty and net profits share to be included as bid variables. As we interpret the intent, subsection (j) was added to limit the circumstances under which a lessee could reduce its royalty below their bid value submitted to obtain a lease at a competitive lease sale. We believe it was not the legislature's intent at that time to prevent the Commissioner from utilizing authorities granted under subsection (p) which apply during the operation of a unit. The record shows specifically that the legislature rejected an amendment in 1978 that would have limited the Commissioner's authority under (p) by the provisions in (j).

As applied however, the limitations of subsection (j) have apparently restricted the Commissioner's actions under subsection (p). The changes to 180 (j), as proposed in HB 128, will remove the interpretation conflicts between language originally intended for bidding provisions and the subsequent operation of a unit either producing or mechanically capable of production.

The late 1970's and early 1980's were "boom" times for both the oil industry and the State of Alaska. With oil prices in excess of \$30/bbl and forecasted to increase further, the perception and financial condition of both the State and industry were vastly different than under the economic realities of today. The realities of resource development today dictate changes by both the State and industry if continued economic development of the State's resources is to continue. Industry must reduce and optimize development and operational costs, and the State must institute royalty and taxing systems that preferentially attract and encourage continued private sector investment in Alaska.

Conoco views it's relationship with the State as a partnership, with each partner adhering to the implied and contractual obligations of the other. The partnership will be successful when both partners are able to work together, trust and respect each other, and perceive that they are receiving an equitable return from the partnership. By amending 180 (j) we believe the State would be contributing significantly towards a successful partnership.

Specifically the proposed amendments to HB 128 will:

- Remove the ambiguities between bidding methods and lease operations;
- Remove the arbitrary and poorly defined "two years initial production;"
- Give the Commissioner broader authority to protect the State's interests with crude price increases.

For these reasons, Conoco enthusiastically supports all of the proposed revisions.

Although we have made the decision to resume production from the Milne Point Unit, it should be noted that our anticipated income stream, while generating a small positive cash flow, remains insufficient to provide a positive rate of return on our total investment. Under existing statutes we are eligible to apply for a reduced royalty at Milne Point after approximately ten additional months of production. Although the proposed amendments to 180 (j) may not directly affect Milne Point at this time, we envision they may, given the volatility of crude prices, be of direct future benefit to Milne Point or any other smaller field in the State.

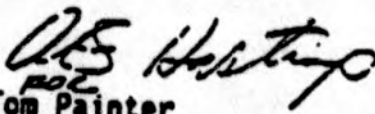
The Honorable Kay Brown
March 16, 1989
Page 3

Section 3. Amendment to AS 38.05.180(w).

Changing the proposed lease term from five years to ten years is very important for leases in frontier areas such as Alaska. With the long lead times for permitting and the potentially limited exploratory drilling seasons, five years is insufficient to adequately evaluate a lease. Increasing the term to ten years will make the leases more attractive to industry, which should also be reflected in lease bonuses to the state.

This concludes my statement supporting HB 128. If you have any questions or need additional clarification, please call me at 564-7601.

Very truly yours,


Tom Painter
Division Manager

AEH(jah)

**State Of Alaska Five-Year Oil And Gas Leasing Program
For The Period 1990 Through 1994**

	<u>Sale Number</u>	<u>Sale Name</u>	<u>Proposed Date</u>
FY91	67A	Cook Inlet Exempt	September 1990
	70A	Kuparuk Uplands Exempt	September 1990
	64	Kavik (North Slope)	May 1991
	65	Beaufort Sea	May 1991
FY92	74	Cook Inlet	September 1991
	61	White Hills (North Slope)	January 1992
	68	Beaufort Sea	May 1992
FY93	75	Kuparuk Uplands	September 1992
	76	Cook Inlet	January 1993
	77	Nanushuk (North Slope)	May 1993
FY94	57	North Slope Foothills	September 1993
	78	Cook Inlet	January 1994
	79	Cape Yakataga	May 1994
FY95	80	Shaviovik (North Slope)	September 1994

STEVE COWPER, GOVERNOR

March 15, 1989

DEPARTMENT OF NATURAL RESOURCES

400 WILLOUGHBY AVE.
JUNEAU, ALASKA 99801-1796
PHONE: (907) 485-2400

OFFICE OF THE COMMISSIONER

The Honorable Cliff Davidson
Alaska State Representative
The Honorable Curt Menard
Alaska State Representative
Co-Chairmen
House Resources Committee
Alaska State Legislature
P.O. Box V
Juneau, AK 99811

Dear Representative Davidson and Representative Menard:

Subject: House Bill 128, relating to state oil, gas and geothermal leasing practices, and adjustments of royalties to encourage commercial production.

Position: The Department of Natural Resources supports this bill. It would allow us to be more responsive to industry requests for oil and gas lease sales, would clarify existing public noticing requirements, and would enable us to grant a royalty reduction for shut-in oil and gas that makes resumption of production economically feasible.

Background: Sections one and three of this bill reflect administrative changes in the state's oil and gas leasing program that would lead to increased efficiency for the department, and would generate additional revenues for the state.

An "exempt" oil and gas lease sale consists of acreage that has already been leased at least once by the state, or acreage that is adjacent to already leased lands. A "reoffering" sale consists of acreage that was offered for lease at least once by the state but, for various reasons, was never purchased.

Existing statutes allow the department to hold an exempt oil and gas lease sale without preparing a new written finding, if a written finding has been prepared for the general area during the previous 3 years. This bill would increase the elapsed time before a new finding needs to be prepared to five years. The existing three year period is not enough time for us to offer eligible acreage, as requested by industry, for lease.

This bill would also make the five year exemption from a written finding available to us for reoffering sales, and would increase the lease term for a reoffering sale from five years to ten. Ten

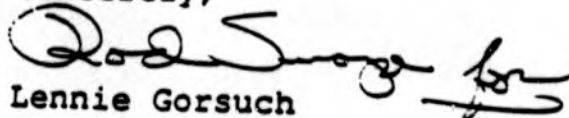
years is the lease term used for other oil and gas lease sales.

Section two of the bill would assist owners of shut-in fields to reestablish commercial production by allowing the Commissioner, based on certain conditions, to reduce the required lease royalty. Royalty reductions granted under this bill would be conditioned to protect the state's interest.

Section four of this bill is an housekeeping measure that would clarify the public noticing requirements for state oil and gas lease sales.

Please let me know if you would like additional information related to this bill.

Sincerely,


Lennie Gorsuch
Commissioner

cc: Committee members
Sponsor
Bob Evans
Denby Lloyd
Dennis Kelso
Don Collinsworth
Jim Eason

Representative Kay Brown
February 7, 1990

SECTIONAL ANALYSIS
CS HB 128 (Finance)

Oil and Gas Leasing Practices and State Royalties

Section 1

Amends existing law regarding the requirement to prepare a new "best interest finding" in the case of "exempt" oil and gas lease sales under AS 38.05.180(d) and AS 38.05.180(w). The proposed change would allow the Department of Natural Resources to lease lands under these statutes without preparing a new "best interest finding" if a finding had been prepared within the previous five years, unless the Commissioner determines that new information has become available that justifies revision of the prior finding.

Section 2

Would give the Commissioner of the Department of Natural Resources authority to reduce royalties in order to reestablish shut-in oil and gas production that would otherwise not be economically feasible. Would remove the provision in existing law requiring two years of initial production from a field before a royalty reduction could be granted. Before granting a royalty reduction, the lessee would be required to make a clear showing that the shut-in resources would not be economical to produce without a royalty reduction. The Commissioner would have to find that the state was obtaining the maximum possible economic return compatible with a reasonable rate of return for the lessee. Further, the Commissioner would have to provide a written finding to the President of the Senate and the Speaker of the House of Representatives before granting a royalty reduction.

Section 3

Amends AS 38.05.180(w) regarding the term of a lease that has been re-offered. Existing law stipulates that the term of a re-offered lease shall be limited to five years. The proposed change would increase the maximum term of a re-offered lease to ten years.

Section 4

Amends the Department of Natural Resources public notice requirements as they pertain to the leasing of hydrocarbon and geothermal resources. The proposed change would reestablish the requirement that the department provide broad public notice of leasing actions to potentially affected parties.

Oil and Gas Lease Sale Options
Comparison of existing statutes with changes proposed in HB 128
to AS 38.05.035(e) and AS 38.05.180(w)
Prepared by Division of Oil & Gas

Regular Sales

Exempt Sales

Reoffering Sales

Regular Sales		Exempt Sales		Reoffering Sales	
Existing Statutes	HB 128 Proposed Change	Existing Statutes	HB 128 Proposed Change	Existing Statutes	HB 128 Proposed Change
Must be on five-year leasing schedule. [AS 38.05.180(b)]	*No changes	Not required to be on five-year schedule. [AS 38.05.180(d)]		Not required to be on five-year schedule. [AS 38.05.180(w)]	
Sales proposed by Div. of Oil & Gas; industry comments solicited each year.		Sales based on unsolicited industry nominations; several received each year.		Sales based on unsolicited industry nominations; several received each year.	
Acreage consists of new "frontier" areas and old areas offered in the past.		Acreage previously leased and now relinquished or expired; or, acreage adjacent to existing leases.		Acreage previously offered but not leased.	
New best interest finding required for each sale; public notices issued.		Can use up to 3-year-old best interest finding if no new significant information; public notices issued.		New best interest finding required for each sale; public notices issued.	
Lease term up to ten years.		Lease term up to ten years.		Lease term no more than five years.	
			*Allows use of up to 5-year-old best interest finding if no new significant information. All public notices will still be issued. [AS 38.05.035(e)(7)]		*Allows use of up to 5-year-old best interest finding if no new significant information. All public notices will still be issued. [AS 38.05.035(e)(8)]
					*Allows lease term of up to ten years. [AS 38.05.180(w)]