

ALASKA LEGISLATURE SPECIAL COMMITTEE/SUBJECT FILE 8672
2128 SCOMM 79: HOUSE SPEC. COMM. ON OIL & GAS, 1991-1992

Hon. Dennis D. Kelso
Department of Environmental
Conversation

October 29, 1990
Page 4

MOA provides indemnification for those circumstances where otherwise there would be liability exposure because the commission is a state rather than municipal agency or where the individual defendant happens to be a non-governmental person.

Question 7. If there are liability risks associated with activities of an LEPC, will the State represent and indemnify the LEPC, the local government under which it is formed, and its members? Are there limits to the coverage for gross negligence or intentional acts? If so what are examples of acts that might trigger a limitation on coverage?

Answer. The MOA provides for representation of the LEPC and its members to the extent that no insurer has coverage obligations. If a local government is the alter ego of the LEPC, the municipality would also be defended where the plaintiff named the municipality as a defendant. The state will represent where there has been a determination that, at most, the defendant's conduct was only ordinary negligence but will not indemnify for conduct found to constitute gross negligence or intentional misconduct.

It is not possible to predict the degree of negligence for any specific type of conduct. Negligence may be ordinary, gross, or willful. Ordinary negligence is the failure to use ordinary care. Gross negligence is a failure to exercise even that care which a careless person would use, while willful negligence describes intentional conduct in disregard of an obvious risk occurring under circumstances that make it probable that harm to the plaintiff will result. W. Prosser, The Law of Torts § 180-85 (4th ed. 1971).

WGM:jal
Attachment

cc w/enc.: Camille Stephens

MEMORANDUM

State of Alaska

RECEIVED

TO: Douglas B. Baily
Attorney General
Department of Law

DATE: July 30, 1980
JUL 31 1980

FILE NO:

TELEPHONE NO:

STATE OF ALASKA
DEPT. OF ENVIRONMENTAL CONSERVATION
DIVISION OF ENVIRONMENTAL QUALITY

FROM: Dennis D. Kelso
Commissioner
Department of Environmental
Conservation

SUBJECT: Liability of State,
Members of the State
Emergency Response
Commission (SERC),
Local Emergency
Planning Committees
(LEPCs) and the
Hazardous Substance
Spill Technology
Review Council

On behalf of the State Emergency Response Commission (SERC), I am requesting an opinion concerning the potential liability arising from the activities of the SERC, the Hazardous Substance Spill Technology Review Council, or the Local Emergency Planning Committees (LEPCs). Members of the SERC are appointed by the Governor under the Superfund Amendments and Reauthorization Act, Title III (SARA Title III), Administrative Order 103, and House Bill 566 which passed last session. The SERC is required by law to review and approve membership on the LEPCs. The Hazardous Substance Spill Technology Review Council was established within the SERC by HB 566. Seven of its nine members are appointed by the Governor.

The SERC and LEPCs have many planning and coordinating functions imposed by federal and recently passed state statutes (AS 46.13). However, neither has any direct administrative function. Response to hazardous substance and oil spill incidents remains the responsibility of Department of Environmental Conservation (DEC), the Department of Military and Veterans Affairs (DMVA), and other local, state, and federal agencies.

For SERC, the LEPCs, and the Council to be effective in their mission, there must be a large pool of potential members representing the various roles and expertise necessary to prepare an emergency response plan for hazardous substance and oil spill incidents. This is especially true at the local level. SERC policy has encouraged LEPCs to establish strong ties with, and even organize under the auspices of, a local government and the strive for the broadest possible representation on the committee. In many cases, LEPC membership exceeds the minimum number of participants mandated by state and federal law.

This policy encourages the level of public participation necessary to effectively carry out the goals of SARA Title III and HB 566. However, it is jeopardized by growing fears on the part of the local governments and the LEPC members about what, if any, liability may be attached to membership on an LEPC. This uncertainty now extends to the SEPC members as well and impedes our ability to accomplish our statutory duties. Although members of the Council have not yet been appointed, it is reasonable to assume the same questions will arise in relation to its activities and members. This concern may result in some candidates being unwilling to accept appointment without reassurance about the degree of potential liability they may be assuming.

Before narrowing this request to the specific questions, I want you to know that I appreciate the likelihood that most fear of liability is hypothetical. However, the fear is real and no one wants to take any significant chance, or perhaps even a slight chance, of being sued for damages associated with a hazardous substance or oil spill incident. The cost of defense alone, as we well know could bankrupt anyone.

Specifically our questions are:

1. What liability, if any, may exist for the SERC or the Council as state agencies or entities?
2. What liability, if any, do the members of the SERC accrue due to their activities, or inactivity, as SERC members? If there is liability, will the state represent and indemnify the members should an award be made? (It is important to remember that some members are appointed to represent business, local governments, and other specific interests.)
3. If the state will represent and indemnify the SERC members, are there any limits, (for example gross negligence or intentional acts)? If there are such limits, please give examples of what may constitute such acts.
4. Questions 2 and 3 also pertain to the Hazardous Substance Spill Technology Review Council and its members.
5. Where an LEPC is formed under the auspices of a local government, does the local government run the risk of liability?
6. What are the liability risks to an LEPC or its individual members?

July 30, 1990

7. If there are liability risks associated with activities of an LEPC, will the State represent and indemnify the LEPC, the local government under which it is formed, and its members? Are there limits to the coverage for gross negligence or intentional acts? If so what are examples of acts that might trigger a limitation on coverage.

I have not tried to list the duties of the SERC, LEPCs or Council, although it is apparent that the answers to the questions are driven by the duties. The best source is the laws themselves, especially since SARA Title III is still relatively new and HB 566 was just passed by the Governor.

Should your review suggest there is any significant risk of liability for the members of any of these three entities, especially if the state will not fully represent and indemnify them, I would appreciate suggestions for a legislative "fix".
The goals of SARA Title III and HB 566 cannot be met if the participants in the activities, local governments, or the State are subject to liability for their participation.

There are voluminous materials concerning SERC and SARA Title III that may be relevant to liability issues. An attached December 28, 1987, memo from a Kentucky Assistant Attorney General may be particularly helpful. Also attached are memos from two LEPC chairs expressing their liability concerns.

Please feel free to contact me or Camille Stephens of DEC's Spill Prevention, Planning and Management staff at 465-2630.

Thank for your assistance with this important matter.

Attachments

bcc: Camille Stephens

MEMORANDUM

TO: COLONEL MIKE MOLLOY
CHAIRMAN, KENTUCKY EMERGENCY RESPONSE COMMISSION

FROM: GREG HOLMES, ASSISTANT ATTORNEY GENERAL *gh*

RE: ASSESSMENT OF LIABILITY OF STATE COMMISSION AND
LOCAL COMMITTEES APPOINTED PURSUANT TO SARA

DATE: DECEMBER 28, 1987

At your request I have prepared the following assessment of the potential liability of the state commission and the local committees appointed pursuant to Title III of the Super Fund Amendments and Reauthorization Act of 1986 (hereinafter "SARA"). This assessment constitutes my legal opinion based on an analysis of existing statutes and case law.

The potential liability of the commission or committee must be thought of in two distinct ways: the liability of the commission or committee itself and the liability of the individual commissioners or committee members. It appears that the commission or committee itself will not be liable unless it fails to comply with a mandatory requirement spelled out in Title III of SARA. For example, should the commission or a committee fail to comply with the time table mandated in the federal statute, and should any future damages to any person or company accrue from such failure, there could be potential liability under the provisions of Title III. Title III does authorize persons to seek injunctive relief (that is orders from the federal courts requiring the commission or committee to undertake a mandated activity or to refrain from a forbidden activity) in matters concerning the enforcement of the provisions of the statute.

With regard to the potential liability of individual commission or committee members, all attorneys with whom I have spoken as well as my own research indicate that while we cannot be certain, it appears at this point that individual commission and committee members would not be liable unless: a) they fail to comply with the mandated requirement as discussed in the paragraph above; and b) such failure was due to gross negligence or willful misconduct.

Finally, it is important to note that commission and committee members, being appointed pursuant to state law to carry out state-mandated functions, are agents of the state with all the attendant immunities from liability conferred by law upon appointees to other state boards, commissions, and agencies.

NORTH SLOPE BOROUGH

BARROW GAS FIELD DEVELOPMENT PROJECT
P.O. Box 1120 Barrow, Alaska 99723

Phone: 907-852-7779
Fax 907-852-8971



April 3, 1990

Ms. Linda Van Houten
SARA Title 111 Coordinator
Department of Environmental Conservation
P.O. Box 0
Juneau, Alaska 99811-1800

Dear Ms. Van Houten;

The Prudhoe Bay Area LEPC membership is concerned about the area of liability in regards to their participation and activity within the framework of the LEPC.

As coordinator, I have been requested to query SERC and relay a response regarding potential liability in the following areas:

1. What is the nature of liability coverage for LEPC members?
2. What is the extent of liability coverage?
3. Who is responsible for liability coverage for members?
4. When is the membership covered and how?
5. Is the membership covered professionally and personally?
6. Is the membership covered against civil or criminal liability?

I understand that the question of liability for LEPC membership is an area yet to be completely clarified. However, the subject remains a timely concern for the Prudhoe Bay Area membership. I appreciate your address to this topic. Our next meeting is scheduled for April 23, 1990. If your schedule permits, please respond before this date. If I can be of further assistance to you, please contact me at your convenience, 852-2611, ext. 247.

Sincerely,

T.R. Reil
Coordinator, Prudhoe Bay Area LEPC

cc: David McDowell ✓
Division of Emergency Services

TO: Commissioner Dennis Kelso, Chair
State Emergency Response Commission

FROM: Steven O'Connor, Interim Chair
Kenai Peninsula Local Emergency Planning Committee

SUBJ: LEPC Budget and concerns

DATE: January 10, 1990

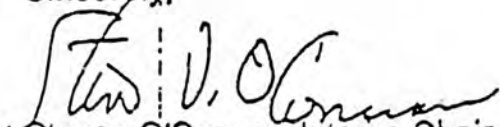
The Kenai Peninsula Local Emergency Planning Committee would like to submit a draft budget for consideration by the State Emergency Response Commission. This budget is just a preliminary draft as we have not had time to develop a workplan. As soon as the workplan is complete we will have a better idea of our fiscal needs.

Our LEPC has met and established a steering committee to draft bylaws and look at short term work objectives. The next full meeting of the Kenai Peninsula LEPC is scheduled for January 22, 1990. At that meeting the draft bylaws will be presented for consideration along with this budget. Dave McDowell is also scheduled to review the SERC workplan with the group with an emphasis on how the SERC workplan will provide guidance for the development of our local workplan. I have attached an agenda for your consideration.

Also attached are some concerns that have come up that the LEPC would appreciate your office or the State Emergency Response Commission addressing for us. These questions may have already been addressed in other areas. If you have any questions to clarify the attached questions please feel free to call Ross Kinney, Finance Director or Phil Reeves, Assistant Borough Attorney for the Kenai Peninsula Borough at 262-4441.

At this time I intend to be present at the SERC meeting scheduled for January 12, 1990 to answer any questions. Thank you for your time and consideration.

Sincerely,


Steven O'Connor, Interim Chair
Kenai Peninsula Local Emergency
Planning Committee

cc: Linda VanHouten
cc: Dave McDowell

enclosures (5)

QUESTIONS FOR SERC REGARDING LEPC FINANCING
AND LIABILITIES OF MEMBERS OF A LEPC

1. Will the SERC account for and allocate funding/expenditures of the LEPC's or will the LEPC's control their own finances? If the latter, we propose that the Borough administer LEPC finances as an agency fund; i.e., account for receipts and disbursements of funds based on the LEPC's budget which remains under the LEPC's discretion and control. This will allow the LEPC to meet the State and Federal single-audit requirements without additional expense.

2. LEPC members are apparently covered by the State of Alaska workmen's compensation coverage under AS 23.30.242. Will volunteer subcommittee members of the LEPC who are not LEPC members; approved by the State be covered by State worker's comp policies, and what will be the procedure for notification and acceptance of such subcommittee members by the CERC for such compensation coverage?

3. Are LEPC members (and subcommittee members) covered under the State's general liability coverage particularly for automobile liability? Are there any particular insurance requirements which the State will impose upon LEPC and subcommittee members for utilization of their personal automobiles in connection with their LEPC service?

4. Are LEPC members covered by any state public officials liability coverage? Will the State commit to providing legal defense for LEPC members in the event they are named defendant in a legal action based upon their LEPC service?

Comment. AS 09.50.250 provides immunity for the State and its agencies from tort actions arising from discretionary activities. This is obviously a limited immunity, and our Borough Risk Management policy is to insure our elected officials who are covered by a similar (but broader) municipal immunity under AS 09.65.070. AS 26.20.140 provides a much broader immunity for the State, its agents and representatives in activities under that chapter on civil defense. There is no similar immunity provided under AS 26.23 which is the Alaska Disaster Act. While we are aware that some people have cited AS 26.20.140 in discussing immunity provisions for disaster actions, we question this interpretation particularly considering AS 26.23.210 which sets out the relationship of the Alaska Disaster Act to the civil defense statute by stating: "The Alaska civil defense statute (AS 26.20), applies to preparedness, response, and recovery from disasters caused by enemy attack and other hostile military or paramilitary action. The provisions of this chapter [AS 26.23], other than AS 26.23.130, apply to preparedness, response, and recovery in cases of natural and nonmilitary man-made disasters." It would seem that AS 26.23.210 expressly denies application of AS 26.20.140 immunities to actions undertaken under AS Chapter 26.23.

corporation, is an employee of the corporation under this chapter. However, an executive officer of a corporation may waive coverage under this chapter, subject to the approval of the commissioner of labor, notwithstanding AS 23.30.245(b). Notwithstanding any other provision of this chapter, an executive officer of a municipal corporation or of a charitable, religious, educational, or other nonprofit corporation may be brought within the coverage of its insurance contract by the corporation by specifically including the officer in the contract of insurance. The election to bring an executive officer within the coverage continues in force for the period the contract of insurance is in effect. During that period an executive officer brought within the coverage of the insurance contract is an employee of the corporation under this chapter. (§ 2(8) ch 193 SLA 1959; am ch 146 SLA 1962)

NOTES TO DECISIONS

Stated in *Gordon v. Burgess Constr. Co.*, Sup. Ct. Op. No. 401 (File No. 716), 425 P.2d 602 (1967).

Cited in *Gordon v. Burgess Constr. Co.*, Sup. Ct. Op. No. 401 (File No. 716), 425 P.2d 602 (1967).

Collateral references. — 51 Am. Jur. 2d, Workmen's Compensation, § 177.

Sec. 23.30.241. Special officers as employees. (2) A special officer appointed under AS 18.65.010(a) is considered an employee under this chapter only when the person is actually traveling or working as a special officer. The weekly wage earned in the special officer's regular employment shall be used in computing the amount of compensation to be awarded. If a special officer has no regular employment, the minimum wage paid a full-time state trooper shall be used in computing the amount of compensation to be awarded.

(b) Annual appropriations to fund the coverage provided for in (a) of this section shall be provided for in the budget of the Department of Public Safety. (§ 1 ch 6 SLA 1978)

§ Sec. 23.30.242. Members of state boards and commissions as employees. (2) A member of a state board or commission is considered an employee under this chapter only while the member is actually traveling or working as a member of the board or commission. The maximum weekly wage shall be used in computing the amount of compensation to be awarded.

(b) Annual appropriations to fund the coverage provided for in (a) of this section shall be provided for in the budget of the Office of the Governor. (§ 1 ch 105 SLA 1969; am § 54 ch 69 SLA 1970)

PLANNING AND RIGHT-TO-KNOW

42 USCS § 11046

paragraph and served upon any person, the district court of the United States for any district in which such person is found, resides, or transacts business, upon application by the United States and after notice to such person, shall have jurisdiction to issue an order requiring such person to appear and give testimony before the administrative law judge or to appear and produce documents before the administrative law judge, or both, and any failure to obey such order of the court may be punished by such court as a contempt thereof.

(Oct. 17, 1986, P. L. 99-499, Title III, § 325, 100 Stat. 1753.)

HISTORY; ANCILLARY LAWS AND DIRECTIVES

Effective date of section:

Act Oct. 17, 1986, P. L. 99-499, § 4, 100 Stat. 1614, which appears as 42 USCS § 9601 note, provides that this section is effective on enactment on Oct. 17, 1986.

SERC Liability under Federal law

11046. Civil actions

(a) Authority to bring civil actions. (1) Citizen suits. Except as provided in subsection (e), any person may commence a civil action on his own behalf against the following:

(A) An owner or operator of a facility for failure to do any of the following:

(i) Submit a followup emergency notice under section 304(c) [42 USCS § 11004(c)].

(ii) Submit a material safety data sheet or a list under section 311(a) [42 USCS § 11021(a)].

(iii) Complete and submit an inventory form under section 312(a) [42 USCS § 11022(a)] containing tier I information as described in section 312(d)(1) [42 USCS § 11022(d)(1)] unless such requirement does not apply by reason of the second sentence of section 312(a)(2) [42 USCS § 11022(a)(2)].

(iv) Complete and submit a toxic chemical release form under section 313(a) [42 USCS § 11023(a)].

(B) The Administrator for failure to do any of the following:

(i) Publish inventory forms under section 312(g) [42 USCS § 11022(g)].

(ii) Respond to a petition to add or delete a chemical under section 313(e)(1) [42 USCS § 11023(e)(1)] within 180 days after receipt of the petition.

(iii) Publish a toxic chemical release form under 313(g) [42 USCS § 11023(g)].

(iv) Establish a computer database in accordance with section 313(j) [42 USCS § 11023(j)].

(v) Promulgate trade secret regulations under section 322(c) [42 USCS § 11042(c)].

(vi) Render a decision in response to a petition under section 322(d) [42 USCS § 11042(d)] within 9 months after receipt of the petition.

(C) The Administrator, a State Governor, or a State emergency response commission, for failure to provide a mechanism for public availability of information in accordance with section 324(a) [42 USCS § 11044(a)].

(D) A State Governor or a State emergency response commission for failure to respond to a request for tier II information under section 312(e)(3) [42 USCS § 11022(e)(3)] within 120 days after the date of receipt of the request.

(2) State or local suits. (A) Any State or local government may commence a civil action against an owner or operator of a facility for failure to do any of the following:

(i) Provide notification to the emergency response commission in the State under section 302(c) [42 USCS § 11002(c)].

(ii) Submit a material safety data sheet or a list under section 311(a) [42 USCS § 11021(a)].

(iii) Make available information requested under section 311(c) [42 USCS § 11021(c)].

(iv) Complete and submit an inventory form under section 312(a) [42 USCS § 11022(a)] containing tier I information unless such requirement does not apply by reason of the second sentence of section 312(a)(2) [42 USCS § 11022(a)(2)].

(B) Any State emergency response commission or local emergency planning committee may commence a civil action against an owner or operator of a facility for failure to provide information under section 303(d) [42 USCS § 11003(d)] or for failure to submit tier II information under section 312(e)(1) [42 USCS § 11022].

(C) Any State may commence a civil action against the Administrator for failure to provide information to the State under section 322(g) [42 USCS § 11042(g)].

(b) Venue. (1) Any action under subsection (a) against an owner or operator of a facility shall be brought in the district court for the district in which the alleged violation occurred.

(2) Any action under subsection (a) against the Administrator may be brought in the United States District Court for the District of Columbia.

(c) Relief. The district court shall have jurisdiction in actions brought under subsection (a) against an owner or operator of a facility to enforce the requirement concerned and to impose any civil penalty provided for violation of that requirement. The district court shall have jurisdiction in actions brought under subsection (a) against the Administrator to order the Administrator to perform the act or duty concerned.

(d) Notice. (1) No action may be commenced under subsection (a)(1)(A) prior to 60 days after the plaintiff has given notice of the alleged

violation to the Administrator, the State in which the alleged violation occurs, and the alleged violator. Notice under this paragraph shall be given in such manner as the Administrator shall prescribe by regulation.

(2) No action may be commenced under subsection (a)(1)(B) or (a)(1)(C) prior to 60 days after the date on which the plaintiff gives notice to the Administrator, State Governor, or State emergency response commission (as the case may be) that the plaintiff will commence the action. Notice under this paragraph shall be given in such manner as the Administrator shall prescribe by regulation.

(e) **Limitation.** No action may be commenced under subsection (a) against an owner or operator of a facility if the Administrator has commenced and is diligently pursuing an administrative order or civil action to enforce the requirement concerned or to impose a civil penalty under this Act [42 USCS §§ 11001 et seq.] with respect to the violation of the requirement.

(f) **Costs.** The court, in issuing any final order in any action brought pursuant to this section, may award costs of litigation (including reasonable attorney and expert witness fees) to the prevailing or the substantially prevailing party whenever the court determines such an award is appropriate. The court may, if a temporary restraining order or preliminary injunction is sought, require the filing of a bond or equivalent security in accordance with the Federal Rules of Civil Procedure.

(g) **Other rights.** Nothing in this section shall restrict or expand any right which any person (or class of persons) may have under any Federal or State statute or common law to seek enforcement of any requirement or to seek any other relief (including relief against the Administrator or a State agency).

(h) **Intervention.** (1) By the United States. In any action under this section the United States or the State, or both, if not a party, may intervene as a matter of right.

(2) By persons. In any action under this section, any person may intervene as a matter of right when such person has a direct interest which is or may be adversely affected by the action and the disposition of the action may, as a practical matter, impair or impede the person's ability to protect that interest unless the Administrator or the State shows that the person's interest is adequately represented by existing parties in the action.

(Oct. 17, 1986, P. L. 99-499, Title III, § 326, 100 Stat. 1755.)

HISTORY; ANCILLARY LAWS AND DIRECTIVES

Explanatory notes:

Brackets are inserted around the first period in subsec. (a)(2)(A)(iv) to indicate the probable intent of Congress to omit such punctuation.

Effective date of section:

Act Oct. 17, 1986, P. L. 99-499, § 4, 100 Stat. 1614, which appears as 42 USCS § 9601 note, provides that this section is effective on enactment on Oct. 17, 1986.

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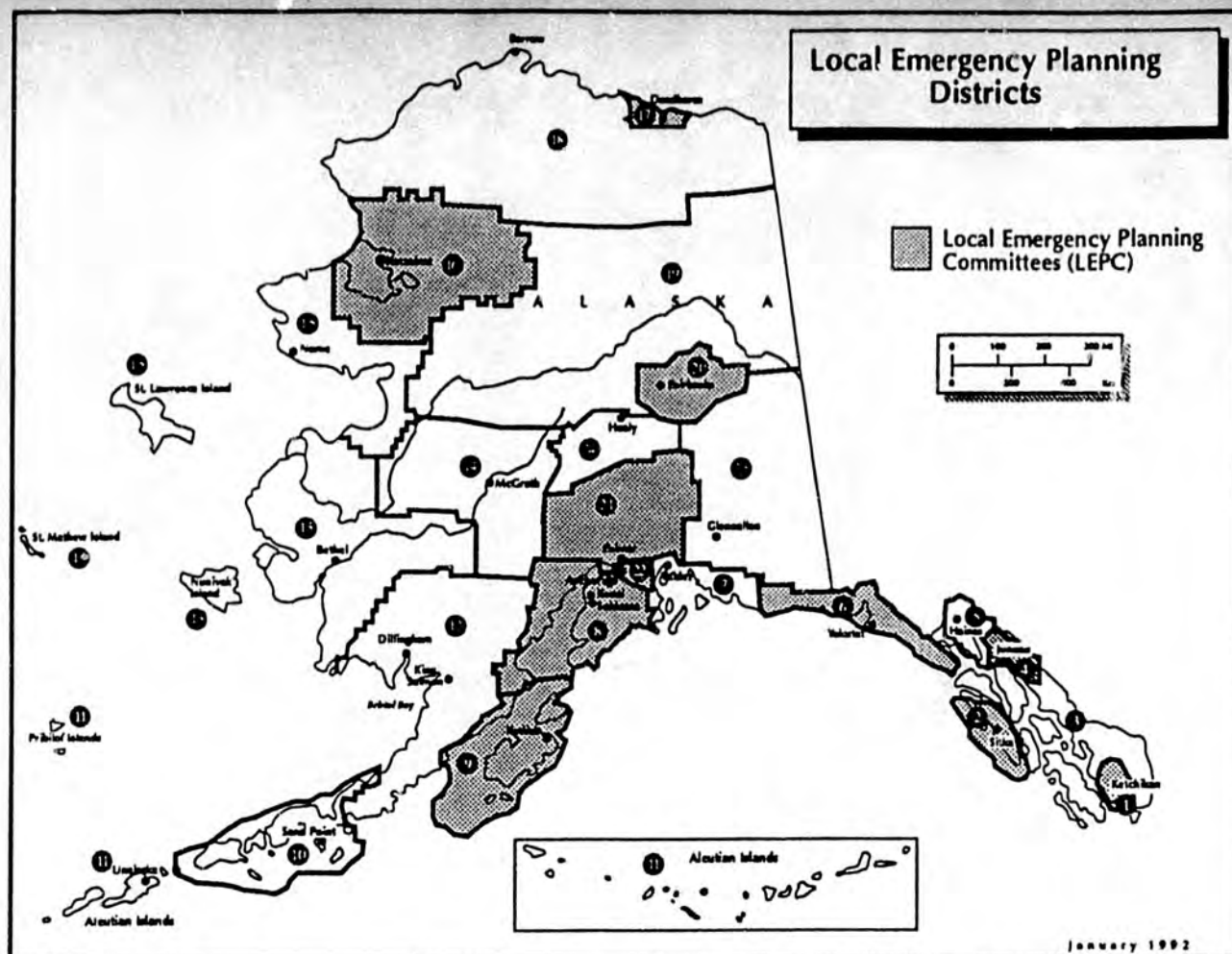
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Amy Skilbred, SERC Coordinator
Department of Environmental Conservation
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Map Key	Local Emergency Planning District (LEPD)	Principal City	LEPC appointed by SERC
1	KETCHIKAN GATEWAY BOROUGH	Ketchikan	April 4, 1991
2	CITY & BOROUGH OF SITKA	Sitka	May 14, 1990
3	Southeast	Juneau	
4	CITY AND BOROUGH OF JUNEAU	Juneau	January 29, 1992
5	Lynn Canal	Haines	
6	CITY OF YAKUTAT	Yakutat	September 18, 1989
7	Prince William Sound	Valdez	
8	KENAI PENINSULA BOROUGH	Soldotna	June 9, 1989
9	KODIAK ISLAND BOROUGH	Kodiak	June 9, 1989
10	Aleutians East Borough	Sand Point	
11	Aleutian Islands	Unalaska	
12	Bristol Bay	Dillingham	
13	Yukon Delta	Bethel	
14	Southwestern Interior	McGrath	
15	Northwestern	Nome	
16	NORTHWEST ARCTIC BOROUGH	Kotzebue	June 14, 1991
17	PRUDHOE BAY	NA	June 14, 1991
18	North Slope Borough	Barrow	
19	Interior Alaska	Fairbanks	
20	FAIRBANKS NORTHSTAR BOROUGH	Fairbanks	June 9, 1989
21	MATANUSKA-SUSITNA BOROUGH	Palmer	June 14, 1991
22	MUNICIPALITY OF ANCHORAGE	Anchorage	June 14, 1991
23	Southeastern Interior	Glenallen	
24	Denali Borough	Healy	

Approved LEPCs in Alaska

LEPC	Members	Chair
Greater Ketchikan	13	Mike Holman
City and Borough of Sitka	21	Nancy Hope
City and Borough of Juneau	20	Lissa Nelson Barnaby Dow
City of Yakutat	14	Larry Powell
Kenai Peninsula Borough	30	Keith Laurie
Kodiak Island Borough	22	Jerome Selby
Northwest Arctic Borough	24	Ron Monson
Prudhoe Bay	13	Gary Stewart
Fairbanks North Star Borough	22	Mike Oden
Matanuska-Susitna Borough	21	James MacIntosh
Municipality of Anchorage	18	Bruce Harding

CURRENT MEMBERSHIP

Revision Date: 5/24/91

BOARDS AND COMMISSIONS CONTACT ROSTER
HAZARDOUS SUBSTANCE SPILL TECHNOLOGY REVIEW COUNCIL

MEMBER	APPT	RAPPT	RAPPT	TERM
Randy Bayliss 119 Seward Street, No. 10 Juneau 99801 (H) 364-3259 (W) 586-6813 (Fax) 586-6819 Public/Restricted/ 1st JD	90/10/30	0/00/00	0/00/00	91/09/24
Edward J. Brown Water Research Center-UAF Fairbanks 99775-1760 (H) (W) 474-7350 (Fax) 474-6087 University of Alaska Rep.	90/10/30	0/00/00	0/00/00	91/09/24
Dr. Luis Proenza University of Alaska, Fairbanks Chancellor for Research 306 Signers Hall UAF Fairbanks, Alaska 99775-1720 (H) (W) 474-7314 (Fax) 474-7720 Governor's Senior Science Advisor	90/10/30	0/00/00	0/00/00	0/00/00
Jim Butchart Department of Emergency Service E. 3401 Bogard Road Wasilla, Alaska 99687 (H) (W) 376-2337 (Fax) Designee for Adjutant General/DMVA	90/12/27	0/00/00	0/00/00	0/00/00
Gordon W. Ito P. O. Box 307 Kotzebue 99752 (H) 442-3680 (W) (Fax) Public/Restricted/2nd JD	90/10/30	0/00/00	0/00/00	92/09/24

John (Randy) R. McGovern 90/11/15 0/00/00 0/00/00 93/09/24
1611 Carr
Fairbanks 99701
(H) 451-0124
(W) 456-4248
(Fax)
Public/Restricted/4th JD

Peter G. Mickelson 90/10/30 0/00/00 0/00/00 92/09/24
PWS Science Center/Box 705
Cordova 99574
(H) 424-5111
(W) 424-5800
(Fax)
Prince William Sound Science Center/Cordova/Rep.

Walter B. Parker 90/10/30 0/00/00 0/00/00 93/09/24
3724 Campbell Airstrip Road
Anchorage 99504
(H)
(W) 333-5189
(Fax)
Public/Restricted/3rd JD

Mead Treadwell 90/12/03 0/00/00 0/00/00 0/00/00
Deputy Commissioner - DEC
Commissioner's Office/DEC
P. O. Box 0
Juneau 99811
(H)
(W) 465-2600
(Fax) 465-2617

Commander Edward E. Page 00/00/00 0/00/00 0/00/00 0/00/00
Seventeenth Coast Guard Dist.
P. O. Box 3-5000
Juneau, Alaska 99802
(H) 789-4970
(W) 463-2210
(Fax) 463-2218
Coast Guard Rep./Nonvoting

Carl Lautenberger 00/00/00 0/00/00 0/00/00 0/00/00
EPA, Federal Bldg. Rm. 537
222 West 7th Ave. #19
Anchorage, AK 99501-5126
(H)
(W) 271-5083
(Fax)
EPA Rep./Nonvoting

SCOMM

79:17

STATE OF ALASKA

1992 LEGISLATIVE SESSION

BILL NO. HB 433Revision Date: 7-Feb-92Department Affected: Natural ResourcesTitle: Oil & Gas ConservationBRU: Management & AdministrationCommission DutiesComponents: AOGCCSponsor: Rep. Kay BrownRequestor: House Oil & Gas

COMPONENT SERIAL NO.

368

EXPENDITURES/REVENUES:

(Thousands of Dollars)

OPERATING	FY 93	FY 94	FY 95	FY 96	FY 97	FY 98
PERSONAL SERVICES	333.2	333.2	333.2	333.2	333.2	333.2
TRAVEL	10.0	10.0	10.0	10.0	10.0	10.0
CONTRACTUAL	330.0	330.0	330.0	330.0	330.0	330.0
SUPPLIES	10.0	10.0	10.0	10.0	10.0	10.0
EQUIPMENT						
LAND&STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	683.2	683.2	683.2	683.2	683.2	683.2

CAPITAL						
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REVENUE						
Funding Source:						

FUNDING: (Thousands of Dollars)

GENERAL FUND	683.2	683.2	683.2	683.2	683.2	683.2
FEDERAL FUNDS						
OTHER						
Funding Source:						
TOTAL	683.2	683.2	683.2	683.2	683.2	683.2

POSITIONS:

FULL-TIME	5.0	5.0	5.0	5.0	5.0	5.0
PART-TIME						
TEMPORARY						

Estimate of Current year impact:

ANALYSIS: (Attach a separate page if necessary)

See Attached

Prepared by: David JohnstonPhone: 279-1433Division: AK Oil & Gas Conservation CommissionDate: 7-Feb-92Approved by Commissioner: David JohnstonDate: 7-Feb-92Agency: Department of Natural Resources, AOGCCDistribution (by preparer) : Legislative Finance, legislative Sponsor, Requestor, OMB,
& Impacted Agency(ies).

HB 433 - "Oil & Gas Conservation Commission Duties"

Petroleum Economist (1), Range 22	78.4
Petroleum Reservoir Engineer (2), Range 24	171.4
Engineering Assistant (2), Range 12	83.4
Travel	10
Reservoir Simulation Hardware/Software/Office Space	330.0
Commodities	<u>10.0</u>
Total	683.2

The Commission advises that this estimate is based on a cursory examination of the overall intent of the proposed legislation. It provides a rough estimate of the costs required to approach the economic analysis necessary to make waste determinations.

Representative Kay Brown

ALASKA STATE LEGISLATURE

Legislative Information Office
3111 C Street #435
Anchorage, Alaska 99503
(907) 561-7627

During Session
P.O. Box V
Juneau, Alaska 99811
(907) 465-4998

TO: Representative Bill Hudson, Chair
House Oil and Gas Committee

FROM: Representative Kay Brown

DATE: February 6, 1992

SUBJ: HB 433/AO&GCC and the Definition of Waste

In anticipation of the House Oil and Gas Committee's consideration of HB 433, legislation concerning the Alaska Oil and Gas Conservation Commission and the definition of "waste," please find attached the following materials.

1. Sponsor Statement
2. Sectional Analysis
3. "Petroleum — An Overview of the Industry"
Alaska Department of Commerce and Economic Development
4. Legal Opinion
Frederick Boness/Assistant AG to Hoyle Hamilton/AO&GCC
5. Presentation to the House Finance and House Oil & Gas Committees
Kevin Meyers/ARCO Alaska, Inc. & Dave Szabo/BP (excerpt)
6. News Articles —
 "Hickel plans to test market for gas"
 Anchorage Daily News (January 23, 1992)
 "Engineers warn against loss of Prudhoe oil"
 Anchorage Daily News (January 24, 1992)

It is my understanding that the Alaska Oil and Gas Conservation Commission will be preparing a fiscal note for this legislation and will submit that fiscal note under separate cover.

If you have any questions concerning this legislation, please let me know or contact Eric Myers of my staff at 465-4998.

attachments

DISTRICT 12

Downtown • Fairview • City View • Bootleggers Cove • Inlet View • South Addition • Thunderbird Terrace
Eastridge • Penland Park • Airport Heights • Government Hill

printed on recycled paper

SPONSOR STATEMENT

House Bill 433 — AO&GCC and the Definition of Waste

House Bill 433

House Bill 433 expands the statutory responsibilities of the Alaska Oil and Gas Conservation Commission (AO&GCC) to address issues concerning the public interest in achieving maximum oil and gas recovery.

In determining whether "waste" exists, the AO&GCC shall specifically consider 1) the economic value of oil and gas that may be left behind in a reservoir; 2) the cost of recovering those resources; and 3) the public interest in achieving maximum recovery.

Consideration of Economic Factors Under Current Law

An advisory legal opinion issued by the Alaska Attorney General in 1977 concluded that the AO&GCC is allowed to consider economic factors in its establishment of conservation practices. (Boness to Hoyle, February 14, 1977). However, the opinion also suggests that further direction from the legislature would be appropriate to eliminate ambiguity regarding the AO&GCC's consideration of the public economic interest in maximizing field production.

In short, while it appears that AOGCC use of economic criteria is permissible under state statute, it is not present practice for the AO&GCC to expressly consider the public's economic interest in maximum field recovery.

The Public Interest in Maximum Oil & Gas Recovery

The public interest in maximum feasible and economic oil recovery from Alaska's oil and gas resources is compelling.

The economic significance of oil and gas development in Alaska is well documented. The petroleum sector accounted for more than a third of Alaska's state product in 1987. Oil and gas development and production activities account for a substantial fraction of total state employment. The petroleum sector directly employed over 10,000 workers in 1988 and accounted for 5% of the state's employment. The same year, it paid over \$600 million, or 10 percent, of the state total in wages and salaries. Approximately 85% of the state's revenue comes from oil and gas royalties and taxes.

The public interest in Alaska petroleum development extends beyond the economic impact of oil and gas development experienced in the state. There are substantial national, even international, interests in Alaska oil and gas development. The Prudhoe Bay oilfield is by far the largest oil field in North America — it accounts for approximately 20% of U.S. oil production and more than 3% of world oil production. As evidenced by the U.S. war with Iraq, the continued supply and availability of hydrocarbon resources is a fundamental matter of national security.

Prudhoe Bay Natural Gas Development

As indicated during recent hearing sponsored jointly by the House Oil and Gas Committee jointly with the House Finance Committee, alternative Prudhoe Bay reservoir development strategies may significantly impact the maximum achievable recovery from the reservoir.

During those hearings, testimony was presented indicating that premature, large-volume natural gas sales from the Prudhoe Bay reservoir might adversely impact the long-term recovery of oil from Prudhoe Bay. As much as a billion barrels of recoverable oil could be left behind if large-scale gas sales started by 1997, according to industry experts who testified at the hearing.

There is a compelling public interest in assuring that development of the Prudhoe Bay reservoir achieves the maximum recovery that is economically and technically feasible. While there might be substantial short-term economic benefits that would result from sale of Prudhoe Bay gas and the development of a gas line project, the value of those developments should be considered in light of long-term recovery of all hydrocarbon resources from the reservoir. If a large volume of oil were to be "left behind" in the Prudhoe Bay reservoir as a result of large volume gas sales and reduced field pressures, the net benefit to the public of gas sales could well be negative.

House Bill 433 would provide the AO&GCC clear direction to safeguard the public's economic interest in reservoir development decisions.

2/6/92 Rep. Kay Brown

SECTIONAL ANALYSIS

House Bill 433 — AO&GCC and the Definition of Waste

Section 1

Amends AS 31.05.030(b) by directing the Alaska Oil and Gas Conservation Commission (AO&GCC), when examining issues pertaining to waste, to address issues regarding the public interest in achieving maximum oil and gas recovery. In determining whether waste exists, the AO&GCC shall specifically consider 1) the economic value of oil and gas that may be left behind in a reservoir; 2) the cost of recovering those resources; and 3) the public interest in achieving maximum recovery.

Section 2

Amends AS 31.05.170(14), the statutory definition of "waste" to include "abandoning oil or gas in a reservoir if the oil or gas could be feasibly and economically recovered."

Section 3

Effective date.

Representative Kay Brown

ALASKA STATE LEGISLATURE

Legislative Information Office
3111 C Street #435
Anchorage, Alaska 99503
(907) 561-7627

During Session
P.O. Box V
Juneau, Alaska 99811
(907) 465-4998

TO: Representative Bill Hudson, Chair
House Oil and Gas Committee

FROM: Representative Kay Brown

DATE: February 7, 1992

SUBJ: HB 433/AO&GCC — Additional Materials

Oil & Gas Oversight Hearing Minutes

In addition to the materials previously provided to the House Oil and Gas Committee regarding HB 433, I would like to also provide the Committee with copies of the minutes from the recent oversight hearings regarding Prudhoe Bay oil recovery development.

Proposed Amendment

Please also find attached a proposed amendment to House Bill 433 that I would like to offer for the Committee's consideration. This additional language would clarify that the commission, when determining whether waste exists, shall consider all applicable laws and other relevant factors in addition to the specific items enumerated in subparts AS 31.05.030(b)(1) - (3).

attachment

DISTRICT 12

Downtown • Fairview • City View • Bootleggers Cove • Inlet View • South Addition • Thunderbird Terrace
Eastridge • Penland Park • Airport Heights • Government Hill

2/7/92

AMENDMENT

by BROWN

TO: House Bill 433

Page 1, line 11

delete "and"

Page 1, line 12, after "recovery"

insert "; and (4) applicable laws and any other relevant factors"



Official Business

Alaska State Legislature

HOUSE OF REPRESENTATIVES

State Capitol
Juneau, AK 99801-1182

HOUSE SPECIAL COMMITTEE ON OIL AND GAS

February 22, 1992

MEMORANDUM

TO: All Members
House Special Committee
on Oil and Gas

FROM: Bill Hudson, Chair *Bill*

SUBJECT: HB 433, correspondence and testimony
of David W. Johnston, Chairman Alaska
Oil and Gas Conservation Commission

I am attaching a copy of the testimony of Mr. David W. Johnston, Chairman of the Alaska Oil and Gas Conservation Commission pertaining to HB 433, "An Act relating to the waste of oil and gas and amending the powers and duties of the Alaska Oil and Gas Conservation Commission relating to determination of waste; and providing for an effective date," as well as a copy of his transmittal letter.

BH:lh

STATE OF ALASKA

ALASKA OIL AND GAS CONSERVATION COMMISSION

February 11, 1992

WALTER J. HICKEL, GOVERNOR

3001 PORCUPINE DRIVE
ANCHORAGE, ALASKA 99501-3192
PHONE: (907) 279-1433
TELECOPY: (907) 276-7542

The Honorable Bill Hudson
Alaska State Representative
State Capitol, Room 114
P.O. Box V
Juneau, Alaska 99801-1182

Dear Representative Hudson:

Enclosed is a copy of my testimony on HB #433 presented to the House Special Committee for Oil and Gas on February 10. You also requested additional thoughts on the Commission's existing authority to consider economic factors in the prevention of waste.

AS 31.05.170(14)(A) states: "waste" means, in addition to its ordinary meaning, "physical waste" and includes the inefficient, excessive, or improper use of, or unnecessary dissipation of, reservoir energy; and the locating, spacing, drilling, equipping, operating or producing of any oil or gas well in a manner which results or tends to result in reducing the quantity of oil or gas to be recovered from a pool in this state under operations conducted in accordance with good oil field engineering practices (emphasis added).

This provision is the heart of our conservation statute. It not only provides broad authority for the Commission to take action to prevent physical waste, but also provides a yardstick by which to measure when such action is appropriate. In other words, action by the Commission becomes appropriate when "good oil field engineering practices" are abandoned by the operator and physical waste occurs. Essentially, this is our equivalent of the "reasonable and prudent" test applied in legal argument.

The Commission believes that economic factors play an essential part in considering what constitutes "good oil field engineering practices." Reservoir depletion planning must be based not only on what is technically feasible but also on what is economically feasible. Accordingly, we believe sufficient latitude exists in the current statutory framework for the Commission to formally consider the economics of production in its determinations. While our primary focus has been on technical matters, the Commission believes it would be appropriate to expand its capability along economic lines.

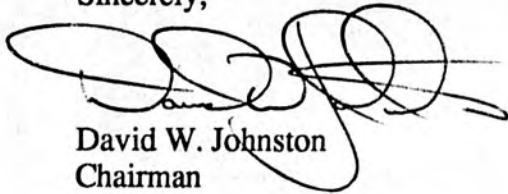
Basically, where we depart from HB 433 is in intent. We believe that the state should be provided with reasonable assurance that the reservoir is being developed consistent with the state's conservation principles, and that investments are indeed wise and appropriate for obtaining the "maximum ultimate recovery of oil and gas that is prudent" (20 AAC 25.517). Our approach would have the Commission asking those questions of the

operator to better insure that the depletion plan is fair and reasonable, but not to substitute our judgement for that of industry's in determining economic viability of projects.

To obtain "reasonable assurance" that appropriate investments are being made by the operator will require additional resources within the Commission. It is our recommendation we proceed along these lines in a prudent and deliberate manner. The Commission believes a sensible approach would be to begin with funding sufficient to hire one petroleum economist and two engineering assistants, with some contractual and travel money. We would anticipate requesting funding in the neighborhood of \$180.0 in this case.

I hope this has answered some of your questions in this matter. We, of course, would enjoy working with you and members of the committee to further develop these ideas, and thank you for your support.

Sincerely,

A handwritten signature in black ink, appearing to read 'David W. Johnston', with a large, stylized flourish extending to the right.

David W. Johnston
Chairman

Testimony for H.B. #433
House Special Committee for Oil and Gas

by
David W. Johnston, Chairman
Alaska Oil and Gas Conservation Commission

Chairman Hudson, members of the House Special Committee for Oil and Gas, my name is David W. Johnston. I am currently chairman of the Alaska Oil and Gas Conservation Commission. Seated with me today are Commissioners Russell A. Douglass and Lonnie C. Smith. The Commission appreciates this opportunity to provide comments on House Bill #433: "An act relating to the waste of oil and gas and amending the powers and duties of the Alaska Oil and Gas Conservation Commission relating to determination of waste.

During the past week, the Commission has carefully considered this bill. To better assess its possible impacts, we have consulted with a number of individuals, including the executive director of the Interstate Oil and Gas Compact Commission, the director of the Oil and Gas Section of the Texas Railroad Commission, an economist with the Division of Oil and Gas, staff within the Department of Law and various representatives of Alaska's oil industry.

HB 433 would greatly expand the authority of the Commission to make a determination of waste based upon economic criteria. We are aware of no other state that has placed such authority with its conservation commission. Some states have granted the authority to limit production to meet market demand (notably Texas, Oklahoma and Louisiana), but in this case Alaska would be breaking new ground.

Thus, we must recommend that the Legislature carefully examine the effects of such legislation before it places such broad authority in the hands of the Commission. Several concerns become apparent to us when reading this bill. First, under paragraph b, the proposed change would mandate that the Commission consider only three factors in determining if waste exists. These being: (1) the economic value of the oil and gas that may be left behind in a reservoir, (2) the cost of recovering those resources, and (3) the public interest in achieving maximum recovery. Essentially, this change could be interpreted to circumvent the Commission's traditional role of determining the existence of physical waste utilizing our knowledge of reservoir mechanics and the principles of sound engineering practices. We do not believe that is the intent of the amendment, but as written ambiguity would exist.

Secondly, the addition of the proposed phrase, "or is likely to occur," may or may not suggest a separate point in time than the term "imminent." We can only assume that the intent of this language is to require the Commission to take action to prevent waste well in advance of when it may (or may not) actually occur. In other words, the Commission may be placed in the position of acting on assumptions as opposed to evidence. This creates ambiguity as it is no longer clear as to when Commission action would be necessary and appropriate.

The intent of the proposed legislation is our third and greatest concern. If it is the intent of this legislation to provide the Commission with the authority to substitute its judgement for that of industry's in determining economic viability of projects, then the Legislature will have altered the fundamental purpose of the Commission. No longer will the Commission's review of proposed reservoir depletion plans be based upon technological merit, but will hinge on such factors as oil price forecasting, assessment of risk, discount rate of money, inflation, rate of return, pay back period, sunk costs, assessment of alternative projects, as well as examining taxes and royalty rates.

If this legislation, in fact, removes economic decision-making from industry and places it with the Commission and requires production beyond when industry believes it is reasonable, then we see industry responding by not purchasing new leases or greatly depreciating the amount it is willing to pay to explore and develop the state's oil and gas resources. We see industry turning existing leases back to the state before being compelled to make what they perceive as unsound investments, thus contributing to premature abandonment of fields. We also see the possibility of continuing lawsuits as the economics of recovery becomes the basis for waste determinations. All things considered, we see the risks of such legislation greatly outweighing its benefits.

On the other hand, if the intent of this legislation is to provide the resources and support for the Commission to expand its consideration of the economics of production in order to better insure that fields are not prematurely abandoned, then we see merit in that concept. However, we do not believe it is necessary to amend our statutory authority to accomplish such a goal. Rather, what we see as necessary is a commitment of additional funding and appropriate legislative intent language, which earmarks the funding for purposes of improving the ability of the Commission to consider economic factors in the prevention of waste. The Commission stands willing to accept this expanded role, and strongly urges the Legislature to adopt this latter approach.

Thank you, Commissioners Douglass, Smith and I are now open to any questions you may have.

FEB 6 1992

Memorandum

State of Alaska

Oil and Gas Conservation Commission

To: Landa Holton
Rep. Hudson's Office

Date: February 6, 1992

Telephone: 279-1433
Fax number: 276-7542

From: David W. Johnston
Chairman

Subject: HB433

Fiscal Note for H.B. 433

Petroleum Economist (1), Range 22	\$75,000/Yr
Petroleum Reservoir Engineer (2), Range 24	\$190,000/Yr
Engineering Assistant (2), Range 12	\$90,000/Yr
Reservoir Simulation Hardware/Software	\$300,000/Yr
Total	\$655,000/Yr

The Commission advises that this estimate is based on a cursory examination of the overall intent of the proposed legislation. It provides a rough estimate of the costs required to approach the economic analysis necessary to make waste determinations.

STATE OF ALASKA

DEPARTMENT OF LAW

OFFICE OF THE ATTORNEY GENERAL

JAY S. HAMMOND, GOVERNOR

POUCH K - STATE CAPITOL
JUNEAU 99811

February 14, 1977

Mr. Hoyle Hamilton
Director, Division of
Oil and Gas Conservation
Dept. of Natural Resources
3001 Porcupine Drive
Anchorage, Alaska 99501

RE: ECONOMIC WASTE UNDER
AS 31

Dear Hoyle:

You have asked if AS 31.05 permits the Conservation Committee to consider "economic waste" as well as physical waste. It is my conclusion that the Conservation Committee is allowed to consider economic factors in its establishment of conservation practices but that the term "economic waste" must be defined and the question related to a specific regulatory decision before a more meaningful legal opinion is possible.

I.

Brief History of Conservation Regulation

It will be helpful to an understanding of AS 31.05 to review briefly the history of oil and gas conservation regulation by states.* This is appropriate and useful because Alaska's conservation statute contains many of the same clauses and provisions found in the IOCC model statute and/or other state conservation statutes.

*/ This review is taken principally from S. McDonald, Petroleum Conservation in the United States: An Economic Analysis (1971); see also, Interstate Oil Compact Commission, A Study of Conservation of Oil and Gas in the United States (1964).

Initial conservation legislation was designed to prevent damage to other resources caused by oil and gas production and to eliminate certain obvious and easily preventable losses of natural gas. These initial conservation statutes usually established regulations applicable to individual wells (rather than whole reservoirs) and prohibited specific practices or conversely required certain specific practices, such as for example, requiring the proper casing and plugging of wells to prevent interchange of fluids among reservoir or the contamination of ground water supplies, or to prevent natural gas leaks. Later regulatory statutes usually retained the specific prohibitions of the earlier statutes but also included a general prohibition against waste which was defined in broad terms (or more often undefined). Thus, many state conservation statutes (including Alaska's) contain something of a collection of specific prohibitions and some rather broad, but undefined limitations.*

Conservation legislation, no doubt, was necessary because some operators in their haste to produce oil, employed poor production techniques and disregarded the impact of those practices on other resources (e.g. on ground water). However, another consideration was even more significant. Multiple ownership of the land overlying oil reservoirs combined with the rule of capture** to create an overpowering incentive for each owner of a lease to produce as

*/ AS 31.05.020 provides: "The waste of oil and gas in the state is prohibited." "Waste" is defined by AS 31.05.170(11) which because of its length is attached as appendix A hereto.

**/ The rule of capture says that whoever produces the oil owns it, regardless of where it is located underground. Railroad Commission v. Rowan & Nichols Oil Co., 310 U.S. 573 (1939).

much oil as rapidly as possible. This resulted in a number of production practices which frequently caused unnecessary capital expenditures and/or the loss of large quantities of oil. For example, since each producer was competing with other producers in the same reservoir, he would usually drill as many wells as possible and operate each well as long as possible. This meant that more wells would be drilled than were actually required to produce all the oil which could be produced from a reservoir; and even more significantly, it usually meant reservoir pressure would be rapidly depleted resulting in less total oil being produced from the reservoir than could have been produced if production had been coordinated. Similarly, large quantities of oil were lost in above ground earthen storage reservoirs which were used because they were the fastest and cheapest way to store the rapidly produced oil. The more modern regulatory statutes (those enacted or amended after 1930) were intended to give state regulators more power to control production practices so as to prevent losses of oil and gas, resulting from the competitive race to produce oil as rapidly as possible from each reservoir.

The methods of production control employed by various state regulators have involved a number of overlapping and/or alternative approaches. One of the earliest approaches and also one of the simplest and most widely accepted regulatory methods has been to control the number and spacing of wells. Every state which has a conservation statute expressly authorizes the control of well spacing.* A second method of regulation has been to control directly the quantity of oil and/or gas produced. In practice, this type of regulation has

*/ IOCC, A Study of Conservation of Oil and Gas in the United States, at 180 (1964).

taken two distinct forms, each of which will be discussed in greater detail below. A third method of regulation has been to authorize voluntary or compulsory unitization, and a fourth method of regulation has been to require the use of secondary recovery techniques. Many state statutes authorize one or more of these methods (several authorize all four methods), with individual states relying to varying degrees upon each method.

Direct Control of Production and "Economic Waste"

In the early years of the industry, the price of oil often was very low because producers, in their haste to capture as much oil as possible, frequently produced oil far in excess of market demand. Low prices, of course, meant little profit for the industry and also little revenue for those states which depended heavily on royalty payments and taxation of the oil industry for their income. Out of this situation emerged the concept of "economic waste", that is, the production of oil (or gas) in excess of market demand. In 1915 the Oklahoma conservation statute was amended to prohibit "economic waste" (which was not defined) and on the basis of that language, the Oklahoma regulatory agency adopted a regulatory scheme which allowed the agency to establish a statewide production limit and allocate production back to each well so that total production would not exceed that limit. Although this method of regulation effected prices (many persons charged it fixed prices), limiting production to market demand was found by the courts to be a valid method of preventing waste. Julian Oil and Royalties Co. v. Capshaw, 292 P. 841 (1930); Champlin Refining Co. v. Oklahoma Corp. Commission, 286 U.S. 210 (1932). In Texas, a 1929 amendment to the conservation statute expressly stated that the prohibition against waste was not to be construed to mean "economic waste."

After the 1929 amendment, suits were filed challenging Texas's policy of limiting oil production to market demand. In one case, the court held Texas' regulatory approach valid despite the statutory reference to "economic waste." Danciger Oil and Refining Co. v. Railroad Commission, 49 S.W.2d 837 (1932). In a second case, however, the court held that the Railroad Commission's orders were intended to prevent "economic waste", and that this was in violation of the 1929 amendment. Alfred Macmillan v. Railroad Commission, 51 F.2d 400 (1931). In response to the MacMillan decision, the Texas legislature repealed the reference to "economic waste" and authorized the prohibition of "production of crude petroleum oil in excess of transportation or market facilities or reasonable market demand". Since the MacMillan case, the practice has been to avoid use of the term "economic waste" in conservation statutes.* Rather those states which employ a market demand method of production control have adopted such a regulatory policy through the use of language similar to that in the Texas statute.**

In the light of the above legal history, it is my conclusion that the term "economic waste", when used in reference to oil and gas conservation practices, is best understood to mean regulation which limits production to market demand.***

*/ Only four state statutes use the term "economic waste." The Oklahoma and Kansas statutes each prohibit "economic waste", while the statutes of Illinois and Kentucky prohibit limitation of production to prevent or control "economic waste." IOCC, at 188-89.

**/ Ibid. at 176-79.

***/ One commentator has written: "Despite its apparent breadth, the term 'economic waste' is usually employed narrowly to mean the sale of oil or gas at a price below full cost or actual value and/or the use of oil or gas in ways which fail fully to exploit its intrinsic value". S. McDonald, Petroleum Conservation in the United States; An Economic Analysis 127 (1971).

II.

While the above discussion answers the question you have asked, I believe it might be helpful to discuss "economic waste" as the term might be defined or perceived by others. This discussion, because it is unrelated to any particular regulatory problem is general.

Direct Production Control and the Maximum Efficient Rate of Production

In those states which do not employ a market demand method of production regulation, production is regulated on a reservoir-by-reservoir basis, with total production from a reservoir being limited to the maximum efficient rate (MER). Typically, the MER is determined with respect to engineering factors rather than economic considerations. Thus, the MER is that rate which will maximize the total output of oil (in an oil reservoir). A rate which causes total oil production to diminish (because, say reservoir pressure is dissipated too rapidly) will be in excess of the MER and will not be allowed. Once the MER is established, shares of production are allocated to each producer and/or well.

Although in practice, engineering considerations have dominated the determination of the MER, it is clearly possible that economic criteria could equally be used as the efficiency criteria. If this were done, the regulatory agency might establish rates designed to maximize total present value rather than total output. Thus, at a time of declining real prices for oil (or perhaps ever slowly rising prices) the regulator might well determine that the MER was at a rate which

sacrificed future oil production for increased present production.*

There is certainly nothing express in AS 31.05 which would prevent the Conservation Committee from implementing production control using economic, rather than engineering criteria, to determine the MER. Indeed, words such as "unnecessary", "inefficient", and "excessive" might well connote economic criteria (at least to an economist) rather than engineering criteria. Nevertheless, I believe use of economic criteria, rather than engineering criteria, would represent a drastic change in regulatory practice in Alaska (and anywhere else for that matter) and thus, should only be undertaken in response to clear legislative directive in the form of amendments to the conservation statute.

Having noted that the regulatory practice in Alaska and elsewhere is to use engineering, rather than economic criteria to determine the MER, it should not go unstated that economic considerations are involved in many conservation decisions at least in a gross sense. For example, where the Conservation Committee is considering whether to require a water injection program, it certainly must compare the cost

*/ The most striking difference between the use of engineering criteria and economic criteria may occur where a reservoir contains both oil and non-associated gas, and the production of one results in a diminishment of the other which can be produced. In that case, engineering criteria might call for maximization of total hydrocarbons (BTU's) while economic criteria would call for consideration of the present and probable future value (price) of each and maximization of the present value.

It should be noted that this is not the regulatory problem you face with the Prudhoe Bay field, since (based on my understanding) hydrocarbon production can be maximized provided gas production is held within reasonable bounds (which bounds may be zero if water flood is not employed; however, in that event, the field can be blown down once oil production ceases). Thus, if one is willing to indulge the assumption that gas prices will increase at a rate at least equal to the discount rate, the MER will be the same using either engineering or economic criteria.

of such a program with the expected increase in recovered hydrocarbons. In doing so, the Conservation Committee need not adopt the economic criteria used by the producers, thus, a water injection program which the producer did not wish to undertake because the rate of return was too small (in their opinion) might still be required by the Conservation Committee. However, in the extreme case, where costs greatly exceeded any possible economic benefits to be derived, constitutional limitations likely would prevent the Committee from requiring an injection program.

Unitization of a Reservoir

One commentator has concluded that state conservation statutes "should require unitization of every oil reservoir within a reasonable time following discovery", and that such a statute "should supplant all present regulations (e.g. of well spacing and production rates) except those designed to protect other resources from damage by oil operations." The conclusion is incorrect because it embodies a false assumption (which will be discussed below) but it nevertheless highlights an important consideration. That is, by eliminating the competition among producers of oil from a reservoir, one eliminates most of the incentive to engage in "wasteful" practices. In a unitized reservoir, all producers will be better off if production is maximized.

If a unitized reservoir was unregulated, production rates would be determined in accordance with procedures adopted by the unit participants. In such case, one would expect the unit participants acting as profit maximizing entities to produce the reservoir in a fashion which

*/ S. McDonald, Unit Operation of Oil Reservoirs as an Instrument of Conservation, 49 Notre Dame Lawyer 305 (1973).

maximized the reservoir's present value.* Such rate of production likely would not correspond to the MER as determined by engineering principles. The public's interest in the production of nonrenewable oil and gas resources will correspond exactly with the producers' interest only in the hypothetical world of economists where competition is infinite and institutional constraints nonexistent. In practice, the public's interest may be served by requiring the operators of a unitized reservoir to operate at a rate different from that which they would choose on their own. For example, the unit operators may decide against fluid injection because the anticipated rate of return is too low (in their view). The public's interest, however, might best be served by requiring an injection program. Or to give another example, where oil prices are controlled, maximization of present value by the producers likely will run counter to the public's interest.

Regulators of unitized fields have in the past required maximization of hydrocarbons while considering at least in gross terms economics factors. As before, regulators could well require maximization of other objective criteria. However, I would not advise such a course of action without clear Legislative direction in the form of amendments to the present conservation statute.

*/ For various reasons in practice production rates may not be such as to maximize present value. For example, integrated producers may be facing crude shortages and willing to sacrifice future revenues while others may face a glut situation. The actual rate may represent a compromise. Some producers may want to hold back production to speculate on future market conditions, while others may prefer to follow less venturesome corporate policies. In short, producers may each have different discount rates.

Mr. Hoyle Hamilton, Director
Div. of Oil and Gas Conservation

February 14, 1977
Page 10

Sincerely,

AVRUM M. GROSS
ATTORNEY GENERAL

Frederick H. Boness

By: Frederick H. Boness
Assistant Attorney General

AHB:bvd

**PRESENTATION TO THE
HOUSE FINANCE AND
HOUSE OIL AND GAS COMMITTEES**

**KEVIN MEYERS, ARCO ALASKA, INC.
DAVE SZABO, BP EXPLORATION (ALASKA), INC.**

JANUARY 23, 1992

Impact of Major Gas Sales

- Major gas sales prior to waterflood/EOR completion (2015) do not permit simultaneous increase in field gas offtake
 - Continuing need for artificial lift prevails early in gas sales project
 - Deliverability (reservoir energy) of gas is limiting later
- Benefits of extensive field development activities implemented in 1990s to maximize liquid recovery are diminished with early major gas sales

<u>Major Gas Sales Date</u>	<u>Incremental Recovery, STB</u>
2005	-0.4 billion
1997	-1.0 billion

Engineers warn against loss of Prudhoe oil

Industry experts criticize Hickel plan to tap state's gas; commissioner disagrees

By RALPH THOMAS
Daily News reporter



Daily News file photo
Harold Heinze

JUNEAU — Oil recovery from Prudhoe Bay could fall by up to 1 billion barrels — nearly a quarter of the field's remaining recoverable reserves — if gas from the field is sold on a large scale by 1997, a pair of industry experts told state lawmakers Thursday.

But a top Hickel administration official said the industry estimate might be too drastic.

Timing of future gas sales has become a hot topic around the Capitol lately. During the past week, a pair of House committees has held three hearings focusing mostly on the same question: How

will gas sales affect oil recovery at Prudhoe Bay and other, North Slope fields?

Since his election in 1990, Gov. Wally Hickel has pushed hard for North Slope gas sales and a pipeline to carry the gas to Valdez. Some lawmakers are concerned, however, that removing the gas too soon might drastically reduce the amount of oil recovered.

The state now gets about 85 percent of its revenue from oil and gas activities, but most of it is from oil.

Oil companies use natural gas to maintain pressure that's needed to pump oil. Gas also is used as a solvent to free up substantial amounts of crude that would

not otherwise be recovered. If the gas is sold instead of being pumped back down the wells, oil recovery will decline, industry officials say.

A pair of Prudhoe Bay engineers — Dave Szabo of BP Exploration (Alaska) Inc. and Kevin Meyers of Arco Alaska Inc. — told legislators Thursday that there are about 4.4 billion barrels of recoverable oil left at Prudhoe Bay. If gas were sold on a large scale by 1997, that estimate could fall to 3.4 billion barrels, they said.

Meyers prefaced his predictions, however, by saying such estimates are based

Please see Back Page, GAS

A10 Anchorage Daily News Friday, January 24, 1992

THE BACK PAGE

GAS: Engineers say too-early sale could cost Prudhoe billion barrels

Continued from Page A-1

on "highly uncertain science."

If North Slope oil held at its current low prices — about \$15 per barrel — a 1 billion barrel recovery decline would amount to \$15 billion less earned from Prudhoe Bay.

"The benefits from gas would have to be enormous to overcome that amount of lost oil," Rep. Kay Brown, D-Anchorage, said after Thursday's joint meeting of the House Finance Committee and the Special Committee on Oil and Gas.

By waiting until the year 2005 before making major gas sales, the decline in re-

covery would be about 400 million barrels, the industry officials said.

But Harold Heinze, Hickel's natural resources commissioner and former president of Arco Alaska, said he thought the industry estimates of recovery losses were too high, though he said the state has no estimate of its own.

Heinze urged legislators to support his plan to sell part of the state's gas royalty share at Prudhoe Bay as a way of testing markets.

"More is better; sooner is better," should be the state's credo as part owner of the gas, Heinze said.

The state owns one-eighth of the 30 trillion cubic feet

of gas at Prudhoe Bay. Under Heinze's plan, the state would seek a buyer for half its royalty share and enter into a long-term contract.

Heinze said finding such a buyer wouldn't be enough to support a new pipeline, but he said it would be a start. He said the gas producers and the buyers — not the state — should pay for building a pipeline, which administration officials have estimated would cost \$11 billion.

Szabo and Meyers said their companies want to sell their North Slope gas, but not until it makes economic sense. Meyers said Arco has made no projections of when that might be.

But both industry officials supported Heinze's proposal to put part of the state's gas up for sale as a way to test markets.

In a letter Heinze sent Brown on Wednesday, he said gas sales could occur by the late 1990s and that he didn't think it would substantially hurt oil recovery.

At Thursday's hearing, however, Heinze agreed with lawmakers that the state needs to get a better understanding of the Prudhoe Bay field and how gas sales will affect oil recovery.

The oil companies now have the only up-to-date models for projecting how the reservoir will perform, and those models are kept

secret. Szabo and Meyers said the models are proprietary, but said their companies might be willing to share with the state some of the information used to create the models.

That wasn't good enough for Brown.

"I did not get a lot of comfort from what they said," Brown said. "I think it's unfortunate that the state has to rely only on the knowledge of the producers and that we don't have our own models. There's a lot at stake here; we should know some of this stuff."

Hickel and Heinze have estimated that selling North Slope gas could boost state revenue by up to \$500 mil-

lion per year.

"I can't bring you any other opportunity that starts to measure up to that potential," Heinze said.

Heinze said the state has not done a gas market analysis, but he frequently mentioned a "window of opportunity" for finding markets and getting a gasoline built.

"I've got a boss who I think can get some doors open for us," Heinze said.

Until last month, Hickel was part owner of Yukon Pacific, the company he founded in the early 1980s to build a gas pipeline. He gave up his stock, however, to settle an ethics complaint against him.

The company now says just 31 barrels were lost. There are 42 gallons of oil to the barrel.

As recently as two weeks ago, pipeline manager Bob Williams said as much as 171

frozen pipe burst.

The release was estimated at 1,006 barrels of an oil and water mixture.

The National Oceanic and Atmospheric Administration said that about 40 percent of the oil had been recovered.

very rough estimate, and Kenai Pipe Line agreed.

But DEC environmental specialist Mark Sienkiewicz said Tuesday the agency now thinks only about 16 barrels of oil were picked up

That's 672 gallons.

The agency arrived at the figure after heating the collected oil and water mixture to separate the oil from the water.

Williams said demanding news organizations had

estimates of the spill's size had been as much as 400 barrels, which is roughly 17,000 gallons.

That would have made it

Please see Page B-3, SPILL

c staff, directors els of fired chief

Post-it brand fax transmittal memo 7671 # of pages 1

To	Rep. Kay Brown
From	Jeff Laventure
Co.	Ca
Dept.	VPC
Fax #	465-2278
Fax #	265-3180

Hickel plans to test market for gas

Administration forges ahead despite pipeline setback, industry reluctance

By GEORGE FROST
Daily News reporter

The administration of Gov. Wally Hickel said it will announce today a plan to sell state-owned natural gas from the Prudhoe Bay oil field.

Harold Heinze, commissioner of natural resources, said his plan is to "test all potential gas markets, including Asia," with the state's share of the 30 trillion cubic foot bubble atop the field, the largest in North America. The state of Alaska owns one-eighth of the gas at Prudhoe Bay.

He made the statement in a letter Wednesday to Rep. Kay Brown, D-Anchorage. Heinze did not return telephone calls to discuss his idea and the letter provided few details, but it did say Heinze will discuss the plan today at a joint hearing of the House finance and oil and gas committees.

The plan comes as a surprise to state regulators who must approve or deny it.

"This is all news to me. I don't know what he is saying there," said Dave Johnston, chairman of the Alaska Oil and Gas Conservation Commission, the state agency with the authority to approve

or deny gas sales on the North Slope.

"It sounds like possibly he may be trying to do a gas sale. Or he may be trying to float royalty balloons."

As both private entrepreneur and as governor, Hickel has been the biggest promoter of building an 800-mile gas pipeline from Prudhoe Bay to Valdez, where the gas would be turned into a liquid and exported to Asia. Last month, the governor settled an ethics complaint from a special prosecutor by giving away his stock in Yukon Pacific, the company he founded in the early 1980s to build the gasline. The project has been stymied by the reluctance of the North Slope oil companies to sell gas, and by the reluctance of Japan, Korea and Taiwan to buy it.

Neither Arco Alaska nor BP Exploration (Alaska) — the two biggest North Slope operators — could be reached for comment late Wednesday, but both companies have said recently they don't want to sell any Prudhoe Bay gas before the year 2005, while the Hickel administration has been pushing for sales in the late 1990s.

The oil companies say they

need the gas to inject into the reservoir to maintain pressure to pump oil. Gas is also increasingly used as a oil-dissolving solvent that over the life of the field will free up hundreds of millions of barrels of otherwise unrecoverable crude oil.

In his letter, however, Heinze maintains that selling gas would not substantially hurt oil production. He said that, by the late 1990s, "the earliest gas sales can start," about 2 billion barrels of recoverable oil will remain in Prudhoe Bay. As a result of gas sales, up to 15 percent of that oil might be lost due to "leaving lower pressured oil in the reservoir," he wrote.

Heinze said the pressure loss could be partially made up by flooding the reservoir with water. He said gas sales ultimately would increase the recovery of oil and gas by prolonging the life of the field.

Johnston said the three-member oil and gas conservation commission may schedule public hearings to consider the proposal. He said he doubted selling the state's one-eighth royalty share of the Prudhoe gas would in itself be enough to get the project going.

PETROLEUM

An Overview of the Industry

A synopsis based on *Petroleum: Sector Report*, a complete review of the economic data describing this industry from the Alaska Economic Database

The petroleum sector is comprised of industries which produce, transport, and process Alaska's crude oil and natural gas. It also includes exploration for new oil and gas fields and investments for developing or enhancing production.

This sector accounted for more than a third of Alaska's gross state product in 1987. The petroleum sector directly employed over 10,000 workers in 1988, second only to fishing among the resource producing industries, and accounted for 5 percent of the state's employment. The same year, it paid over \$600 million, or 10 percent of the state total, in wages and salaries. Average annual wages per employee have consistently been highest in this sector: they are currently about twice as high as the state average.¹

Although the petroleum sector's share of total wages and salaries is low, it makes other important contributions to the economy. In particular state government has derived about 85 percent of its revenues from petroleum taxes and royalties over the last decade. Most production occurs on land owned by the state from which it collects a royalty. About 25 percent of the royalties are paid into the state Permanent Fund and the rest go into the state general fund.

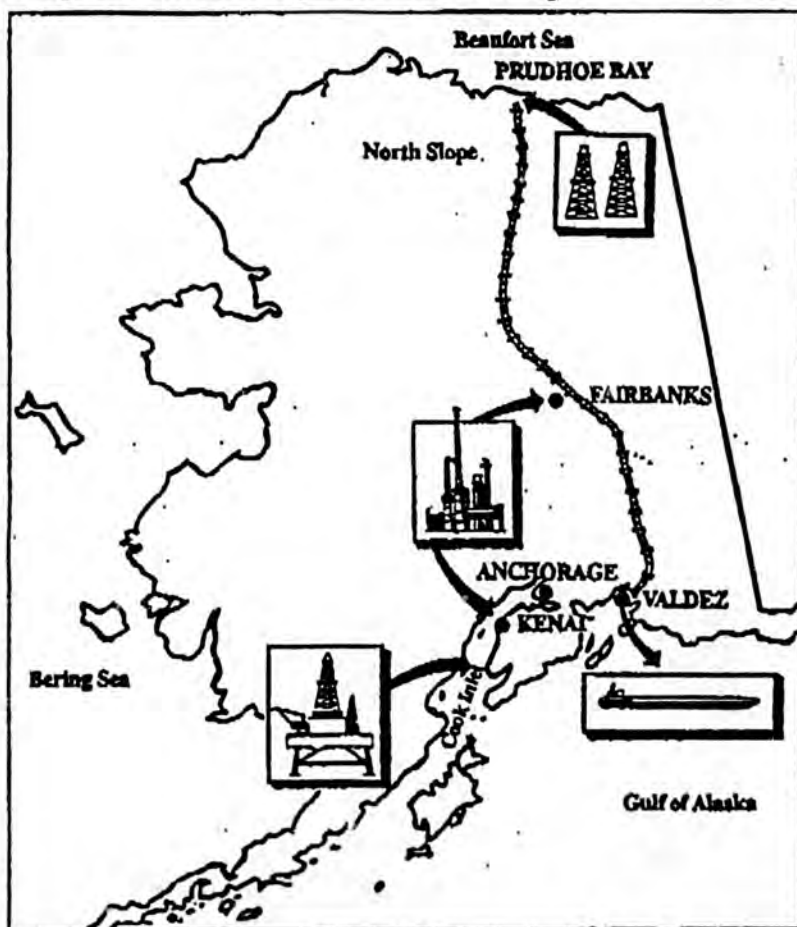
The petroleum sector extracts oil and natural gas on the North Slope and in Cook Inlet. By the end of 1988, 7.7 billion barrels and 4.5 trillion cubic feet of natural gas had been extracted from Alaska's reserves. The Prudhoe Bay oilfield on the North Slope is by far

the largest—it accounts for 20 percent of U.S. oil production and more than 3 percent of world oil production. In 1988, Alaska produced 738 million barrels of crude oil, 98 percent of which came from North Slope fields.

North Slope oil is transported via the trans-Alaska pipeline from Prudhoe Bay to Valdez, where it is loaded on tankers for shipment south. There are also several smaller oil and gas pipelines on the North Slope, in the Interior near Fairbanks and around Cook Inlet. Alaska has six oil refineries which make gasoline, diesel, jet fuel, and kerosene. Chevron and Tesoro refineries are located near Kenai; MAPCO and Petrostar refineries operate outside Fairbanks; and two small ARCO refineries process oil for use on the North Slope. Two facilities on the Kenai Peninsula which process Cook Inlet natural gas are the Phillips-Marathon liquified natural gas (LNG) and Unocal Chemical ammonia-urea plants.

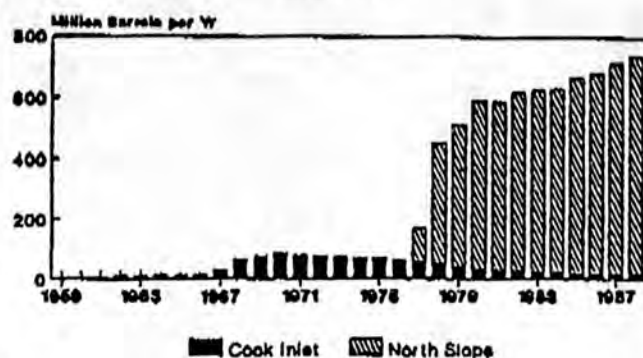
Production

As shown in Figure 1, oil production began in Cook Inlet in 1959, and peaked in



Further information on the Alaska Economic Database is available from the Division of Business Development of the Alaska Department of Commerce and Economic Development. This database was prepared under the sponsorship of the Alaska Industrial Development and Export Authority and the Alaska Department of Commerce and Economic Development by the Institute of Social and Economic Research, University of Alaska Anchorage. This overview was prepared by Marybeth Holleman of ISER.

Figure 1. Annual Crude Oil Production Cook Inlet and North Slope Regions 1959-1988



Source: Alaska Oil and Gas Conservation Commission, Statistical Reports and Bulletin.

1970 at an annual rate of 82 million barrels. Though it has gradually declined, Cook Inlet still produced 16 million barrels in 1988. North Slope fields began producing commercially in 1977, increased quickly to 700 million barrels in 1980, and slowly grew to 722 million barrels in 1988.

North Slope oil is taken mainly from the Sadlerochit field at Prudhoe Bay which, after 12 years of production, has now begun to decline. However, production from the Kuparuk River, Endicott, Lisburne, and Milne Point fields, developed in the 1980s, more than offset Prudhoe Bay's decline in the last three years. Sadlerochit oil production averaged around 1.6 million barrels per day (mmb/d) in 1988, but fell to less than 1.5 mmb/d by February 1989.

Cook Inlet oil production is dominated by the McArthur River field. All the producing Cook Inlet fields have been active for many years and are slowly declining as reserves are depleted. In 1988, Cook Inlet production ranged from 20 thousand barrels per day (mb/d) at McArthur River to 0.5 mb/d at Beaver Creek.

Alaska natural gas production averaged around 1,100 million cubic feet per day (mmcf/d) in 1988. About half this total was production on the North Slope and half was production in the Cook Inlet Region. Only about 516 mmcf/d, half the total, was marketed. Cook Inlet gas represents the major proportion of marketed natural gas production. North Slope gas is used primarily at the lease site for oil production operations, fueling pipeline pump stations, and reinjection.

Exports

Besides the petroleum processing for Alaska markets discussed earlier, a portion of Cook Inlet oil and some refined oil products such as heavy residual

oil are exported to other countries. In addition, all liquefied natural gas (LNG) and much of the fertilizer produced in Alaska are exported to Japan. The value of all petroleum sector exports fluctuated between \$300 and \$400 million dollars a year in the late 1980s.

Exploration and Development

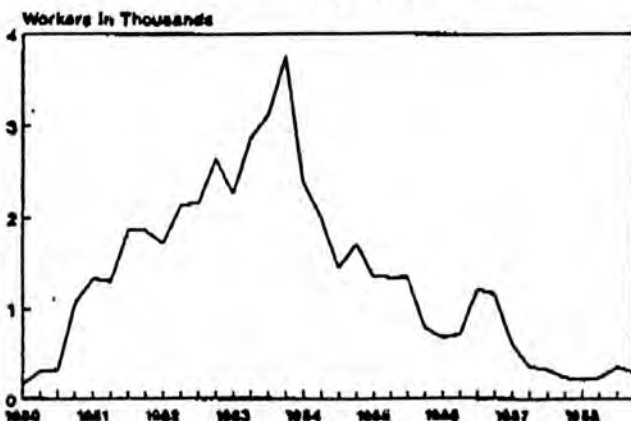
Exploration and development activities have dropped significantly since 1982. This is in part because of dropping oil prices, but also because development at several major North Slope fields has been completed. The primary indicators of exploration activities are the number of geological and geophysical crews operating in the field and the rate of exploratory drilling. For development activities, the primary indicators are the rate of development drilling and the number of people hired to build development facilities.

Exploration activity as measured by field crew months has been extremely variable. From 1958 through 1985, peak exploration activity immediately followed state and federal Outer Continental Shelf (OCS) lease sales. Lower oil prices since 1986 have discouraged exploration activity.

Throughout the 1970s and 1980s, most wells drilled have been development wells. Both exploratory and development drilling permits increased from 1970 to reach a peak in 1985 at over 300 wells, and then dropped to less than one-half that in 1987 and 1988. Exploratory wells averaged 15 to 20 per year, both onshore and offshore. In 1988, oil companies received permits to drill 12 exploratory wells. In contrast, nearly 150 permits were obtained for development wells that same year.

The volatile level of construction employment for drilling wells and constructing production facilities, pipelines, and pumping stations on the North Slope

Figure 2. Average Monthly Construction Employment, Prudhoe Bay Area, 1980-1988

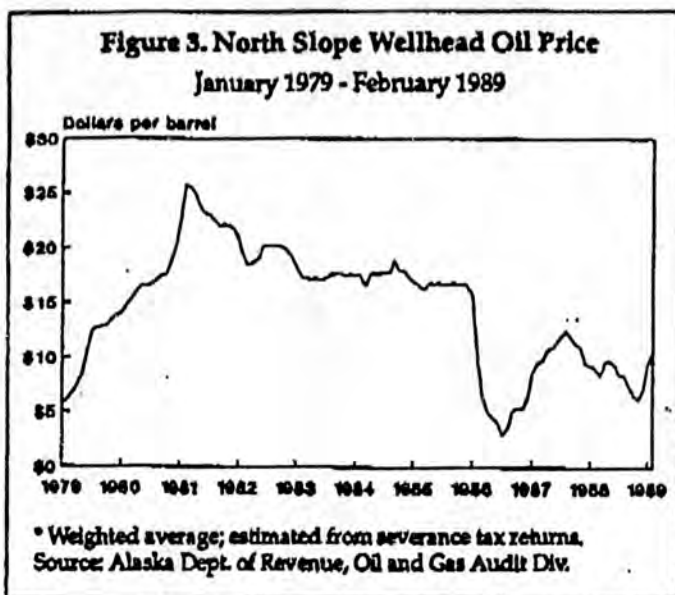


Source: Alaska Department of Labor.

is shown in Figure 2. The work force grew from a few hundred in 1980 to nearly 4,000 in late 1983, as large facilities were installed at Prudhoe Bay and Kuparuk. This number dropped back down to 1980 levels of around 300 workers by early 1988.

Prices

The price of Alaska's petroleum products is determined in worldwide markets for crude oil and its



energy substitutes. Because Alaska contributes just over 3 percent of world oil production, Alaska's production has little influence on world prices. And because the cost of transporting oil by tanker represents only a small fraction of the product's value, oil produced anywhere in the world may compete with Alaska oil.

Figure 3 shows the wellhead price of Alaska North Slope oil from 1979 through early 1989. The wellhead price is the market price minus the transportation cost, consisting of both the tanker cost and the pipeline tariff. For North Slope oil, the pipeline tariff declined from \$6 per barrel early in the 1980s to about \$3 per barrel in the late 1980s when a legal dispute over the tariff was settled.

There have been three distinct periods in Alaska wellhead prices in the past decade. In 1979, the wellhead value of North Slope oil was about \$5 per barrel. It then jumped to \$25 per barrel by 1981, while price controls kept Cook Inlet oil prices down. From 1981 to 1985 prices were stable and high. Then, in 1986, world oil prices crashed, and North Slope prices fell below \$5 per barrel. Prices between 1986 and early 1989 fluctuated between about \$6 and \$12.

On an energy-equivalent basis, world market natural gas prices have been close to oil prices. From 1979 through 1986, wellhead prices for Cook Inlet gas

remained stable at about 70 cents per thousand cubic feet (Mcf) because producers had long-term, fixed-price contracts with utility companies in southcentral Alaska. These contracts have expired and new contracts have been set at higher, more flexible prices. Current Cook Inlet prices in 1989 increased to about \$1.30 per Mcf, slightly higher than world prices.

North Slope natural gas prices do not reflect market conditions because, as noted earlier, the purchasers are also the producers. There is as yet no other market for the reserves in place there.

Employment

Figure 4 shows petroleum extraction employment. When Alaska production began in 1959, only a few hundred people worked in the petroleum industry. This grew to about 8,000 people by 1982, and has remained near this level even with dropping oil prices. Employment in the processing of oil and natural gas has steadily increased since the mid 1970s to just under 300 workers today.

Over 90 percent of Alaska's oil is transported to the Lower 48 states after passing through the trans-Alaska pipeline. Employment in the transportation of oil and gas declined from a peak of about 1,100 workers between 1978 and 1984 to just under 900 employees in the late 1980s. This figure excludes ocean tanker employment levels.

Wages

Oil field construction wages are an important cost of business for installing production facilities, pipelines, and processing plants. Average earnings of construction workers in the Prudhoe Bay area peaked at about \$7,000 per month in 1983, and then fell 40 percent before stabilizing at roughly \$4,500 per month in 1988.²

In contrast to construction wages, industry wages have continued a steady rise, from an annual average

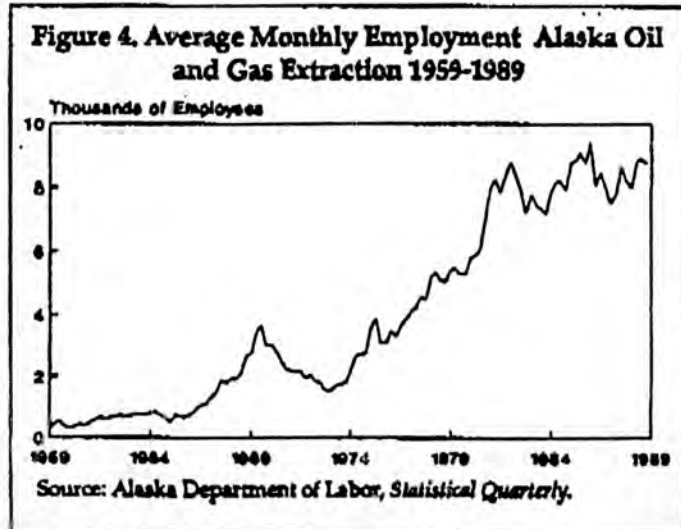
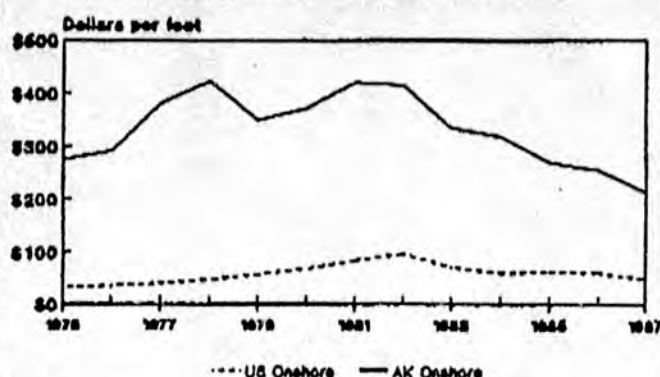


Figure 5. Estimated Average Drilling Costs, United States and Alaska 1975 - 1987



Source: Joint Assn. Survey on Drilling Costs. American Petroleum Institute.

of \$20,000 in 1974 to around \$60,000 in the late 1980s. These average annual earnings reflect trends in operating and management costs.

Costs of Production

Alaska drilling costs reflect the cost of basic exploration and field development investments. As shown in Figure 5, Alaska onshore drilling costs averaged more than \$400 a foot in the early 1980s, but had dropped to just over \$200 a foot by 1987. Even with this sharp drop, Alaska onshore drilling costs remain well above the U.S. average, which was about

\$50 a foot in 1987. Alaska offshore costs, which have usually been closer to the U.S. average, vary widely by location and reflect sporadic activity, so do not serve as a reliable indicator of changes in costs.

The major costs of transportation are pipeline tariffs and tanker rates. The pipeline tariffs are particularly important for North Slope fields, and represent the revenues received by the Alyeska Pipeline Service Company. As discussed earlier, the pipeline tariff dropped by half in the late 1980s.

The primary state tax on the petroleum industry is the production or severance tax. Effective oil severance tax rates range from zero for most Cook Inlet fields to near 15 percent for Prudhoe Bay fields. But because these rates vary widely by field and by producer, an average tax rate can't be calculated. The rate for a particular field is determined by a formula that includes the average production per well as well as total field production. The other major taxes are the petroleum property tax and the special corporate income tax on petroleum.

End Notes

1. These numbers do not include indirect contributions evidenced in other sectors, including construction, transportation, wholesale trade, financial services, business services, utilities, and state and local government.
2. These earnings data from the Alaska Department of Labor cannot be adjusted for changes in hours and overtime, so there is considerable variation.

INDUSTRY OVERVIEWS

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University of Alaska Anchorage
E. Lee Gorsuch, Director
Anchorage, Alaska 99508

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Copies of minutes listed below were originally included in this file. The minutes are available on the STAIRS database CMPR. In order to save space copies of minutes have not been left in the files.

Mary Van Nimwegen

HB 433

House Finance 1/17/92

Joint House OSG and 1/21/92
House Finance

~~House Finance~~ / -

SCOMM

79:18

(7)

Date Referred: February 18, 1992

FURTHER REFERRALS:

Resources
Judiciary

Date of Committee Action: 4/28/92

The HOUSE SPECIAL COMMITTEE ON OIL AND GAS Committee considered:

HB 501

HOUSE BILL NO. 501

OIL FINANCIAL RESPONSIBILITY LAWS

"An Act relating to evidence of financial responsibility provided by persons who conduct oil operations; and providing for an effective date."

RECOMMENDATIONS:

be replaced with CS & B 501 (O&G). ☒ the same title
☐ a new title

☐ have attached amendments(s)

☐ do pass

☐ do not pass

☐ no recommendations

☒ individual recommendations

☐ additional referral to the _____ Committee

ADOPTS: _____ letter of Intent

ATTACHES NEW FISCAL NOTE(s): (Dept)

APPROVES PREVIOUS: (Dept/Date)

☐ fiscal impact _____

☐ fiscal note(s) _____

☐ zero fiscal note _____

☐ zero fiscal note(s) _____

SIGNING <u>DO</u> PASS	DP	OTHER RECOMMENDATIONS	DNP	NR	AM
<i>Mike Savane</i>	☒				
<i>Larry Brown</i>	☒				
<i>Larry Phillips</i>	☒				
<i>Bill Hudson</i>	☒				
<i>Paul Uy</i>	☒				

Bill Hudson
CHAIRMAN'S SIGNATURE

FISCAL NOTE

STATE OF ALASKA
1992 LEGISLATIVE SESSION

BILL NO. HB 501

Revision Date: _____ Department Affected: Environmental
Title: Financial Responsibility for Oil Operations Conservation
Sponsor: Representative Foster BRU: Spill Prevention and Response
Requestor: (H) Oil and Gas Component Spill Prevention, Planning and Management

COMPONENT SERIAL NO. 1 4 3 0

EXPENDITURES/REVENUES: (Thousands of Dollars)

OPERATING	FY 93	FY 94	FY 95	FY 96	FY 97	FY 98
PERSONAL SERVICES	0.0	0.0	0.0	0.0	0.0	0.0
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND&STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0

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

REVENUE						
FUND SOURCE:						

FUNDING: (Thousands of Dollars)

GENERAL FUND	0.0	0.0	0.0	0.0	0.0	0.0
FEDERAL FUNDS						
OTHER						
FUND SOURCE:						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

POSITIONS:

FULL-TIME	0	0	0	0	0	0
PART-TIME						
TEMPORARY						

Estimate of current year impact: none

ANALYSIS: (Attach a separate page if necessary.)

Prepared by: Janice Adair

Phone: 465-5010

Division: Commissioner's Office

Date: 3/6/92

Approved by Commissioner: Janice Adair for John Sander

Agency: Environmental Conservation

Date: 3/6/92

Distribution (by preparer): Legislative Finance, Legislative Sponsor, Requestor, OMB, & Impacted Agency(ies).

TO: Representative Bill Hudson
Chairman, Oil and Gas Committee

FROM Representative Richard Foster
House District 23

SUBJECT: HB 501

As HB 501 has a companion bill SB 405, I have provided you with a quick synopsis of the current status of both bills.

HB 501 and SB 405 (Senator Hoffman) are currently identical.

SB 405 was heard yesterday in Senate Oil and Gas. Several differences between the department, the AG's office and the sponsor were identified. Basically, the major problem is "DIRECT ACTION" The department require it, the insurance companies won't provide it, therefore the non-crude operators are out of compliance and therefore subject to being shut down.

HB 501 and SB 405 propose:

1. limiting financial responsibility of insurer to maximum amount covered by insurance policy.
2. Limits the current waiver of "direct action" requirements to crude oil operations, requiring a minimum of \$50 million direct action insurance. A crude operator may obtain insurance for any amount of \$50 million from a company who does not have direct access.
2. Gives authority for DEC to waive direct action requirement for non-crude oil operation. Non-crude operators may obtain insurance from a company, however, the company may not have agreed to direct access.

The Department of Environmental Conservation propose:

1. clarifies that insurers are only liable up to the amounts specified in their policies.
2. Narrows scope to allow an injured Alaskan to sue to insurer in Alaska court, however, jurisdiction would be limited to the limits of the insurance policy.

**HB 501
FINANCIAL RESPONSIBILITY
OF NONCRUDE OPERATORS
SPONSOR STATEMENT**

In 1989, the legislature enacted strong legislation dealing with oil spill prevention and clean up standards. HB 567, which passed in 1990, made three major changes in state oil spill protection:

1. It established new response planning standards
2. Allowed Department of Environmental Conservation to give credits for incorporating prevention measures into contingency plans
3. imposed new financial responsibility requirements for contingency plan holders.

Although HB 567 was passed as a result of the Exxon Valdez oil spill and was aimed at the crude oil industry, non-crude carriers and facilities were also subject to the changes. Regulations implementing these changes have been drafted by the Department of Environmental Conservation, and are still being reviewed by the Department of Law.

PROBLEM

Smaller fuel distributors, barge lines that transport refined petroleum products, and rural electric utilities that must maintain fuel stores have found it all but impossible to meet the new financial responsibility requirements imposed by HB 567. Although these non-crude operators are able to purchase the required amounts of pollution insurance, underwriters in both the domestic and overseas markets steadfastly refuse to include the "direct action" clause in these policies that Alaska law requires.

WHY?

The insurance companies perceive the risk as far too great. With Alaska state courts seemingly allowing large direct action claims, the insurance industry feel the their liability is unlimited.

Alaska's direct action requirements have been in effect since 1981. The provision allows an action to be brought in state court directly against the insurer, rather than going first to the responsible party. Ambiguities about whether insurers are limited to the face amount of the policy, plus the greatly increased amounts of coverage required since the *Exxon Valdez* spill, have combined to produce the current unavailability of direct action coverage.

When it became clear by early 1991 that insurers would not provide direct action coverage, Senator Lyman Hoffman introduced legislation to delay the effective date of HB 567's financial responsibility requirements for non-crude operators. The hope was that over the year's time, either the insurance markets would overcome their objections to providing direct action, or that perhaps a risk pool could be developed to provide such coverage. The Legislature unanimously approved Senator Hoffman's bill.

Sen. Hoffman's legislation also delayed the effective date of the enhanced oil discharge prevention and contingency plans HB 567 required of non-crude operators; most operators appear to be prepared to meet the new requirements and no further delay in complying with them is being sought.

Nearly one year later, however, there has been no change in the insurance markets' position on direct action coverage, and development of an insurance pool so far has proved unfeasible. With the June 1, 1992, effective date of the financial responsibility requirements approaching, and the unavailability of direct action coverage just as complete as it was in 1991, non-crude operators once again face the prospect of either operating out of compliance with Alaska law or ceasing operations. The large crude oil operators do not face this problem, because they have sufficient assets and working capital to either self-insure or comply with the law through other means, such as surety bonds or letters of credit.

Over the past two years, DEC has given conditional waivers to some non-crude operators who have been unable to obtain direct action insurance but who in all other respects meet the state's financial responsibility requirements. Whether DEC has authority to grant such waivers is highly questionable, however, and the agency recently decided to end the practice.

SOLUTION

HB 501 does several things:

1. It clarifies that financial responsibility of an insurer is limited to the maximum amount covered by the insurance policy, except for traditional exceptions such as attorney fees, litigation costs, or bad faith failures to settle claims.
2. It limits the current quasi-waiver of the "direct action" requirements to crude oil operators, which requires a minimum of \$50,000 of "direct action" insurance.
3. It gives new authority to DEC to waive the "direct action" requirement for non-crude oil operations, with no minimum "direct action" insurance requirement.

CSHB 501
FINANCIAL RESPONSIBILITY
OF NONCRUDE OPERATORS
Background Paper

History: On March 24, 1989 the Exxon Valdez ran aground on Bligh Reef in Prince William Sound, causing the largest crude oil spill in United States history. As a result, the Alaska Legislature and the United States Congress significantly strengthened oil spill prevention and cleanup standards. One bill, HB 567, passed in 1990, made three major changes in state oil spill protection. It 1) established new response planning standards; 2) imposed new financial responsibility requirements for contingency plan holders; and 3) allowed the Department of Environmental Conservation to give credits for incorporating prevention measures into contingency plans. These major changes were to have gone into effect on and after June 1, 1991.

Although HB 567 was passed as a result of the Exxon Valdez oil spill and was aimed at the crude oil industry, non-crude carriers and facilities were also subject to the changes. Regulations implementing these changes have been drafted by the Department of Environmental Conservation, and are still being reviewed by the Department of Law.

Problem: Smaller fuel distributors, barge lines that transport refined petroleum products, and rural electric utilities that must maintain fuel stores have found it all but impossible to meet the new financial responsibility requirements imposed by HB 567. Although these non-crude operators are able to purchase the required amounts of pollution insurance, underwriters in both the domestic and overseas markets steadfastly refuse to include the "direct action" clause in these policies that Alaska law requires.

Alaska's direct action requirements have been in effect since 1981. The provision allows an action to be brought in state court directly against the insurer, rather than going first to the responsible party.

Ambiguities about whether insurers are limited to the face amount of the policy, plus the greatly increased amounts of coverage required since the Exxon Valdez spill, have combined to produce the current unavailability of direct action coverage.

When it became clear by early 1991 that insurers would not provide direct action coverage, Senator Lyman Hoffman introduced legislation to delay the effective date of HB 567's financial responsibility requirements for non-crude operators. The hope was that over the year's time, either the insurance markets would overcome their objections to providing direct action, or that perhaps a risk pool could be developed to provide such coverage. The Legislature unanimously approved Senator Hoffman's bill.

Sen. Hoffman's legislation also delayed the effective date of the enhanced oil discharge prevention and contingency plans HB 567 required of non-crude operators; most operators appear to be prepared to meet the new requirements and no further delay in complying with them is being sought at this time.

Nearly one year later, however, there has been no change in the insurance markets' position on direct action coverage, and development of an insurance pool so far has proved unfeasible. With the June 1, 1992, effective date of the financial responsibility requirements approaching, and the unavailability of direct action coverage just as complete as it was in 1991, non-crude operators once again face the prospect of either operating out of compliance with Alaska law or ceasing operations. The large crude oil operators do not face this problem, because they have sufficient assets and working capital to either self-insure or comply with the law through other means, such as surety bonds or letters of credit.

Over the past two years, DEC has given conditional waivers to some non-crude operators who have been unable to obtain direct action insurance but who in all other respects meet the state's financial responsibility requirements. Whether DEC has authority to grant such waivers is highly questionable, however, and the agency recently decided to end the practice.

Solution: CS HB 501 (O&G) does several things:

- Section 1 clarifies that the financial responsibility of an insurer is limited to the type of risk assumed and the amount of coverage specified in the proof of financial responsibility. It also clarifies that these limits do not apply to an applicant who self-insures.
- Section 2 gives new authority to DEC to approve an applicant's proof of financial responsibility if the applicant attests in a sworn statement that direct action insurance has been diligently sought, but is determined to be unavailable; if such efforts are made and proven every six months; and if all other financial responsibility requirements are met.
- Sections 3 and 4 ratify similar exemptions made by DEC during the past year.
- Sections 5,6 and 7 calls for an immediate effective date; if that date is after June 1, 1992, makes it retroactive to June 1, 1992; and repeals the exemption law on June 1, 1994.
- Letter of intent adopted by the Senate Oil and Gas Committee directs DEC, the Division of Insurance within Commerce Department, and the Legislative Research Agency to research possible alternative solutions to assist non-crude operators in meeting the state's financial responsibility requirements for oil spill pollution coverage.

CS HB 501 (O&G) Sectional Analysis

- **Section 1** clarifies that the financial responsibility of an insurer is limited to the type of risk assumed and the amount of coverage specified in the proof of financial responsibility. It also clarifies that these limits do not apply to an applicant who self-insures.
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- **Sections 3 and 4** ratify similar exemptions made by DEC during the past year.
- **Sections 5,6 and 7** calls for an immediate effective date; if that date is after June 1, 1992, makes it retroactive to June 1, 1992; and repeals the exemption law on June 1, 1994.
- A letter of intent adopted has been adopted by the Senate Oil and Gas Committee to the companion bill SB 405. This letter directs DEC, the Division of Insurance within Commerce Department, and the Legislative Research Agency to research possible alternative solutions to assist non-crude operators in meeting the state's financial responsibility requirements for oil spill pollution coverage.

adopted

Revised Letter of intent to SB 405:

The Department of Environmental Conservation, the Division of Insurance within the Department of Commerce and Economic Development, and the Legislative Research Agency shall research the possibility of group pooling or other mechanisms to assist non-crude operators in meeting the state's financial responsibility requirements for oil spill pollution coverage, and shall report back to the Legislature with their findings and recommendations by February 1, 1993.

letter of intent adopted by Senate (orig)
for companion bill SB 405



Senator Lyman F. Hoffman

Alaska State Senate

P.O. Box V • Juneau, Alaska 99811 • (907) 465-4453

District M
Akiachak
Akiak
Alatna
Aliakaket
Andreasky
Aniak
Anvik
Arctic Village
Atmautluak
Beaver
Bethel
Bettles
Birch Creek
Chaikyltsik
Chefnak
Chuathcuk
Crooked Creek
Eek
Evansville
Fort Yukon
Galena
Goodnews Bay
Graying
Holy Cross
Hughes
Huslia
Kaiskag
Kaitag
Kasiguk
Kionuk
Kongiganak
Kovukuk
Kwethuk
Kwigillingok
Lake Minchumina
Lime Village
Lower Kaiskag
Manley Hot Springs
Marshfield
McGrath
Mekoryuk
Minto
Mountain Village
Napakiak
Napaskiak
Newtok
Nightmute
Nikolai
Nulato
Nunapitchuk
Oscarville
Pilot Station
Pitkas Point
Platinum
Quinhagak
Rampart
Red Devil
Ruby
Russian Mission
Shageluk
Sleetmute
St. Mary's
Stevens Village
Stony River
Takotna
Tanana
Telida
Toksook Bay
Tuluksak
Tuntutuliak
Tununguk
Tyonek
Venetie
Wesley

SB 405 FINANCIAL RESPONSIBILITY OF NONCRUDE OPERATORS Background Paper

History: On March 24, 1989 the *Exxon Valdez* ran aground on Bligh Reef in Prince William Sound, causing the largest crude oil spill in United States history. As a result, the Alaska Legislature and the United States Congress significantly strengthened oil spill prevention and cleanup standards. One bill, HB 567, passed in 1990, made three major changes in state oil spill protection. It 1) established new response planning standards; 2) imposed new financial responsibility requirements for contingency plan holders; and 3) allowed the Department of Environmental Conservation to give credits for incorporating prevention measures into contingency plans. These major changes were to have gone into effect on and after June 1, 1991.

Although HB 567 was passed as a result of the *Exxon Valdez* oil spill and was aimed at the crude oil industry, non-crude carriers and facilities were also subject to the changes. Regulations implementing these changes have been drafted by the Department of Environmental Conservation, and are still being reviewed by the Department of Law.

Problem: Smaller fuel distributors, barge lines that transport refined petroleum products, and rural electric utilities that must maintain fuel stores have found it all but impossible to meet the new financial responsibility requirements imposed by HB 567. Although these non-crude operators are able to purchase the required amounts of pollution insurance, underwriters in both the domestic and overseas markets steadfastly refuse to include the "direct action" clause in these policies that Alaska law requires.

Alaska's direct action requirements have been in effect since 1981. The provision allows an action to be brought in state court directly against the insurer, rather than going first to the responsible party. Ambiguities about whether insurers are limited to the face amount of the policy, plus the greatly increased amounts of coverage required since the *Exxon Valdez* spill, have combined to produce the current unavailability of direct action coverage.

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Over the past two years, DEC has given conditional waivers to some non-crude operators who have been unable to obtain direct action insurance but who in all other respects meet the state's financial responsibility requirements. Whether DEC has authority to grant such waivers is highly questionable, however, and the agency recently decided to end the practice.

Solution: SB 405 does several things:

- It clarifies that financial responsibility of an insurer is limited to the maximum amount covered by the insurance policy, except for traditional exceptions such as attorney fees, litigation costs, or bad faith failures to settle claims.

- It limits the current quasi-waiver of the "direct action" requirement to crude oil operations, which requires a minimum of \$50,000,000 of "direct action" insurance.

- It gives new authority to DEC to waive the "direct action" requirement for non-crude oil operations, with no minimum "direct action" insurance requirement.

DIVISION OF LEGAL SERVICES

LEGISLATIVE AFFAIRS AGENCY STATE OF ALASKA

(907) 465-3867 or 465-2450
FAX (907) 465-2029
Mail Stop 3101

240 Main Street, Suite 500
Juneau, Alaska 99801-2101

MEMORANDUM

February 24, 1992

SUBJECT: Sectional Analysis (SB 405)

TO: Senator Lyman Hoffman

FROM: Terri Lauterbach 
Legislative Counsel

Following is a sectional analysis of SB 405, a bill relating to financial responsibility laws affecting the oil industry:

Section 1 clarifies the extent of liability borne by an insurance carrier or P & I group that agrees to help an insured demonstrate financial responsibility. While the first sentence of this section (current law) demands that the financial responsibility extend to certain types of losses and assessments, the second sentence (new law) limits the amount of exposure of the insurer or group to the face amount of the policy issued or the group's agreement. Full liability for amounts above the insurance policy would be borne by the person who is insured.

This clarification is intended to address a fear that has reportedly been expressed by insurers and P & I clubs. As I understand it, they have feared that their exposure might be unlimited, regardless of what the face amount of their policy or agreement is. DEC tried to address this fear in its regulations, but the insurers and clubs have reportedly not been satisfied that DEC has such authority to interpret the law's intent.

This section is made retroactive by sec. 6. Retroactivity will have the effect of ratifying DEC's practice of requiring a "face amount" endorsement on policies and agreements since the effective date of the new financial responsibility requirements -- June 1, 1991.

Section 2 amends a subsection of current law under which DEC can accept some evidence of financial responsibility that does not allow for an action to be filed directly against the insurer as long as the applicant shows that the first \$50 million of liability is covered by "direct action" insurance. The applicant must also show that

Senator Lyman Hoffman
February 24, 1992
Page 2

additional "direct action" insurance is unavailable. The amendment limits the applicability of this section to crude oil operations.

Section 3 enacts a new subsection of law that applies only to noncrude oil operations. The new law would allow DEC to accept evidence of financial responsibility that does not allow for an action to be filed directly against the insurer without any minimum amount of "direct action" insurance being provided. The applicant would still have to show that "direct action" insurance is unavailable.

Section 4 repeals the new noncrude "direct action" exemption of section 3 in 1994.

Section 5 repeals a 1991 session law that provides that all of the new 1990 changes in financial responsibility laws apply on June 1, 1992, to noncrude operators. The repeal is necessary because SB 405 would make changes in the 1990 Act. If SB 405 passes, it would no longer be true that all of the 1990 changes will apply to noncrudes in 1992. They will all apply, except as amended by SB 405.

Section 6 makes sections 1 - 3 of this bill retroactive to June 1, 1991 (the effective date of the new financial responsibility laws passed in 1990). This will ratify actions taken by DEC since that date that may have been done with questionable authority with respect to "face amount" endorsements and waiver of the "direct action" requirement for noncrudes.

Section 7 ensures that the repealer of section 5 will apply as of June 1, 1992, even if the governor signs SB 405 after June 1. This will cover transmittal delays and the delay involved in reviewing bills before the governor signs them. Without this section, late signing of SB 405 could mean that for some time period the full financial responsibility changes made in 1990 would apply to noncrude operations without the amendments made by SB 405.

Section 8 gives SB 405 an immediate effective date.

I hope you find this description helpful. Please let me know if you have further questions.

TML:pl
92-125.plm

CS FOR HOUSE BILL NO. 501 (O&G)

IN THE LEGISLATURE OF THE STATE OF ALASKA

SEVENTEENTH LEGISLATURE - SECOND SESSION

BY THE HOUSE SPECIAL COMMITTEE ON OIL AND GAS

Offered:

Referred:

Sponsor(s): REPRESENTATIVES FOSTER, Lincoln, G.Phillips

A BILL

FOR AN ACT ENTITLED

1 "An Act relating to evidence of financial responsibility provided by persons who conduct
2 oil operations; and providing for an effective date."

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

4 * Section 1. AS 46.04.040(e) is amended to read:

5 (e) Financial responsibility may be demonstrated by (1) self-insurance, (2) insurance, (3)
6 surety, (4) guarantee, (5) letter of credit approved by the department, or (6) other proof of
7 financial responsibility approved by the department, including proof of financial responsibility
8 provided by a group of insureds who have agreed to cover pollution risks of members of the
9 group under terms the department may prescribe. An action brought under AS 46.03.758,
10 46.03.759, 46.03.760(a) or (e), 46.03.822, or as 46.04.030(g) may be brought in a state court
11 directly against the insurer, the group, or another person providing evidence of financial
12 responsibility; however, the liability under this section of a third-party insurer is limited to
13 the type of risk assumed and the amount of coverage specified in the proof of financial
14 responsibility furnished to and approved by the department. The applicant, and an insurer,

surety, guarantor, person furnishing an approved letter of credit, or other group or person providing proof of financial responsibility approved by the department shall appoint an agent for service of process in the state. For purposes of this subsection, an insurer, other than a group of insureds whose agreement has been approved by the department, must either be authorized by the Department of Commerce and Economic Development to sell insurance in the state or be an unauthorized insurer listed by the Department of Commerce and Economic Development as not disapproved for use in the state. In this subsection, "third-party insurer" means a third-party insurer, surety, guarantor, person furnishing a letter of credit, or other group or person providing proof of financial responsibility on behalf of an applicant under this section; "third-party insurer" does not include the applicant.

* Sec. 2. TEMPORARY LAW APPLICABLE TO NONCRUDE OIL OPERATIONS.

Notwithstanding AS 46.04.040, the Department of Environmental Conservation may, with respect to noncrude oil operations, approve proof of financial responsibility by a person, other than the applicant, who does not agree to be subject to a direct action in the state or to appoint an agent for service of process if the applicant

(1) provides proof of financial responsibility in the form and amounts otherwise required under AS 46.04.040;

(2) provides a sworn statement that

(A) is acceptable to the department;

(B) attests that the applicant has diligently attempted to obtain a form of proof of financial responsibility that would provide for a direct action and appointment of an agent for service of process;

(C) describes the steps the applicant has taken to obtain a form of proof of financial responsibility that would provide for a direct action and appointment of an agent for service of process;

(D) states that a form of proof of financial responsibility that would provide for a direct action and appointment of an agent for service of process is unavailable to the applicant;

(3) continues diligent efforts to obtain a form of proof of financial responsibility that would provide for a direct action and appointment of an agent for service of process and provides a sworn statement every six months that is acceptable to the department, containing the information required in (2) of this section.

1 * Sec. 3. RATIFICATION OF PREVIOUS EXEMPTIONS GIVEN BY DEPARTMENT OF
2 ENVIRONMENTAL CONSERVATION TO NONCRUDE OIL OPERATIONS. Notwithstanding
3 AS 46.04.040, the Department of Environmental Conservation may, with respect to noncrude oil
4 operations, approve proof of financial responsibility by a person, other than the applicant, who does not
5 agree to be subject to a direct action in the state or to appoint an agent for service of process if the
6 applicant, before June 1, 1992,

7 (1) provides proof of financial responsibility in the form and amounts otherwise required
8 under AS 46.04.040;

9 (2) attests in a statement to the department that the applicant has diligently attempted to
10 obtain a form of proof of financial responsibility that would provide for a direct action and appointment
11 of an agent for service of process and that this form of proof is unavailable to the applicant; and

12 (3) agrees to continue diligent efforts to obtain a form of proof of financial responsibility
13 that would provide for a direct action and appointment of an agent for service of process.

14 * Sec. 4. Section 3 of this Act is retroactive to June 1, 1991.

15 * Sec. 5. If this Act takes effect after June 1, 1992, sec. 2 of this Act is retroactive to June 1, 1992.

16 * Sec. 6. Section 2 of this Act is repealed June 1, 1994.

17 * Sec. 7. This Act takes effect immediately under AS 01.10.070(c).

STATE OF ALASKA

DEPARTMENT OF LAW

OFFICE OF THE ATTORNEY GENERAL

WALTER J. HICKEL, GOVERNOR

REPLY TO:

☒ 1031 W 4TH AVENUE, SUITE 200
ANCHORAGE, ALASKA 99501-1954
PHONE: (907) 269-5100
FAX: (907) 273-3697

☐ KEY BANK BUILDING
100 CUSHMAN ST., SUITE 400
FAIRBANKS, ALASKA 99701-4679
PHONE: (907) 452-1558
FAX: (907) 458-1317

☐ P.O. BOX K - STATE CAPITOL
JUNEAU, ALASKA 99811-0300
PHONE: (907) 465-3500
FAX: (907) 463-5295

February 24, 1992

The Honorable Lyman Hoffman
Alaska State Senate
Room 510, Capitol
P.O. Box V
Juneau, AK 99811

RE: SB 405 DEC Alternative

Dear Senator Hoffman:

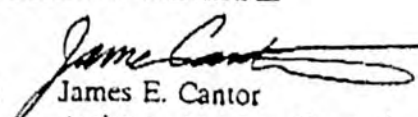
I am enclosing an alternative to SB 405 which the Department of Environmental Conservation would like to propose for consideration. SB 405 deals with the oil spill financial responsibility requirements which oil facility operators must meet. SB 405 was proposed because operators are generally no longer able to obtain insurance which complies with state law. SB 405 puts a two year moratorium on the financial responsibility requirements.

The attached alternative does not propose a moratorium. Instead, the alternative directly addresses the insurance industry's reasons for not writing policies. The most important points in the proposal are contained in subsection (j).

Subsection (j) clarifies that insurers are only liable under AS 46.04.040 up to the amounts specified in their policies. With subsection (j), the financial responsibility law could not subject an insurer to unlimited liability.

Subsection (j) also narrows the potential scope of the current direct action requirement. Subsection (j) would allow an injured Alaskan to sue the insurer in Alaska court, as is currently allowed. However, jurisdiction would be limited so that an insurer appearing pursuant to this section could not be sued for additional damages, above and beyond the limits of the insurance policy.

CHARLES E. COLE
ATTORNEY GENERAL

By: 
James E. Cantor
Assistant Attorney General

JEC:bnk

Encl

cc: Janice Adair
Deborah Behr

MEM: AG's Office - Jim Cantor

TO: Glenn Adams JUNEAU/ADEC

DATE: 02-20-92

TIME: 16:00

CC:

SUBJECT: Financial Responsibility

PRIORITY: R

ATTACHMENTS: fr

Glenn: I am attaching a copy of our proposal for tightening up AS
46.04.040. Look particularly a subsection (j). Please call me if you have
any comments. Also, I sent a copy of Sen. Hoffman's bill (SB 405) via fax to
Lynn.

Jim Cantor

=====

oil barge has furnished to the department, and the department has approved, proof of financial ability to respond in damages. Proof of financial responsibility required under this subsection is

(1) \$300, per incident, for each barrel of storage capacity or \$100,000,000, whichever is greater, for a tank vessel or barge carrying crude oil;

(2) \$100, per incident, for each barrel of storage capacity or \$1,000,000, whichever is greater, subject to a maximum of \$35,000,000, for a tank vessel or barge carrying noncrude oil.

~~[(d) Except as provided in (k) of this section, it is not a defense to an action brought for violation of (a) (c) of this section that the person charged believed in good faith that proof of financial ability to respond in damages had been furnished to, and approved by, the department.]~~

Current subsection (d) concerns defending against actions brought for violation AS 46.04.040. In this proposal, current subsection (d) has been moved and combined below with subsection (k), which addresses the same topic.

(d) ~~[(e)]~~ Financial responsibility may be demonstrated by (1) self-insurance, (2) insurance, (3) surety, (4) guarantee, (5) letter of credit approved by the department, or (6) other proof of financial responsibility approved by the department, including proof of financial responsibility provided by a group of insureds who have agreed to cover pollution risks of members of the group under terms the department may prescribe. ~~[An action brought under AS 46.03.758, 46.03.759, 46.03.760(a) or (e), 46.03.822, or AS 46.04.030(g) may be brought in a state court directly against the insurer, the group, or another person providing evidence of financial responsibility. The applicant, and an insurer, surety,~~

~~guarantor, person furnishing an approved letter of credit, or other group or person providing proof of financial responsibility approved by the department shall appoint an agent for service of process in the state.]~~ For purposes of this subsection, an insurer, other than a group of insureds whose agreement has been approved by the department, must either be authorized by the Department of Commerce and Economic Development to sell insurance in the state or be an unauthorized insurer listed by the Department of Commerce and Economic Development as not disapproved for use in the state.

The deleted portions of current subsection (e) have been moved to proposed subsection (j), below.

(e) Upon acceptance and approval of proof of financial responsibility under this section, the department shall issue to the applicant a certificate stating that the state's financial responsibility requirements have been satisfied. The certificate must include the name of the facility, pipeline, tank vessel, or oil barge for which it is issued and the expiration date of the certificate.

Proposed subsection (e) is exactly the same as current subsection (j). This organizational change is proposed to aid the readability and logic of this increasingly complex statute.

- (f) Acceptance of proof of financial responsibility expires
- (1) one year from its issuance for self-insurance;
 - (2) on the effective date of change in the surety bond, guarantee, insurance agreement, letter of credit, or other proof of financial responsibility; or
 - (3) on the expiration or cancellation of the surety bond, guarantee, insurance agreement, letter of credit, or other proof of financial responsibility.