

SCOMM

96:9

FISCAL NOTE

STATE OF ALASKA
1995 LEGISLATIVE SESSION

BILL NO. HB 207

Revision Date: 3/14/95 Dept. Affected: Revenue
Title: Adjustments to Oil and Gas Royalty BRU: Revenue Operations
Sponsor: (H) Rules Component: Oil & Gas Audit
Requester: Governor COMPONENT SERIAL NO. 115

Expenditures/Revenues

(Thousands of Dollars)

OPERATING EXPENDITURES	FY 96	FY 97	FY 98	FY 99	FY 00	FY 01
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	*	*	*	*	*	*

CAPITAL EXPENDITURES						
----------------------	--	--	--	--	--	--

CHANGE IN REVENUES ()	*****See Analysis*****
------------------------	------------------------

FUND SOURCE

(Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1006 GF/MHTIA						
Other						
TOTAL	*	*	*	*	*	*

Estimate of any current year (FY95) cost: \$ _____

POSITIONS

FULL-TIME						
PART-TIME						
TEMPORARY						

ANALYSIS: (Attach a separate page if necessary)

This Bill would grant the Commissioner of Natural Resources broad authority to reduce the royalty terms of an oil and gas lease if such reduction would allow new commercial development, prolong field life, or reestablish commercial production from idle leases. The reduction could be no greater than the percentage required to deposit royalty income under the initial lease terms into the permanent fund. The net impact of this provision will be to insure that the permanent fund share under the original lease terms will be covered in the event of reduction in royalty rate. In theory, the ability to grant royalty relief should raise the cash bids on new leases.

New production from this royalty reduction would most likely pay little severance tax because the Economic Limit Factor is designed to provide almost total tax relief to the kind of marginal fields this legislation is aimed at benefiting. Each new barrel of production would be subject to the \$.05/bbl or \$.03/bbl hazardous release surcharge (depending on the balance in the 470 fund) and the \$.004/bbl conservation tax. The impact on the corporate income tax would be too small to measure because of the world-wide apportioned tax base and since hft definition these fields would have marginal profitability.

Prepared by: Chuck Logsdon Phone: 277-5627
Division: Oil and Gas Audit Division Date: 3/14/95
Approved by Commissioner: Deborah Vogt Date: 3/15/95
Agency: Revenue

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FISCAL NOTE

No. 3*Corrected*Bill Version: HB 207(H) Publish Date: 3/8/95

STATE OF ALASKA

1995 LEGISLATIVE SESSION

Revision Date: OriginalDept Affected: Natural ResourcesTitle: An Act relating to adjustments to royalty reserved to the state to encourage otherwise uneconomic production of oil and ...BRU: Resource DevelopmentComponent: Oil & Gas DevelopmentSponsor: House Rules CommitteeRequestor: Governor KnowlesComponent Serial No. 439

Expenditures/Revenues

(Thousands of Dollars)

OPERATING EXPENDITURES	FY96	FY97	FY98	FY99	FY00	FY01
PERSONAL SERVICES	90.6	94.0	97.5	101.2	105.0	108.9
TRAVEL	5.0	5.0	5.0	5.0	5.0	5.0
CONTRACTUAL	5.0	5.0	5.0	5.0	5.0	5.0
SUPPLIES	5.0	5.0	5.0	5.0	5.0	5.0
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	105.6	109.0	112.5	116.2	120.0	123.9
CAPITAL EXPENDITURES	0.0	0.0	0.0	0.0	0.0	0.0
CHANGE IN REVENUES ()	0.0	0.0	0.0	0.0	0.0	0.0

FUND SOURCE

(Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF	105.6	109.0	112.5	116.2	120.0	123.9
1005 GF/Program Receipts						
1006 GF/MHTIA						
Other						
TOTAL	105.6	109.0	112.5	116.2	120.0	123.9

Estimate of any current year (FY95) cost: \$

None

POSITIONS

FULL-TIME	1	1	1	1	1	1
PART-TIME	0	0	0	0	0	0
TEMPORARY	0	0	0	0	0	0

ANALYSIS:

(Attach a separate page if necessary)

SEE ATTACHED

Prepared by: Ken Boyd, Acting DirectorPhone: 762-2547Division: Oil & GasDate: 3-Mar-95Approved by Commissioner: *John Stively*Date: 3-7-95Agency: Natural Resources

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ATTACHMENT FOR FISCAL NOTE - HB207
REDUCE ROYALTY SHARE/HOLD PERMANENT FUND "HARMLESS"

Implementation of this legislation will create an increased workload for the Division of Oil & Gas. We anticipate that some of the applications will be analyzed within the Division and many will require analysis by third parties (the bill provides that third-party costs will be paid for by the companies). Because of the extremely sensitive and confidential nature of the data a considerable amount of interaction between the third-party contractor and the state will be needed. Furthermore, the bill requires that applicants make a clear and convincing showing of the need for royalty reduction, so the Division will need to evaluate the economic, geological and engineering data submitted for compliance with the law prior to seeking the assistance of a third party.

Because this legislation contains provisions that may cause the terms of the application to vary over time, any approved application will need to be monitored on a continuing basis. We expect this program to have broad appeal, however, we cannot anticipate how many applications will be submitted or when they will be submitted.

An exempt Petroleum Engineer, Range 26A, will provide the broad background that will be needed to evaluate these proposals effectively. This position will need to be skilled not only in Petroleum Engineering, but will also need to have extensive knowledge of petroleum geology and petroleum economics. The salary cost of this position will be approximately \$90.6 the first year, including benefits. Additional, minor expenses such as travel, contractual and supplies will be required which we estimate will not exceed \$15.0. This position and the associated costs are our estimates of the funding needed to get the program started; if many applications are received, other positions may be required. We assume that each application will take between 4-6 employee-months to evaluate.

This legislation will effect state operating revenues in an unquantifiable manner (the Permanent Fund share is not affected by this legislation). This legislation gives the commissioner authority to grant royalty reduction which, on its face, would seem to indicate a decrease in revenue. However, since the purpose of this legislation is to promote development of fields that would not otherwise be produced, the net effect on state revenues should be positive. As a result of this legislation we are gaining new revenues based on this new production (albeit at a somewhat reduced rate from currently producing fields).

FISCAL NOTE

STATE OF ALASKA

BILL NO. HB207

1995 LEGISLATIVE SESSION

Revision Date: Original Dept Affected: Natural Resources
 Title: An Act relating to adjustments to royalty reserved to BRU: Resource Development
the state to encourage otherwise uneconomic production of oil and ... Component: Oil & Gas Development
 Sponsor: House Rules Committee
 Requestor: Governor Knowles Component Serial No. 439

Expenditures/Revenues

(Thousands of Dollars)

OPERATING EXPENDITURES	FY96	FY97	FY98	FY99	FY00	FY01
PERSONAL SERVICES	90.6	94.0	97.5	101.2	105.0	108.9
TRAVEL	5.0	5.0	5.0	5.0	5.0	5.0
CONTRACTUAL	5.0	5.0	5.0	5.0	5.0	5.0
SUPPLIES	5.0	5.0	5.0	5.0	5.0	5.0
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	105.6	109.0	112.5	116.2	120.0	123.9

CAPITAL EXPENDITURES	0.0	0.0	0.0	0.0	0.0	0.0
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CHANGE IN REVENUES ()	0.0	0.0	0.0	0.0	0.0	0.0
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FUND SOURCE

(Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1006 GF/MHTIA						
Other						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

Estimate of any current year (FY95) cost: \$ None

POSITIONS

FULL-TIME	1	1	1	1	1	1
PART-TIME	0	0	0	0	0	0
TEMPORARY	0	0	0	0	0	0

ANALYSIS:

(Attach a separate page if necessary)

SEE ATTACHED

Prepared by: Ken Boyd, Acting Director Phone: 762-2547
 Division: Oil & Gas Date: 3-Mar-95
 Approved by Commissioner: [Signature] Date: 3-6-95
 Agency: Natural Resources

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**ATTACHMENT FOR FISCAL NOTE - HB207
REDUCE ROYALTY SHARE/HOLD PERMANENT FUND "HARMLESS"**

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Because this legislation contains provisions that may cause the terms of the application to vary over time, any approved application will need to be monitored on a continuing basis. We expect this program to have broad appeal, however, we cannot anticipate how many applications will be submitted or when they will be submitted.

An exempt Petroleum Engineer, Range 26A, will provide the broad background that will be needed to evaluate these proposals effectively. This position will need to be skilled not only in Petroleum Engineering, but will also need to have extensive knowledge of petroleum geology and petroleum economics. The salary cost of this position will be approximately \$90.6 the first year, including benefits. Additional, minor expenses such as travel, contractual and supplies will be required which we estimate will not exceed \$15.0. This position and the associated costs are our estimates of the funding needed to get the program started; if many applications are received, other positions may be required. We assume that each application will take between 4-6 employee-months to evaluate.

This legislation will effect state operating revenues in an unquantifiable manner (the Permanent Fund share is not affected by this legislation). This legislation gives the commissioner authority to grant royalty reduction which, on its face, would seem to indicate a decrease in revenue. However, since the purpose of this legislation is to promote development of fields that would not otherwise be produced, the net effect on state revenues should be positive. As a result of this legislation we are gaining new revenues based on this new production (albeit at a somewhat reduced rate from currently producing fields).

FISCAL NOTE

No. 3

Bill Version: HB 207

(H) Publish Date: 2/27/95

STATE OF ALASKA

1995 LEGISLATIVE SESSION

Revision Date: Original

Dept Affected: Natural Resources

Title: Reduce royalty share/hold permanent
fund "harmless"

BRU: Resource Development

Component: Oil & Gas Development

Sponsor:

Requestor: Governor

Component Serial No.

439

Expenditures/Revenues

(Thousands of Dollars)

OPERATING EXPENDITURES	FY96	FY97	FY98	FY99	FY00	FY01
PERSONAL SERVICES	90.6	94.0	97.5	101.2	105.0	108.9
TRAVEL	5.0	5.0	5.0	5.0	5.0	5.0
CONTRACTUAL	5.0	5.0	5.0	5.0	5.0	5.0
SUPPLIES	5.0	5.0	5.0	5.0	5.0	5.0
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	105.6	109.0	112.5	116.2	120.0	123.9

CAPITAL EXPENDITURES	0.0	0.0	0.0	0.0	0.0	0.0
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CHANGE IN REVENUES ()	0.0	0.0	0.0	0.0	0.0	0.0
-------------------------------	------------	------------	------------	------------	------------	------------

FUND SOURCE

(Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1006 GF/MHTIA						
Other						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

Estimate of any current year (FY95) cost: \$

None

POSITIONS

FULL-TIME	1	1	1	1	1	1
PART-TIME	0	0	0	0	0	0
TEMPORARY	0	0	0	0	0	0

ANALYSIS:

(Attach a separate page if necessary)

SEE ATTACHED

Prepared by: Ken Boyd, Acting Director

Division: Oil & Gas

Approved by Commissioner: John Smith

Agency: Natural Resources

Phone: 762-2547

Date: 22-Feb-95

Date: 2-12-95

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**ATTACHMENT FOR FISCAL NOTE
GOVERNOR'S LEGISLATION
REDUCE ROYALTY SHARE/HOLD PERMANENT FUND "HARMLESS"**

Implementation of this legislation will create an increased workload for the Division of Oil & Gas. We anticipate that some of the applications will be analyzed within the Division and many will require analysis by third parties (the bill provides that third-party costs will be paid for by the companies). Because of the extremely sensitive and confidential nature of the data a considerable amount of interaction between the third-party contractor and the state will be needed. Furthermore, the bill requires that applicants make a clear and convincing showing of the need for royalty reduction, so the Division will need to evaluate the economic, geological and engineering data submitted for compliance with the law prior to seeking the assistance of a third party.

Because this legislation contains provisions that may cause the terms of the application to vary over time, any approved application will need to be monitored on a continuing basis. We expect this program to have broad appeal, however, we cannot anticipate how many applications will be submitted or when they will be submitted.

An exempt Petroleum Engineer, Range 26A, will provide the broad background that will be needed to evaluate these proposals effectively. This position will need to be skilled not only in Petroleum Engineering, but will also need to have extensive knowledge of petroleum geology and petroleum economics. The salary cost of this position will be approximately \$90.6 the first year, including benefits. Additional, minor expenses such as travel, contractual and supplies will be required which we estimate will not exceed \$15.0. This position and the associated costs are our estimates of the funding needed to get the program started; if many applications are received, other positions may be required. We assume that each application will take between 4-6 employee-months to evaluate.

This legislation will effect state operating revenues in an unquantifiable manner (the Permanent Fund share is not affected by this legislation). This legislation gives the commissioner authority to grant royalty reduction which, on its face, would seem to indicate a decrease in revenue. However, since the purpose of this legislation is to promote development of fields that would not otherwise be produced, the net effect on state revenues should be positive. As a result of this legislation we are gaining new revenues based on this new production (albeit at a somewhat reduced rate from currently producing fields).

FISCAL NOTE

No. 2

Version: HB 207

(H) Publish Date: 2/27/95

STATE OF ALASKA 1995 LEGISLATIVE SESSION

Revision Date: _____ Dept. Affected: Revenue
Title: Reduce Royalty Share/Hold Permanent Fund BRU: APFC
Sponsor: GOV Component: APFC
Requester: GOV COMPONENT SERIAL NO. 109

Expenditures/Revenues

(Thousands of Dollars)

OPERATING EXPENDITURES	FY 96	FY 97	FY 98	FY 99	FY 00	FY 01
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0

CAPITAL EXPENDITURES						
-----------------------------	--	--	--	--	--	--

CHANGE IN REVENUES ()						
-------------------------------	--	--	--	--	--	--

FUND SOURCE

(Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1006 GF/MHTIA						
Other						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

Estimate of any current year (FY95) cost: \$ _____

POSITIONS

FULL-TIME						
PART-TIME						
TEMPORARY						

No additional costs or significant impact is anticipated with the implementation of this proposed legislation upon the Alaska Permanent Fund Corporation.

Prepared by: Martin Pihl, Acting Executive Director
Division: APFC
Approved by: Deborah Vogt
Commissioner: Revenue
Agency: Revenue

Phone: 465-2047
Date: 2/23/95
Date: 2/23/95

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Oil + Gas

~~HOUSE SPECIAL COMMITTEE ON FISHERIES~~

DATE: 3/7/95

PLACE: Rm 124

SUBJECT OF MEETING:

HB207 - Royalty Reductions
HB209 - " " " "
" Work Session "

NAME	REPRESENTING	BUSINESS/PERSONAL MAILING ADDRESS	ZIP	(H) PHONE	(W) PHONE	DO YOU WANT TO TESTIFY?	WHAT SUBJECT/ WHICH BILL?
PATRICK COUGHLIN	State	Attorney General's Office 1031 W 4th Ave Anchorage, AK 995	99501	249-6207	269-5255	Y	N
Bill Van Dyke	State DNR	DNR / DO & G 3601 C Street Suite 1380 Anchorage AK			7622550	Y	N
						Y	N
						Y	N
						Y	N
						Y	N
						Y	N
						Y	N
						Y	N
						Y	N
						Y	N

B

F USE COMMITTEE REPORT

3/22/95

(7)

Date Referred: February 27, 1995

FURTHER REFERRALS:

Resources
Finance

Date of Committee Action: _____

The HOUSE SPECIAL COMMITTEE ON OIL AND GAS Committee considered:HB 207

HOUSE BILL NO. 207

ADJUSTMENTS TO OIL AND GAS ROYALTIES

"An Act relating to adjustments to royalty reserved to the state to encourage otherwise uneconomic production of oil and gas; relating to the depositing of royalties and royalty sale proceeds in the Alaska permanent fund; and providing for an effective date."

recommends it be replaced

with the following committee substitute

CS HB 207 (O+G)

[] the same title

[X] a new title

[] additional referral to _____ Committee

[] attached amendment(s)

ADOPTS: Oil & Gas Letter of Intent

ATTACHES NEW FISCAL NOTE(S):

(Dept)

APPROVES PREVIOUS:

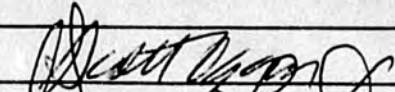
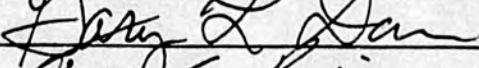
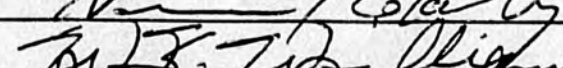
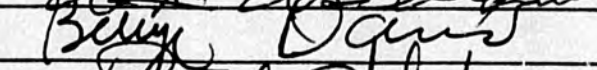
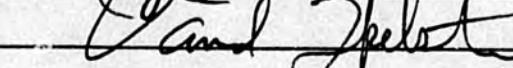
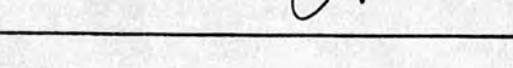
(Dept/Date)

[X] fiscal note(s)

REV (indeterminate)

fiscal note(s)

DNR 3/8/95[] zero fiscal note(s)[X] zero fiscal note(s)REVENUE 2/27/95

SIGNING WITH RECOMMENDATIONS		DP	DNP	NR	AM
	Ogan	✓			
	G. Davis			✓	
	Brice	✓			
	Rokeberg	✓			
	Williams	✓			✓
	B. Davis	✓			
	Finkelstein				✓

CHAIR'S SIGNATURE


 Rokeberg

Oil's Legislative Outlook

Some difficult issues must be resolved between the Alaska Legislature and the state's oil and gas industries.

By Ray Tyson

Looking ahead, 1995 could prove to be a critical year for Alaska's oil and gas industries as the spotlight turns to a new governor and legislature once again faced with eroding petroleum and budget gaps.

And with the lion's share of state income coming from royalties and taxes on North Slope crude production, industry has plenty reason to be concerned. The main theme of this year's legislative session promises to be taxes — and more taxes.

"Back taxes, future taxes, tax regulations, confusion in tax interpretation, and use of taxes collected are going to be the key issues," projects Jeff Lowenfels, an Anchorage attorney and vice president of Yukon Pacific Corp.

In addition to the tax issue, expect industry to seek government incentives for development of so-called "marginal" fields, or fields companies say cannot otherwise be developed because of Alaska's weak oil-price environment, competition and other factors.

"I think there is going to be heightened discussion about whether we are doing enough ... for oil and gas companies, or regardless of what we do whether that would be enough," says Jim Eason, director of the Alaska Department of Natural Resources' oil and gas division.

However, state lawmakers and the governor shouldn't have any difficulty figuring out what companies want in 1995.

Aggravating Attitudes

The dilemma facing the petroleum industry was clearly echoed last year by Gaffney, Cline & Associates, an international oil and gas consulting firm hired by the state to assess the Alaska industry. Gaffney concluded industry here was in a state of "near-crisis" and that the problem was being compounded by taxes, regulations and government attitude toward industry.

Roger Herrera, an Anchorage-based industry consultant, believes Alaska's problem runs much deeper than the tax issue or the want of state incentives. He says oil companies and the state need to start communicating, suggesting the new governor and company representatives meet every two weeks to "chat" about their problems.

"It's that old adage that if there's a will, there's a way," Herrera says. "If you really want to come to a solution, you can do it without going through all of the excruciating pain of changing laws."

What Herrera and others are suggesting is that a fundamental change in relationship between industry and government must first occur if Alaska is going to resolve its problem with declining oil production and dwindling state income.

"Even if you could take 24 different laws and regulations and change them all, you wouldn't end up with the (desired) result," Herrera says. "So often when you mess around with the language of rules and regulations, you enhance one thing and then it's used against you in some other way."



Clark James Mishler

The oil industry seeks a new relationship with state government.

Increasing Incentives

Nevertheless, there no doubt will be some pushing and shoving in the legislative arena this year over specific industry incentives designed to raise North Slope oil production, which has slipped from a peak of just over 2 million barrels a day in 1988 to the current rate of just under 1.6 million barrels a day.

For example, Anchorage Rep. Joe Green, chairman of the House Oil and Gas Committee, is working on a legislative package that would give

companies tax breaks for drilling wells to extract oil that otherwise would be uneconomical to produce. Additional incentives might be offered for Enhanced Oil Recovery projects, such as reservoir waterflooding, a technique used to push oil toward producing wells.

Meanwhile, BP Exploration (Alaska) Inc., the state's largest producer, says it will likely pursue royalty or tax reliefs for at least two marginal North Slope fields — the Schrader Bluff field at Milne Point and the remote, undeveloped Badami field east of Prudhoe Bay.

"There is a real need for the state to have a fiscal pathway to get out of its difficulties. It's a real drag on our ability — and other folks, too — to get investments."

JIM PALMER
BP EXPLORATION

"Badami must compete for funds with projects in the Gulf of Mexico and indeed with projects around the world," explains Dick Oliver, BP Exploration's chief executive officer. "We have to make decisions like that not only about Badami, but about all the other investment opportunities we have — here and everywhere else."

The Back-Tax Debate

However, Alaska's oil and gas industry appears to be most concerned about government's spending habits in the wake of declining production and its hot pursuit of back oil taxes to make ends meet. Companies say they want more "clarity" and "certainty" on their tax obligations, a major stumbling block when it comes time to negotiate with their parent companies for Alaska investment capital.

As of mid-November, Alaska producers had already shelled out almost \$4 billion in settlements for tax and royalty claims, some dating

back as far as 1977, the year North Slope crude began to flow.

Collection of back taxes has been placed in a reserve account, which lawmakers have used to balance the state budget — a practice that has made companies nervous.

"There's a need for the state to have a fiscal pathway to get out of its difficulties. It's a drag on our ability — and other folks, too — to get investments," says Jim Palmer, BP Exploration's director of external affairs.

For the first time in more than a

dozen years, the state Department of Revenue last year overhauled its tax regulations in an effort to resolve some of the problem. While commending the state for working with industry on the issue, however, the Alaska Oil & Gas Association (AOGA) concluded the new regulations fell "just short of achieving a major breakthrough in tax reform."

Perhaps the biggest industry complaint over the years stems from how the revenue department values crude oil and its lengthy and complicated



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452-5694

Saturday, January 21, 1995

Registration 9:00 a.m.

Program 10:00 a.m. to 4:00 p.m.

Sheraton Anchorage Hotel • Howard Rock Ballroom

Confirmed Speakers:

Ken Thompson
President • ARCO Alaska, Inc.

Dave Pritchard • President
Alyeska Pipeline Service Company

Paul Kelly • Vice President
Rowan Companies

John Morgan • President
BP Exploration (Alaska) Inc.

Ernie Cade • Chairman
American Association of Blacks in Energy

Eric Ball • Senior Vice President
Willis Corroon

The Honorable Ted Stevens
Senator

Hazel O'Leary (via video link)
Department of Energy Secretary

The Honorable Bob Dole
Speaker of the House (via video link)

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The 12th Annual
Opportunities Conference For
Alaska's Business Community

House Oil and Gas Committee

House Bill No. 207

Testimony of Nancy Schoephoester
Government Relations, ARCO Alaska, Inc.
March 9, 1995

Mr. Chairman, members of the House Oil and Gas Committee, my name is Nancy Schoephoester and I am a representative of ARCO Alaska, Inc. Thank you for the opportunity to come before this committee to speak in support of House Bill No. 207 relating to oil and gas royalty adjustments.

We believe that Alaska and the oil and gas industry share common goals, namely jobs and economic opportunity for Alaskans. However, in order to achieve these common goals, we need 1)to mitigate the production decline now occurring in existing fields through the discovery and development of new oil accumulations and the development of marginal horizons in existing fields, and 2)the incremental revenue that will be derived from new production is needed.

The only way to reach these common goals is through sustained oil and gas development. That means:

- Continued exploration of Alaska
- Development of marginal oil accumulations
- And by extending the economic lives of existing fields.

To have sustained oil and gas development we must be competitive in a global economy. That means that companies like ARCO must reduce costs through improved operating practices and development of new, more cost effective technologies. And the state must be willing and able to consider changes in the tax, royalty and regulatory treatment of proposed oil and gas projects. These changes can result in new production, new revenues, and new jobs.

Oil Prices are down and have been down for some time. Investment capital is in short supply and there is an abundance of oil and gas investment opportunities available. Alaska is competing in the world market for investment dollars and must provide incentives to encourage the flow of some of those dollars into the state. We support HB 207 as a step in that

direction, and we believe that it is a good first step in that this legislation may encourage oil and gas production from marginal fields which would otherwise be considered uneconomic.

Time is of the essence in showing a willingness for the state and industry to work together. We would like to see legislation passed this session. We believe that HB 207 is not in any way an overhaul of state oil and gas statutes, but rather a tool to help us accomplish increased production and revenues. This legislation would provide royalty relief in three cases - 1) on new and existing fields which have been delineated but not previously produced, 2) as per barrel or barrel equivalent costs increase in the later stages of production decline, and 3) to reestablish commercial production of shut-in oil or gas that would not otherwise be economically feasible. ARCO believes that the state and the oil and gas industry can come to terms to create a mutually satisfactory climate to allow us to reach our common goals - a win/win situation.

In closing, I would like to thank the House Oil and Gas Committee for devoting the necessary time and energy to work on this bill, and for your consideration of this legislation in such a timely fashion.

**DIVISION OF LEGAL SERVICES
LEGISLATIVE AFFAIRS AGENCY
STATE OF ALASKA**

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

130 Seward Street, Suite 409
Juneau, Alaska 99801-2105

MEMORANDUM

March 8, 1995

SUBJECT: Deposits of royalties and royalty sale proceeds in the permanent fund
(HB 207)

TO: Representative Rokeberg, Chair
House Special Committee on Oil and Gas

FROM: Tamara Brandt Cook *TBC*
Director of Legal Services

HB 207 permits the Commissioner of Natural Resources to grant reductions in mineral royalties in certain cases. AS 37.13.010 is amended under sec. 1 of the bill to require deposits into the permanent fund to be made at the level that would have applied without a reduction in cases where royalties are reduced. You have asked whether this amendment is constitutionally required. I cannot think of a constitutionally based argument that would require this.

Article IX, sec. 15 of the state constitution requires that at least 25 per cent of the money "received by the State" from certain mineral sources be placed in the permanent fund. The amount that must be reserved to the fund depends upon actual state receipts. If HB 207 is enacted it may be that royalties will be reduced in some cases from the levels that currently exist. While this could change the amount received by the State, all that the constitution requires is that at least the set percentage of whatever amount is, indeed, received go to the permanent fund.

TBC:glc:klb
95-201.glc



Resource Development Council for Alaska, Inc.

121 West Fireweed Lane, Suite 250, Anchorage, Alaska 99503-2035
Phone 907/276-0700 Fax 276-3887

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Testimony of Resource Development Council on HB 207

An Act relating to the reduction of royalties reserved to the state to encourage production of oil and gas from marginal fields
House Oil and Gas Committee
March 15, 1995

Good afternoon. My name is Carl Portman, Communications Director of the Resource Development Council for Alaska, Inc. On behalf of RDC, thank you for the opportunity to testify on HB 207.

RDC is a proponent of a strong oil and gas industry and has worked to advance incentives that will encourage the industry to explore for new oil fields in Alaska and to bring into production existing reserves. Oil revenues account for more than 80 percent of state revenues and one in every three jobs in Alaska. As oil production and revenues decline, so will the number of Alaska jobs supported by petroleum revenues.

Current forecast scenarios indicate Alaska oil production will decline to about half of today's current levels by 2006. Half of the oil production projected for 2000 and beyond, however, is based on investments yet to be made. As a result, the outlook could be worse than current projections if investments are cut.

Alaska is at a competitive disadvantage in attracting capital investments because of high transportation, exploration and development costs, long lead times, crude oil characteristics that discount North Slope oil compared to other crudes and a state revenue structure that takes a bigger share of profits. What Alaska needs is a strategy to counter these disadvantages, to make Alaska more competitive in the world market so that more dollars are invested here.

HB 207 is a step in the right direction. Through a reduction in royalties, this bill would encourage otherwise uneconomic production from marginal fields and prolong the production life of declining fields. And this is important because much of Alaska's future production will come from marginal fields. There are a number of undeveloped North Slope oil accumulations, many of which would be in production if they were located in the Lower 48. But in Alaska, high costs, combined with low oil prices, make them uneconomic.

HB 207, however, would encourage the state and the industry to work together to change the economic equation for marginal fields. With passage of HB 207, Alaska's ability to compete for investment capital would improve, as would the prospects for a stable economy with steady, well-paying jobs. The benefits to Alaska are obvious -- new jobs, more production and long-term additions to the tax base for state and local property taxes.

HB 207 sends a clear signal to the board rooms of London, Los Angeles and Houston that Alaska aims to be competitive in the world market to attract the investments necessary to develop its oil and gas potential. It provides the Department of Natural Resources with the flexibility needed in working with investors on a case-by-case basis to make new development a reality. This bill will make a difference in attracting investment capital to Alaska -- instead of it going elsewhere.

HB 207 will help get marginal fields into production -- fields that might otherwise go untapped or would be shut-in without a royalty reduction. Without HB 207, there would be no revenues from these fields.

RDC believes this bill provides adequate safeguards to protect the state's best interests. HB 207 would require the lessee to make a clear and convincing case that a royalty reduction is necessary and is in the best interest of the state. It also provides that if relevant factors change in the future the Commissioner of Natural Resources may raise the royalties that were previously reduced.

Thank you for the opportunity to comment on HB 207.



Official Business

Alaska State Legislature

HOUSE OF REPRESENTATIVES

House Special Committee on Oil and Gas

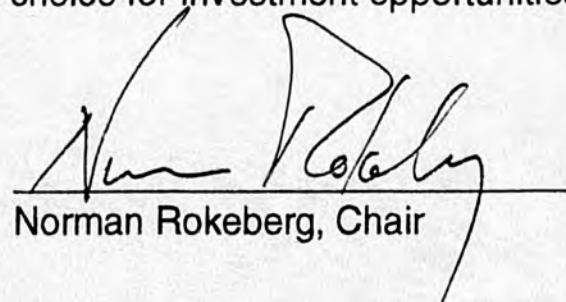
State Capitol
Juneau, AK 99801-1182

Letter of Intent HB 207

In amending AS 38.05.180 (j) it is the intent of the House Special Committee on Oil and Gas to encourage the oil and gas industry in Alaska to develop uneconomic marginal oil and gas fields. Modification of the statutes will encourage future petroleum development in Alaska. The climate for additional capital investment will improve the State of Alaska's ability to compete in a world wide market. The legislation creates an incentive for industry to select Alaska as a place to invest. Continued investment in Alaska will produce quality jobs for Alaskans and an additional source of revenue for the State of Alaska.

Oversight by the Royalty Oil and Gas Development Advisory Board will insure that the State of Alaska's best interests are protected. A stronger definition of a delineated field was included to remove ambiguities. A sliding scale royalty or other mechanism on undeveloped fields has been included for use by the Commissioner of Natural Resources when the price of oil or gas changes. The relevant factors of proved reserves, well productivity or capital investment were elevated to a higher level of consideration if production would not otherwise be economically feasible for a field, pool, or portion of a field or pool.

A better relationship between the State of Alaska and Alaska's primary industry will enable Alaska to be the first choice for investment opportunities.



Norman Rokeberg, Chair

DEPT. OF NATURAL RESOURCES

DIVISION OF OIL AND GAS

P.O. BOX 107034
ANCHORAGE, ALASKA 99510-7034
PHONE (907) 762-2553

July 2, 1992

Mr. L. R. Dartez
Production Manager
Alaska Region
Domestic Production
Marathon Oil Company
P. O. Box 190168
Anchorage, AK 99519-5311

cc:

7/9/92
LLV - (VIA FAX)

ORIGINAL MA → CE

RE: North Trading Bay Unit
Suspension of Operations

Dear Mr. Dartez:

Marathon Oil Company applied for a suspension of production or operations of the North Trading Bay Unit in accordance with 11 AAC 82.670. A suspension of operations of the North Trading Bay Unit is approved on the condition that Marathon commit to the schedule of activities set out in its June 22, 1992 letter.

Preliminary Engineering and Design
Procurement and Construction Planning
Recomplete and Test Wells
Begin Construction
Start Gas Production

Commence
January 1993
June 1993
Spring 1994
Spring 1994
Fall 1994

This constitutes more than two years suspension of production from the unit. Hopefully the conversion to gas production will go smoothly. Annual updates to the unit plan of development will be required.

We will not require abandonment of the Spurr Platform, subsea pipelines and Granite Point Production Facilities at this time. However, planning for the inevitable abandonment of the facilities is critical, as Mr. Watson stated in this March 23rd letter.

RECEIVED

JUL 7 1992

MARATHON OIL CO.
Production Manager
Alaska Region

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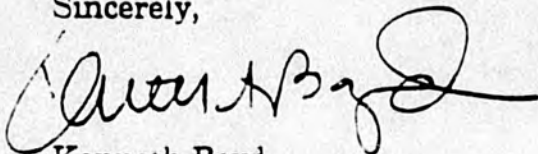
Marathon Oil Company
North Trading Bay Unit
Suspension of Operations
July 2, 1992
Page 2

"A major undertaking during this suspension period will be the evaluation of abandonment options for Spark, Spurr and Granite Point Production Facility. This evaluation will attempt to optimize method and timing of abandonment. As no platform has been abandoned in the Cook Inlet to date, much research needs to be done prior to abandoning the first structure."

We are willing to work with you to develop an acceptable plan and schedule for abandonment, and expect that it will require review and approval by other departments of the state as well as local and federal agencies. This is anticipated to be a lengthy process. Please contact Jim Haynes, Manager of our Permitting Unit to coordinate review of the draft abandonment plan. The draft plan is due on January 1, 1993.

The 19th Plan of Development and Operations for the North Trading Bay Unit, as amended on March 20, 1992 is approved. In accordance with 11 AAC 83.343.(4)(c) "The unit plan of development must be updated and submitted to the commissioner for approval at least 90 days before the expiration date of the previously approved plan, as set out in that plan." The 20th Plan of Development and Operations for the North Trading Bay Unit will be due on or before October 1, 1992.

Sincerely,



Kenneth Boyd
Acting Director

cc: Nancy Cress, Royalty Accounting

cdw/ntbu2

(52)

STEVE COWPER, GOVERNOR

DEPARTMENT OF NATURAL RESOURCES

DIVISION OF OIL AND GAS

P.O. BOX 7034
ANCHORAGE, ALASKA 99510-7034
PHONE: (907) 762-2553

(907) 762-2547

July, 17 1990

Marathon Oil Company
P. O. Box 190168
Anchorage, Alaska 99519

Attention: Bradley G. Penn
Area Landman

Subject: North Trading Bay Unit
Royalty Reduction Application

Dear Mr. Penn:

The Division of Oil and Gas is in receipt of your July 2, 1990 letter concerning the North Trading Bay Unit Royalty Reduction Application. Your letter requests that the division respond to the following questions:

- 1) Please indicate what specific economic data and in what form it should be presented for ARCO's and Texaco's past ownership of the leases;
- 2) Direction on the suitability of the Texaco data submitted with the July 2, 1990 letter;
- 3) Justification of the need for the rate of return information from ARCO and Texaco.

I believe the answers to the first two questions are provided in the division's letter of March 28, 1990 to Mr. A. R. Kukla and the attachment to that letter, Information Sheet on Applications for Royalty Reduction. The data submitted in support of a royalty reduction application must comply with the existing statutes and regulations. The Information Sheet constitutes the division's current interpretation of what existing law requires, either explicitly or implicitly, and provides royalty reduction applicants with the basic information of what the division can and must receive before it will process an application for royalty reduction.

- The answer to the third question is also addressed in the March 28, 1990 letter to Mr. Kukla and the existing statutes and regulations. AS 38.05.180(j) provides

3

Mr. Bradley G. Penn
July 18, 1990
Page 2

...[E]ach lessee requesting the reduction [must make] a clear showing that the revenue from all hydrocarbons produced from the field is insufficient to produce a reasonable rate of return with respect to that lessees' total investment in the field.

(Emphasis added).

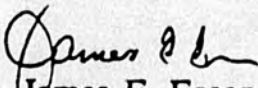
11 AAC 83.185(a)(4) states that an application for royalty reduction must

contain a detailed statement covering the entire life of the lease showing all expenses and costs of operating the lease, including all royalties and overriding royalties and all income from all produced minerals from the lease; ...

(Emphasis added).

Since Marathon is the applicant for royalty reduction, Marathon must satisfy the existing statutes and regulations with respect to its application. As the division interprets AS 38.05.180(j) and 11 AAC 83.185(a)(4), Marathon must submit complete revenue, cost, and expense data for not only Marathon but also ARCO and Texaco; however, only Marathon needs to submit rate of return information.

Sincerely,


James E. Eason
Director

cc: Ken Boyd
Nancy Cress
Bonnie Johannsen
Bill Van Dyke

ntbu.royalred.txt

4

Alaska Region
Domestic Production



P.O. Box 190168
Anchorage, Alaska 99519
Telephone 907/561-5311

July 2, 1990

Mr. James E. Eason
Director
Division of Oil and Gas
Department of Natural Resources
P. O. Box 7034
Anchorage, AK 99510-7034

Subject: North Trading Bay Unit Royalty Reduction Application

Dear Mr. Eason,

Pursuant to your letter of March 28, 1990 we submit the following response and questions for further clarification of our Royalty Reduction Application of July 18, 1989 for the North Trading Bay Unit. In an attempt to clarify our stance I will give a brief history of the project.

In March of 1989 Marathon personnel met with you and your staff concerning the initial application for royalty reduction. After items such as past production, operating costs, and net earning of previous owners was discussed Marathon prepared information for the application. A draft application was submitted for review by your staff in May of 1989. After incorporating the comments on that draft a Royalty Reduction Application was submitted in July, 1989.

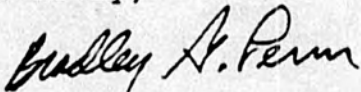
A primary item of discussion, one which Marathon predicated the preparation of the application on, was the need and ability to get financial data from past owners. While Marathon is able to provide economic and cost analysis for these leases under Marathon ownership, it has been unable to acquire the necessary information for past operating costs and net earnings except those which were submitted by Texaco in 1982 and 1983.

(5)

Mr. James E. Eason
July 2, 1990
Page 2

A considerable amount of time and effort went in to preparing the Royalty Reduction Application from Marathon's ownership forward. To prevent unnecessary expenditures of manpower, we are asking that you respond to questions of past economic data. Please indicate what specific economic data and in what form it should be presented for ARCO's and Texaco's past ownership. Direction on the suitability of the Texaco data is requested. Please justify the need for rate of a return for ARCO and Texaco ownership. After this information is received, Marathon will continue with the application update.

Sincerely,



Bradley G. Penn
Area Landman

BGP/cl
NTBU/10

cc: R. J. Murphy
R. J. Barnwell
G. A. Stapleton
S. K. Watson
CEF 801



✓ 66.
STEVE COWPER GOVERNOR

DEPARTMENT OF NATURAL RESOURCES

DIVISION OF OIL AND GAS

PO BOX 7034
ANCHORAGE, ALASKA 99510-7034

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1990

March 28, 1990

OFF Field File # 801
Well File # _____
Other _____
Active Ret. _____
INACTIVE PRI: _____

Mr. A.R. Kukla
Marathon Oil Company
P. O. Box 190168
Anchorage, AK 99519

Re: North Trading Bay Unit Royalty Reduction Application

Dear Mr. Kukla:

I have received the July 18, 1989 royalty reduction application submitted by Marathon Oil Company for the North Trading Bay Unit. While staff have previously met to discuss the application, this letter is the first written response to your request for royalty reduction.

Your cover letter states that the application is being submitted pursuant to AS 38.05.180(j). AS 38.05.180(j) provides:

To prolong the economic life of an oil and gas field, the Commissioner shall adopt regulations for all bidding methods to allow reduction of royalty on leases within the field to compensate for increasing costs in the later stages of production decline. The Commissioner may not grant a reduction of royalty until two years' initial production from the field has occurred and each lessee requesting the reduction has made a clear showing that the revenue from all hydrocarbons produced from the field is insufficient to produce a reasonable rate of return with respect to that lessees' total investment in the field.

11 AAC 83.185(a), promulgated under AS 38.05.180(j), states:

An application for a reduction of royalty on leases under AS 38.05.180(j) must comply with 11 AAC 88.105 and

(7)

March 28, 1990

(1) state all the facts entitling the applicant to relief;

(2) state the location and status of all past and present activities on the lease;

(3) include a detailed report of all production during the six months preceding the filing of the application;

(4) contain a detailed statement covering the entire life of the lease showing all expenses and costs of operating the lease, including all royalties and overriding royalties and all income from all produced minerals from the lease; and

(5) include an agreement by the applicant to defray the cost of publishing a notice as provided by (b) of this section.

(Emphasis added). The royalty reduction application submitted by Marathon is incomplete for a number of reasons, including the following. First, under AS 38.05.180(j), Marathon must submit data on its total investment in the field, which it has not done. Also, that statute implies that Marathon must submit data on its actual rate of return, state what it believes a reasonable rate of return to be, and show that the royalty reduction requested will result in a rate of return no greater than that reasonable rate of return; this Marathon has not done. Furthermore, AS 38.05.180(j) provides for a royalty reduction in the event of increasing costs and an inadequate rate of return. For the Spurr Platform, Marathon has submitted data for a period of less than one year. This, obviously, is not a long enough period to document increasing costs or calculate a representative rate of return.

Second, 11 AAC 83.185(a)(4) requires that the application contain "a detailed statement covering the entire life of the lease showing all expenses and costs of operating the lease . . . and all income from all produced minerals from the lease." Marathon has provided some information on income and expenses for the period it has been the lessee, but not for the entire life of the leases. And the expense and income information provided does not qualify as "detailed." For example, the charts submitted as part of the application start with "net revenue." Yet no data is provided on gross revenue, and on the amount and nature of expenses deducted to arrive at "net revenue." Another significant example of the lack of detail is found in Marathon's failure to separately state individual categories of operating expenses.

Third, Marathon acquired an interest in the Spark Platform in

(E)

Mr. A.R. Kukla
Marathon Oil Company

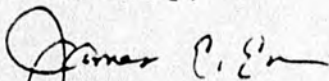
3

March 28, 1990

May, 1984. I understand that Marathon was previously informed that its application need only provide for the period 1986 to present, which it did. Marathon is required to provide figures for the entire life of the lease, and certainly for the entire period Marathon has had an interest in the Sparks Platform.

I have enclosed for your review a copy of the Division's recently prepared Information Sheet on Applications for Royalty Reduction. This Information Sheet constitutes the Division's interpretation of what it can and must receive under AS 38.05.180(j) and 11 AAC 83.185(a)(4) before it will process an application for royalty reduction. I encourage Marathon to revise and resubmit its application after correcting the deficiencies noted in this letter and reviewing the Information Sheet. When a complete application is received, a public hearing on the application will be scheduled, and a notice of hearing published. I also anticipate that the State will audit Marathon's records before granting or denying the application.

Sincerely,



James E. Eason
Director

JE

Enclosure (Information Sheet)

(9)

INFORMATION SHEET ON
APPLICATIONS FOR ROYALTY REDUCTION

CONTENTS OF APPLICATION. (a) An application for royalty reduction under A.S. 38.05.180(j) and 11 AAC 83.185 must comply with the requirements of 11 AAC 88.105.

(b) Three copies of the application must be filed with the office of the director of the division of oil and gas, department of natural resources.

(c) Unless waived by the commissioner of the department of natural resources, the application must include for the leasehold which is the subject of the application:

(1) a statement of all facts entitling the applicant to the relief requested;

(2) the ADL number and location of the lease;

(3) a map and written description of the existing, proposed, and adjoining oil and gas operations;

(4) records and estimates of each year's quantity and quality of oil and gas production for the entire life of the lease, both historical and projected;

(5) a comparison of the timing, quantity, quality, and location of oil and gas production in the event relief is granted vis-a-vis the timing, quantity, quality, and location of oil and gas production in the event relief is denied;

(6) detailed annual financial statements (limited to the subject lease) for each year's income, expenses, assets, and liabilities for the entire life of the lease, both historical and projected;

(7) the report of a certified public accountant which identifies and explains any deviations from generally accepted accounting principles made in the historical portion of the statement required by paragraph (c)(6);

(8) a statement of future action intended or expected to significantly affect income, expenses, assets, or liabilities;

(9) copies of all of the applicant's estimates of oil prices, gas prices, and/or taxes generated within the five years preceding the filing of the application;

(10) copies of all of the applicant's authorizations for expenditures generated within the five years preceding the filing of the application, including all supporting documents (e.g. discounted cash flows, decision memoranda, etc.);

10

(11) a statement of, and supporting calculations for:

(A) the rate of return on the applicant's investment in the leased premises from the date of lease until date of application;

(B) the projected rate of return for the entire life of the lease in the event that the relief requested is denied; and

(C) the projected rate of return for the entire life of the lease in the event that the relief requested is granted;

(12) a statement of efforts made to obtain monetary or other concessions from creditors, overriding royalty interest owners, and purchasers of oil and gas produced from the leasehold;

(13) copies of any operating agreement, overriding royalty agreement, or agreement for the sale of oil or gas produced from the leasehold;

(14) the applicant's certification that, using current standard industry operating procedures, both the oil and the gas are economically unrecoverable without royalty relief;

(15) the applicant's certification that all accounting, financial, tax, geologic, geophysics, and engineering data submitted with the application is accurate and complete; and

(16) all other information and documents as requested by the commissioner.

(d) Any page of the application containing information which is privileged from disclosure to the public by federal or state law may be labelled "PRIVILEGED - DO NOT DISCLOSE" by the applicant. For each page so labelled, the applicant must identify the law which is the basis of its claim of privilege. If the claim of privilege is valid, the state shall not make the privileged information as set forth on the labelled page available to the public without the consent of the applicant. The application must segregate privileged and nonprivileged information so that the disclosure of nonprivileged information is not hindered by the presence of the "PRIVILEGED" label on the page on which it appears.

ACCOUNTING PRACTICES. Financial data shall be calculated and presented in a manner consistent with the State of Alaska Department of Revenue regulations governing taxable income from oil and gas production, 15 AAC 21.100 et. seq., with generally accepted accounting principles (GAAP), and with the principles of the Council of Petroleum Accounting Society (COPAS). Where the regulations, GAAP, and/or COPAS conflict, the regulations shall prevail over GAAP and COPAS, and GAAP shall prevail over COPAS.

(11)

PROJECTED FIGURES. The applicant requesting a royalty reduction must provide projections of production, income, expenses, assets, liabilities, and rates of return that extend through the entire estimated life of the lease.

INSPECTION OF BOOKS AND RECORDS. After an application for relief has been filed, the state is entitled to, but not obligated to, inspect, copy, and audit the books and records of the applicant for the purpose of deciding whether to grant or deny the application. The option to inspect books and records does not relieve the applicant of its obligation to file a complete and accurate application.

(12)

A. Kukla
Production Manager
Alaska Region
Domestic Production



Marathon
Oil Company

P.O. Box 190168
Anchorage, Alaska 99519
Telephone 907/561-5311

July 18, 1989

Lennie Boston Gorsuch
Commissioner, Department of Natural Resources
P. O. Box 107034
Anchorage AK 99510-7034

Dear Commissioner Gorsuch:

ROYALTY REDUCTION APPLICATION FOR THE NORTH TRADING BAY UNIT

Marathon Oil Company respectfully submits the attached application for royalty reduction pursuant to Alaska Statute 38.05.180(j) for state leases ADL 17597, ADL 18776, and ADL 35431. The North Trading Bay Unit encompasses these leases which are produced from the Spark and Spurr (formerly Texaco "A") platforms. These platforms were installed in 1968, and production has continued up to the present.

Pursuant to the criteria under the Alaska Statutes, Marathon requests this royalty reduction to prolong the economic life of the oil and gas field on said platforms within the North Trading Bay Unit. The data presented for operation of the two platforms show the revenue generated has been and is currently insufficient to produce a reasonable rate of return on investment.

Sincerely,

A. R. Kukla

\\DOCS\\DE6\\DKK25
BGP:mh
Enclosure

CEF Field File # 801
Well File # _____
Other _____
Active Ret. 5 yr
Inactive Ret. _____

(13)

ROYALTY REDUCTION APPLICATION FOR NORTH TRADING BAY UNIT LEASES

Purpose

Marathon Oil Company respectfully submits this application for royalty reduction pursuant to Alaska Statute 38.05.180(j) for state leases ADL 17597, ADL 18776, and ADL 35431 as shown in Exhibit 1. A royalty reduction of 7.5% is requested in order to prolong the economic life of production from the two platforms, the Spark and the Spurr (formerly Texaco "A") located in the Cook Inlet. The location of the platforms, wellbores and lease information are presented in Exhibit 2. The following discussion, along with data presented, will support the reasoning for this request.

This application is for all existing production and reserves allocated to state leases ADL 17597, 18776, and 35431. Marathon proposes a review of royalty reduction relief every five years.

The applicant agrees to defray the costs of publishing a notice under 11 AAC 83.185(b).

Unit History

The development of the North Trading Bay Unit occurred from two platforms, the Spark and the "A". The platforms were installed in 1968 and have undergone changes of ownership. Most of the initial development was completed prior to unitization. Effective July 1, 1971, the state of Alaska approved the Unit Agreement for the North Trading Bay Unit between Atlantic Richfield Company, as Operator, Texaco, Inc. and the Superior Oil Company.

The prime intent of that Unit Agreement was to provide for the further orderly development of the Hemlock and "G" Formations of the North Trading Unit area through a water injection and pressure maintenance program. The two platforms in the Unit, operated by Arco, were the Spark and the "A" platforms. Installation of waterflood treating and injection equipment on the Spark platform was completed in 1971. Pressure maintenance by water injection was commenced in February 1972 and continued until March 1981 for the Spark platform. Water injection and pressure maintenance ended in May 1977 for the "A" platform. The production from both platforms is transported by pipeline to the Granite Point Production Facility for processing and handling. In 1977 the sub-operatorship of the "A" platform was assigned to Texaco, Inc. and the name of the platform was changed to Texaco "A".

On May 8, 1984, Marathon acquired Arco's interest in the Spark platform, became the sub-operator, and was elected the Operator for the North Trading Bay Unit area. Effective February 1, 1985, the Superior Oil Company merged with Mobil Oil Corporation.

In a letter dated October 30, 1985, Texaco USA proposed abandonment of all wells producing from the Spark platform. Subsequently, in a letter dated February 24, 1986, Mobil Exploration Producing North America proposed abandonment of the Spark platform wells. Marathon did not approve abandonment, and pursuant to §13.4 of the Unit Operating Agreement, Texaco assigned its interest effective December 31, 1985, and Mobil assigned its interest effective April 14, 1986 to Marathon. These assignments gave Marathon a 100% working interest

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in the Spark platform and all production from the wells then producing from the platform.

Effective August 1, 1988, Texaco and Mobil assigned their respective interests in the Texaco "A" platform to Unocal. Subsequently, Unocal assigned a 50% interest to Marathon for the Texaco "A" platform and lease. Effective September 1, 1988, the Texaco "A" platform name was changed to the Spurr platform, and Marathon was designated sub-operator of the platform.

Statement of Facts - Spark Platform

The Spark platform is located in Township 10 North, Range 13 West, Section 26, Seward Meridian. The platform operating expenses and revenue data is summarized in Table 1 and detailed in Exhibit 3. The Spark platform production and income are depicted on Figure 1. The information presented in Exhibit 3 is since Marathon obtained a 100% interest in the Spark platform.

The total net production from the Spark platform is 450,567 barrels and the total net income is -\$1,156,085 since acquisition of 100% interest in 1986. The total royalty paid the state of Alaska on the unit production since 1986 for the Spark platform totals \$1,040,821, as shown in Table 1 and in Exhibit 4. The net income from original acquisition in 1984 until April 1986 was -\$2,117,402; therefore, the total net income for Spark platform is -\$3,273,487.

The net income and breakdown of operating expenses for the Spark platform are presented in Exhibit 3 which shows the historical data in detail. The numbers are presented as net revenue and operating expenses for Marathon from 1986, when Marathon obtained Texaco Inc.'s and Mobil Exploration and Production North America's interests. At the present time, Marathon has a 100% interest in the oil produced from the Spark platform, as indicated in Exhibit 1 of this application and the unit operating agreement.

History - Spark Platform

The Spark platform was installed by Arco in mid-1968. Production began in January, 1969. Total cumulative oil production is 17,174,147 barrels as of January 31, 1989. Marathon obtained an interest in the Spark platform effective May 1, 1984 and took over sub-operatorship at that time. The total cumulative production since acquisition has been 611,964 barrels. Total production for the last six months (November through April) has been 60,183 barrels or an average of 10,037 barrels per month. The average daily production rate is depicted in Figure 1. A review of the approved plans of development filed with the Alaska Oil and Gas Conservation Commission provide a historical perspective of the lease, unit, and platform activities from the commencement of production.

At present, there are four (4) producing wells on the Spark platform. Production rates for each well are submitted to the State of Alaska Oil and Gas Conservation Commission on the monthly production report. Platform location, wellbore course, and productive interval intercepts are presented on Exhibit 2. Allocation of production in the North Trading Bay Unit was originally based on

(15)

surface acreage Basic Participating Interest. Allocation of production on Spark platform was subsequently amended by letter agreement. All oil from existing completions is allocated to Marathon from the Spark platform. The four wells contributing to Spark platform production are S-1RD, S-2RD, S-8 and S-9. The productive interval for S-1RD and S-8 straddle the lease boundary for ADL 17597 and ADL 35431. The productive interval for S-2RD straddles the lease boundary for ADL 17597 and ADL 18776. The productive interval for S-9 is within the lease boundary of ADL 17597. For this and other reasons, the production is considered unit production and allocated to the Spark platform.

Statement of Facts - Spurr Platform

The Spurr platform is located in Township 10 North, Range 13 West, Section 34, Seward Meridian. The platform was obtained from Texaco, Inc. and Mobil Exploration and Production North America August 1, 1988. The net income and operating expense data is summarized in Tables 2 and 3, depicted in Figure 2, and supported in Exhibits 5 and 6. The Spurr Platform royalty information is presented in Table 2 and Exhibit 6. The Spurr platform production can be divided into three specific areas: unit oil, non-unit oil, and unit gas. The Spurr platform production and income for the last nine months are summarized on Table 2. The Spurr platform gas production and income are summarized in Table 3 and depicted on Figure 3.

The total net production attributed to Marathon from the Spurr Platform is 52,472 barrels of oil and 71,112 MCF of unit gas for the nine months for which Marathon Oil Company has acquired and operated the Spurr platform. This breaks down to 35,886 barrels of unit oil and 16,586 barrels of non-unit oil for the nine-month period. The total net income is -\$12,518 (oil and gas) since acquisition in August 1988. The total royalty paid the state since August 1988 for Spurr platform production totals \$113,176, as shown on Table 2 and in Exhibit 6. The gas produced from the Spurr platform is used for fuel gas on lease. Additional gas from the Cook Inlet Gas Gathering System is treated at Granite Point Production Facility and transported to the platforms for additional fuel gas use for said platforms, as shown on Table 3 and depicted in Figure 3. Severance tax and associated royalty are paid on the additional fuel use gas delivered to the platforms from other off-lease sources. The North Trading Bay platforms are presently fuel gas deficient. Marathon anticipates initiating expense charges associated with this fuel gas at a rate of \$1.20/MCF. These expenses will increase the direct operating expenses by approximately \$40,000 per month. The income and breakdown of expenses for the Spurr platform are presented in Exhibit 5, which shows the production and economic data for the last six months in detail. The numbers are presented as net revenue and operating expenses. Marathon and Union obtained an interest in the lease and platform in August 1988. At the present time, Marathon has a 100% interest in unit oil produced from the Spurr platform and a 50% interest in the non-unit oil and all gas produced from the Spurr platform, as indicated in Exhibit 1 of this application and the unit operating agreement.

History Spurr Platform

The Spurr platform was installed in May of 1968, and production began in September of 1968. Total cumulative production is approximately 9,607,915

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barrels of oil and 3,414,080 MCF of gas as of January 31, 1989. Marathon Oil Company and Union of California purchased the Spurr platform and state lease ADL 17597 effective August 1, 1988. Marathon assumed sub-operatorship of the platform effective September 1, 1988. The total net cumulative production since acquisition has been 53,475 barrels of oil and 606,009 MCF of natural gas. These figures coincide with the detailed statement of production for the last nine months. A review of the approved plans of development filed with the Alaska Department of Natural Resources, Division of Oil and Gas, provide a historical perspective of the lease, unit and non-unit and platform activities from commencement of production. At present, there are eight producing wells from the Spurr platform. There are four unit oil wells and one unit gas well and three non-unit oil wells. Production rates for each well are submitted to the Alaska Oil and Gas Conservation Commission on the monthly production report. Platform and wellbore locations are presented on Exhibit 2. The allocation of production was originally based on the North Trading Bay Unit Operating Agreement, but has subsequently been amended by letter agreement between the parties. All unit oil is allocated to Marathon 100%. All unit gas and non-unit oil will be allocated on a 50-50 basis between Marathon and Union. The four unit oil wells are TS-1, TS-6, TS-8 and TS-9. The unit gas well is TS-3RD. The non-unit oil wells are TS-2, TS-4 and TS-7. All wells are producing from state lease ADL 17597.

Summary

This information is presented for leases, and more specifically the two platforms, for a time period since Marathon and others have acquired the facilities. The reason for presenting the data in this manner is based on the availability of previous owners' data and the relevance of such data to Marathon's investment. The operating income is based on net oil production sales. The royalty is computed on oil sales. Marathon and Union purchased the platforms at different dates, as stated previously. For investment purposes the investments have yet to pay out, but there is further sub-thrust oil potential on the leases as well as undeveloped gas reserves potential. Marathon is currently evaluating the potential for sub-thrust and gas development from both platforms.

The monthly production facilities direct expenses include a credit for treating and disposing of water produced at Amoco's Bruce and Anna platforms and Union's Granite Point platform. This credit is calculated by multiplying total barrels treated times \$.60/bbl. Marathon treats approximately 12,000 bbls/ month for Amoco and Union, resulting in a net monthly credit of approximately \$6,500 to the onshore facilities. Any reduction in the amount of water treated and processed would increase direct operating expenses proportionally.

The costs of gas well TS-3RD are included as direct platform expenses for the following reason. These platform costs were not allocated to the well on a working interest basis, but are based on equivalent hydrocarbon production (6 MCF = 1 bbl). This allocation was necessitated by a letter agreement between Marathon and Union which specified how platform costs would be shared.

Royalty Reduction Application
North Trading Bay Unit
Page 5

The royalty reduction application request is based on the operating income losses from both platforms for a time period since Marathon has acquired the facilities. It is anticipated that royalty relief will be beneficial in lengthening the productive life of the platforms as well as aid in evaluating future resource potential. Although the information in this application is provided by Marathon Oil Company, a royalty reduction result would also benefit Unocal's working interest in the North Trading Bay Unit.

The current estimates for abandoning the two platforms is \$11 million to \$15 million each.

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(18)



LOS ANGELES DIVISION
LAND DEPARTMENT

PETROLEUM PRODUCTS

TEXACO
U.S.A.
A DIVISION OF TEXACO INC.
3350 WILSHIRE BOULEVARD
P. O. BOX 3758
LOS ANGELES, CA 90061
213-739-7100

August 20, 1982

#215699: ADL 17597
NORTH TRADING BAY FIELD - ALASKA

Department of Natural Resources
Pouch M
Juneau, Alaska 99811

Attention: Mr. John Katz, Commissioner

Gentlemen:

Texaco Inc. respectfully requests a reduction of royalty on the Texaco-Superior Platform "A" wells located in the North Trading Bay Field in the Cook Inlet. The Alaska Statutes, 38.05.180 (j), provide for this reduction for the purpose of prolonging the economic life of an oil and/or gas field to compensate for the increasing costs in the later stages of production decline. Such is the case with the wells producing from Platform "A" on the lands within oil and gas lease ADL 17597, located in Township 10 North, Range 13 West, Seward Meridian, Sections 14, 15, 22, 23, 27, 28, 33 and 34.

The information in the attached Exhibit "A" clearly shows the revenue from the producing portion of the subject lease is insufficient to produce a reasonable rate of return with respect to our total investment in the lease.

Platform "A" was installed in April, 1968 and the drilling phase was completed in November, 1969. There are no plans at this time for any additional drilling. The initial production was about 5,000 barrels of oil per day from eight wells.

At the present time two wells are shut in (T/S #8 and #9), two wells are on Reda pumps (T/S #1 and #2), three wells are on gas lift (T/S #4, #6 and #7), and one well has been converted to a gas well (T/S #3).

The total production for the first six months of 1982 was 44,159 barrels of oil and 135,656 barrels of water. The production for July was 8,794 barrels of oil and 28,426 barrels of water.

August 20, 1982

The production for each month is as follows:

<u>MONTH</u>	<u>BBLS. OF OIL</u>	<u>BBLS. OF WATER</u>
January, 1982	12,361	26,048
February, 1982	6,125	12,951
March, 1982	2,874	13,624
April, 1982	6,448	23,381
May, 1982	9,298	34,112
June, 1982	7,053	25,540

Consequently, Texaco hereby requests that the royalty rate of 12½ percent on subject lease be reduced to a rate of 5 percent in order to attempt to prolong the economic life of this lease.

Enclosed is the filing fee of \$20.00 required by Section 11 AAC 88.105(7) and Texaco agrees to defray the costs of publishing the notice required by Section 11 AAC 83.185(b) of the leasing regulations.

Any notice relative to our application for royalty relief may be sent to Texaco Inc., 3350 Wilshire Blvd., Los Angeles, CA 90010, Attention: Division Land Manager. If there are any questions or any additional information needed, please contact the undersigned at Area Code 907, 278-9611.

Very truly yours,

TEXACO Inc.

Ethel H. Nelson

Ethel H. Nelson
Advanced Exploration Land Representative

EHN:bjs

Enclosure

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PLATFORM "A" ~
LEASE ACQUISITION, DRILLING AND PLATFORM
DESIGN, ETC. COSTS*

DRILLING

Total W. I. IDC Cost	\$ 3,126,830
Total W. I. Investment Cost	680,932
Total W. I. Lease Acquisition Cost	383,038

PLATFORM

Total W. I. Investment Cost	<u>6,157,284</u>
GRAND TOTAL	\$10,348,084

*These costs were not included with Operating costs shown on previous page.

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(21)



RECEIVED

OCT 14 1982

DIV. OF MINERALS & ENERGY MGMT.
ANCHORAGE, ALASKA

October 8, 1982

TEXACO INC.
P. O. BOX 4-1579
ANCHORAGE, ALASKA 99509

#215699: ADL 17597
NORTH TRADING BAY FIELD
ALASKA

Division of Minerals
& Energy Management
Pouch 7-005
Anchorage, AK 99510

Attention: Ms. Kay Brown, Director

Gentlemen:

Attached is the additional information we discussed at the time of filing our application for reduction of royalty on the Texaco-Superior Platform "A" wells. This information, along with information submitted with our August 20 letter, shows the revenue from the producing portion of the lease is insufficient to produce a reasonable rate of return with respect to our total investment in the lease.

We apologize for the delay in submitting this information. If there are any questions or any additional information needed, please contact the undersigned at 278-9611.

Very truly yours,

TEXACO Inc.

Ethel H. Nelson
Advanced Exploration Land Representative

EHN:bjs

Enclosures

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Report gross or total gross?

PLATFORM "A" COOK INLET ALASKA
COST, EARNINGS, AND PRODUCTION

<u>YEAR</u>	<u>GROSS W.I. BBLs</u>	<u>GROSS EARNINGS</u>	<u>GROSS OPR. COST</u>	<u>NET EARNINGS</u>
1968	260,884	\$ 637,872	\$ 20,868	\$ 617,004
1969	1,690,736	4,349,932	703,900	3,646,032
1970	1,039,384	2,606,636	945,353	1,661,283
1971	743,000	2,300,122	493,851	1,806,271
1972	1,133,592	3,110,870	1,512,765	1,598,105
1973	933,488	2,921,200	2,336,317	584,883
1974	890,326	3,916,114	2,122,594	1,793,520
1975	671,538	2,932,770	2,654,522	278,248
1976	488,522	2,184,022	3,571,086	-1,387,064
1977	97,668	461,780	1,182,885	- 721,105
1978	159,466	\$1,202,298	\$ 938,174	\$ 264,124
1979	154,322	1,813,108	3,423,790	-1,610,682
1980*	136,212	1,711,176	1,864,502	- 153,326
1981*	120,218	3,426,298	2,709,098	717,200
1982 (6 mos.)	45,148 (40,200)	1,403,520 (2,407,040)	1,688,122 (3,376,244)	- 284,602
TOTAL	8,564,504	34,977,718	26,167,827	8,809,891

*This data includes Windfall Profits Tax where appropriate.

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9-27-82

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EXHIBIT "A"

PLATFORM "A" COOK INLET ALASKA
COST, EARNINGS, AND PRODUCTION

<u>YEAR</u>	<u>GROSS W.I. BBLs</u>	<u>GROSS EARNINGS</u>	<u>GROSS OPR. COST</u>	<u>NET EARNINGS</u>
1978	159,466	\$1,202,298	\$ 938,174	\$264,124
1979	154,322	1,813,108	3,423,790	-1,610,682
1980*	136,212	1,711,176	1,864,502	- 153,326
1981*	120,218	3,426,298	2,709,098	717,200
1982* (6 mos.)	45,148	1,403,520	1,688,122	- 284,602

*This data includes Windfall Profits Tax

BJC
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8-20-82

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TEXACO/SUPERIOR PLATFORM "A"
Gross Production

<u>YEAR</u>	<u>OIL</u> <u>(bbls)</u>	<u>GAS</u> <u>(mcf)</u>	<u>WATER</u> <u>(bbls)</u>
1982	92,915	430,228	253,445
1983	94,387	650,904	233,315
1984	78,844	643,414	365,206
1985	112,593	441,371	401,552
1986	104,551	407,888	310,821
1987	105,543	466,232	248,081
1988(Jan.-July)	65,320	149,453	165,257

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Immediate Actions for the Short Term



Review / Support Flexibility in DNR to Provide Royalty Relief

- **Smaller Discoveries**
- **Prolonging Economic Life**
- **Lease Sale Terms**

[HB-207, SB-101]

Review / Clarify Legislative Intent for Application of Existing Incentives

- **Exploration Incentive Credits**
- **Lease Sale Schedule**
- **Discovery Royalty Credit**

Support Calls for Federal Tax Incentives for Oil and Gas Development

Next Steps for the Long Term



Implement the Process Described Below to Examine Alaska's Long Term International Competitive Position and Recommend Alternative Proposals for Legislative Consideration

- **Legislative / Administrative / Industry Cooperation**
- **Focus First on Gathering Information on Competitive Fiscal Regimes**
- **Develop a Broad Range of Options**
- **Narrow Finally to Specific Proposals for Legislative Action**

Current Plans

- **Oil and Gas Policy Council**
- **Tax Royalty Conference**
- **96 Legislative Agenda**

TESTIMONY ON HB207 BEFORE THE HOUSE OIL & GAS COMMITTEE

Mr. Chairman, and members of the committee, My name is Bradley G. Penn, Advanced Landman for Marathon Oil Company in Anchorage.

Marathon appreciates the efforts of the legislature to develop incentives to encourage investment for development of marginal fields and to extend the life of mature fields .

Marathon has previously testified to the Senate Oil and Gas Committee that there are current legislation and regulations providing for royalty relief, however, this legislation has been ineffective in providing royalty relief.

I would like to provide the committee with Marathon's experience at royalty reduction.

1982-TEXACO application, state requires more economic data, Texaco does not pursue.

1988- Marathon and Unocal purchase Texaco "A" Platform from Texaco.

1989- July Marathon applies for royalty reduction.

1990 March DNR responds that the expenses and costs from the lease. DNR interprets to be previous owners, Marathon did predicate the application on ability to provide the data during its ownership.

1990-July Marathon requests clarification and justification.

1990-July DNR responds that Marathon has to provide "complete revenue, cost, and expense data for not only Marathon but also ARCO and Texaco; however, only Marathon need to submit rate of return information.

1992- June In the Plan of Development for the North Trading Bay Unit Marathon ask for a suspension of Operations and Production.

The oil production from the platform became uneconomical. The state may have extended the productive life of the oil production on the platforms had a royalty reduction been less burdensome to obtain. Thus extending the income stream to the state and the jobs associated with operating the platform and production facility.

Based on our experience we request that the data requested be from the applicant during their ownership. The proposed language reads " The lessee shall be required to submit data, for a royalty reduction application, for the two year time period preceding an application, it has owned an economic interest in the field."

It appears that HB 207 does not solve the problem of the discretion of the commissioner or the director of the DNR. Perhaps some other avenue of appeal could be provided, such as judicial review.

We believe there should be a sliding scale royalty based on product price increases and operating costs would be more suitable than the apparently arbitrary ability of the commissioner to "increase or otherwise modify the state's royalty share.."

Marathon appreciates the committees efforts and those of the legislature to encourage new investment and provide relief for mature fields in the state.

Testimony of

**Paul Wessells
Director, Tax**

BP Exploration (Alaska) Inc.

to the

House Oil & Gas Committee

**Juneau, Alaska
March 15, 1995**

Good afternoon, Mr. Chairman. My name is Paul Wessells, and I am Director of Tax for BP Exploration (Alaska) Inc. Thank you for the opportunity to testify on behalf of BP regarding HB 207.

BP supports HB 207 and encourages this Legislature to enact the bill. This bill represents a very positive step along the road to development of the State's marginal new oil fields and marginal projects within existing fields. It is our belief that initiatives such as HB 207 signal a new spirit of cooperation between the oil industry and state government, and it is a joint effort that will be required for the State to fully realize the value of its oil and gas resources.

In what manner does HB 207 promote full development of the State's resources? First, it clarifies the existing statute by specifying that new developments - that is, properties that have never produced oil and gas - may qualify for royalty reduction. Second, the bill provides that relief may be granted with respect to individual leases, rather than solely as part of a unit application.

The bill takes additional steps to protect the public interest by assuring that the Commissioner of Natural Resources will receive the financial and technical information necessary to allow a reasoned judgment on the merits of an application, and by requiring that the cost of third party professional assistance to the Commissioner in analyzing the application be borne by the applicant. In addition, the public interest is served by the provision in the bill that the State may condition a reduction in royalty on a readjustment at a later time if the circumstances which supported the grant of the reduction change.

It is this last aspect of the bill that makes it clear that it is not just about reducing the royalty obligations of producers in the absolute sense. Indeed, it is entirely possible that a royalty adjustment program negotiated by the State and a leaseholder will lead to greater royalty payments over the full life of a property.

We in BP believe that HB 207 will make it possible for the State and the oil industry to devise, through open sharing of information and good faith negotiation, methods for sharing the risks of developing marginal properties. It is imperative that we capture the potential of these properties to assure a strong and stable industry and a strong and stable Alaskan economy.

Thank you for the opportunity to testify.

TO: Shirley Armstrong
90 Rep. N. Rockefeller
465-2040

FR: R. A. Finckel

(6 pages + cover)

IF the chair is taking testimony,
I would like to present the
enclosed tomorrow.

Testimony to the House Oil & Gas Committee on HB 207

Richard A. Fineberg
Research Associates
P.O. Box 416
Ester, Alaska 99725

March 15, 1995

A. A strong substantive case for easing the state's existing royalty relief provisions, as the Administration proposes in HB 207, has yet to be made.

At this point we appear to be making policy not on substantive information, but on empty rhetoric. Consider production trends and profitability.

1. Production Trends. On reviewing North Slope production forecasts for 1985, 1990 and 1995, a clear trend is evident: the North Slope production decline, although real, consistently plays out in a more benign manner than forecasted. If you compare 1985 forecasts to the current forecast through 2010, you will find that we now expect to produce 3.75 billion more barrels of oil through 2010 than forecasted in 1985. Put otherwise: Over the last ten years, the current tax and royalty regime has generated five years more of production at two million barrels per day than was forecasted in 1985. Every two years, we booked an additional year of forecasted production at TAPS' maximum throughput. This trend of increasing production (i.e., slowed decline in production) was established in the face of declining prices. Most importantly, the phenomenon of increasing production continues today, despite dire predictions by the industry in the late 1980's that we had seen the last of such increases.¹

2. Profitability. We are told repeatedly that "[t]he target is to get Arco Alaska and BP Exploration to divert exploration and production dollars from foreign areas and put them into marginal areas on the North Slope."² But the dialogue is bereft of facts. We are being asked to buy (or trade away) a pig in a poke. The economics of North Slope production are unique and dimly understood. Arco's North Slope profits are so unusual, in fact, that in considering the flight of domestic capital in 1991, a First Boston report isolated Arco's results from other companies in a separate box. In that same study, BP

¹ Based on Dept. of Natural Resources forecasts (see: Richard A. Fineberg, Alaska North Slope Production Prospects: Preliminary Analysis [a report prepared for the Northern Alaska Environmental Center, et al.], Feb. 22, 1995).

² "Tapping New Oil," Anchorage Times, March 2, 1995, p. B-7.

*Fineberg / Testimony on HB 207 (House Oil & Gas Committee)
March 15, 1995 (Page 2)*

was alone among the internationals in bucking the trend of greater returns overseas than in the U.S.³ In Alaska, we just don't get it. Consider the color, front-page graph in the Anchorage Daily News last spring showing a slide in Arco Alaska's profits from \$700 million in 1990 to \$225 million in 1993. The graph excluded Arco's Alaska pipeline profits, estimated at over \$100 million per year. Even more important, the accompanying story failed to note that in 1993 Arco's Lower-48 and overseas production endeavors lost \$180 million. Far from being a millstone around Arco's neck, from this perspective Alaska appears to be Arco's lifeboat.

In fact, N. Slope profitability is apparently sufficient to induce the consistent production increases (i.e., slowed decline) identified above. But the public dialogue in this area is blunted because North Slope producers steadfastly refuse to disclose information that would justify its petition for royalty relief and other goodies.⁴

B. HB 207 contains serious structural defects

1. I believe that it is not wise to grant royalty reduction without providing for clear and unambiguous clarification on the public record of the necessity for that assistance. Instead of making the case for royalty relief public, the bill calls for the crucial information to be held confidential at the request of the lessee. In a 1992 decision, the Alaska judge who has probably reviewed more confidential oil industry documents than any other ruled that the producer's efforts to bar public access to documents batch-stamped "confidential" without review both unwarranted and contrary to the public interest.⁵ It has been clearly and convincingly documented in other North Slope revenue disputes that public policy evils flourish where confidentiality erodes the

³ First Boston Equity Research, "Assessing the Domestic Operations of International Oil Companies: Explaining the Exodus of Capital," September 5, 1991, pp. 2-13. (See Richard A. Fineberg, North Slope Profits and Production Prospects [prepared for the Alaska State Legislature], Nov. 12, 1991, pp. 25-27.)

⁴ Last May, in an "Open Letter to the People of Alaska" published in major Alaskan newspapers, BP Alaska President John Morgan stated that BP had paid more in taxes and royalties than it has taken out in profits or cash flow. This statement flies in the face of every public study of which I am aware. BP has refused repeated requests to put on the public record information that would substantiate its claim (see attached letters).

⁵ "Memorandum Opinion and Order No. 92-71 (Denying Motions by BP Exploration [Alaska], Inc. for Continued in camera Treatment of Certain Documents in Court Record)," ANS Royalty Litigation, 1JU-77-847 Civil, May 27, 1992 (19 pp.). The court specifically refused to hold material confidential merely at the request of the industry because "the public's right to know what the executive branch is about" outweighed the industry's speculative assertion of possible damage resulting from the release of information about its business.

*Fineberg / Testimony on HIB 207 (House Oil & Gas Committee)
March 15, 1995 (Page 3)*

checks and balances and balances that normally protect the public interest and keep the public process on a steady course.⁶

2. At this time the terms "economically feasible" and "commercially viable" are the subject of some dispute in the public policy arena, while the term "best interest" is, at best, an overly broad term.

3. In my estimation, no valid public purpose is served by granting relief without appealability.

C. The current approach to incentives is flawed.

In the policy arena, where the mission is to protect the public interest in both the revenue stream and the environment, industry desires must be balanced against these concerns. To do this, measures such as royalty relief should be viewed in their broad administrative and economic context. Two factors here are particularly worth noting: The companies that bid on these leases did so with the expectation that they would pay the nominal royalty they now wish to reduce. Second, producers look at the bottom line. To effect balanced public policy, it is necessary to consider measures such

⁶ In a current case whose very existence would be hidden from the public had Exxon Corp. not been required to make some documents public in the United States Tax Court, Exxon is asking for retroactive tax deductions that the Internal Revenue Service has said could ultimately be worth \$18 to 25 billion if applied to all North Slope producers. Exxon argues that ultimate abandonment of costs of Prudhoe Bay are deductible for federal tax years 1977 through 1984 under federal tax law because those claims are both knowable and fixed (United States Tax Court Dockets No. 18618-89 and 18432-90). In December 1994, the Alaska Oil & Gas Association recommended that the state should clarify what it might require for the abandonment of Prudhoe Bay. Ironically, Exxon was identified as the lead source for that recommendation ("AOGA Briefing Paper: Lease Closure," presented to Knowles-Ulmer Transition Team Dec. 28, 1994). The blatant contradiction between Exxon's position in separate arenas is indicative of the kind of skullduggery that takes place under the cloak of confidentiality.

A second example of public policy abuses flourishing behind the veil of confidentiality is the 1985 TAPS tariff settlement. Due to confidentiality, key elements of that sorry record were not available to the public until after the settlement had been formally approved. In one instance during the latter stages of the TAPS saga, the Governor was briefed on an erroneous document that was subsequently removed from files and replaced with an altered document, in apparent violation of Alaska statutes. (See Richard A. Fineberg, The 1985 TAPS Settlement: A Case Study in the Effects of Confidentiality on Information Available to Decision Makers in Oil and Gas Revenue Disputes (prepared for the Alaska State Legislature), Feb. 5, 1990), pp. 30-36. For a later study of a TAPS settlement defect with enormous state and federal revenue consequences that was mis-stated and consequently overlooked during the flawed 1985 settlement review process, see Richard A. Fineberg, Hidden Billions: The TAPS DR&R Provision (report prepared for Stan Stephens, Valdez, Alaska), August 21, 1992.

*Fineberg / Testimony on HB 207 (House Oil & Gas Committee)
March 15, 1995 (Page 4)*

as royalty relief in the context of the tax and pipeline regulatory regimes, where powerful incentives for development of marginal fields already exist.

In the tax regime, Milne Point, Niakuk, Lisburne and several satellite fields are already virtually exempt from production taxes at current prices, thanks to the working of the modified Economic Limit Factor (ELF) the industry so staunchly opposed in 1989.

Regarding pipelines: There was discussion in committee Wednesday of BP's success at Milne Point without royalty relief. One might ask, why is BP was increasing production at Milne Point when Conoco (who traded the property to BP in 1993) apparently could not make a go of it? The most obvious difference between the two companies is this: Conoco was the lone North Slope field operator that did not share ownership of TAPS. Consequently, Conoco paid BP approximately \$1.00 per barrel in pipeline profits for every barrel of oil that it produced. While discussion of pipeline economics is beyond the scope of this hearing, I submit that one of the most important factors affecting North Slope development may be the control and operation of TAPS.

D. Concluding Remarks

It is self-evident that any bill that increases industry revenue at the expense of the State Treasury will tend to stimulate production. The industry will, of course, advocate such a measure. But even if the rather astounding provision that automatically grants confidentiality at lessee (producer) request were removed or replaced with language that guarantees public access to information necessary to evaluation of public policy, it remains to be demonstrated that this legislation is necessary, or that it reflects the wise stewardship of public resources mandated by the Alaska Constitution.

In view of the well-documented history of abuses of confidentiality that have found their way into the public record, it makes little sense to allow the lessees, at their own initiative, to prevent these materials from seeing the light of day.⁷ Were that defect corrected, the case for the proposed incentives would have yet to be made.

⁷ As the U.S. Supreme Court has observed, "People do not demand infallibility from their institutions, but it is difficult for them to accept what they are prohibited from observing." (Richmond Newspapers, Inc. v. Virginia, 448 U.S. 555, 572 [1980]; quoted in Memorandum 92-71, *op. cit.*, cover page). To accomplish his well-intentioned desire to reduce needless litigation, the Governor might consider introducing legislation that puts more information on the public record — not less.

From the desk of

Richard A. Fineberg
Ester, Alaska 99725

P.O. Box 416

Phone / Fax (907) 479-7778

Return Receipt Requested

January 17, 1995

John C. Morgan, President
BP Exploration
P.O. Box 196612
900 E. Benson Blvd.
Anchorage, Alaska 99519-6612

[COPY]

Dear Mr. Morgan:

More than seven months after I wrote you concerning assertions about North Slope profits you published in various Alaska newspapers in a May 12 "Open Letter to the People of Alaska," I am still waiting for substantive reply. In that open letter, you stated:

BP has paid \$20 billion to the state in taxes and royalties since 1977. This exceeds our total profits and cash flow from Alaska for the period.

Your statement appears to contradict all systematic published analyses of North Slope profitability of which I am aware.¹ I therefore asked you May 14 to document your claim. To help identify the differences in existing estimates, I submitted my year-by-year breakdown of estimated production and pipeline profits and a line-by-line worksheet establishing the basis for my most recent (1993) profit estimates. I requested your equivalent figures, as well as your analysis of the significant differences.

You responded July 14 with a short letter repeating that BP paid more in taxes and royalties than it earned in Alaska from 1977 through 1993. You lowered your estimated state taxes and royalty payments to \$19.3 billion, which you compared to "after tax book income for Alaska in 1977-93" of \$17.6 billion. You also stated that BP disagrees with my figures and those of a 1989 profitability study by Edward Deakin, C.P.A., then Price-Waterhouse Professor of Petroleum Accounting, University of Texas. For the second time, on July 25 I requested substantive information, noting that your letter did not provide documentation for your revised numbers or deal with the specific differences between your figures and the two tables I had presented. I received no response.

Careful analysis indicates that the North Slope continues to be one of the most profitable industrial ventures in the United States. Following my letters of May 14 and July 25, 1994, again I ask your cooperation in providing the public with accurate, sourceable data capable of supporting intelligent public policy debate on North Slope development policy.

Sincerely,



Richard A. Fineberg

¹ For example: Deakin (1989), *Oil Industry Profitability in Alaska, 1969-1987*, p.2 (1969-87 industry profit \$42.6 billion, state share \$29.3 billion); Legislative Research Agency (1993), *Distribution of Income from Alaska Oil and Gas Operations*, p. 14 (1985 industry net income \$5.6 billion, state net revenue \$3.3 billion); Fineberg (1992), p. 43, *Alaska North Slope Oil Profits*, (1991 West Coast industry profits \$4.95 per barrel, state share \$3.82); Wilson-Gillette (1994), *Consequences of Exporting Alaska Crude Oil*, p. 36 (April 1994 West Coast major field wellhead profits \$2.66 per barrel, state share \$2.63 [excludes estimated TAPS industry profits of \$1.00 per barrel v. state taxes of approximately \$0.30]).

**BP EXPLORATION**

BP Exploration (Alaska) Inc.
200 East Benson Boulevard
P.O. Box 106612
Anchorage, Alaska 99519-0612
(907) 561-5111

March 3, 1995

Mr. Richard Fineberg
P. O. Box 416
Ester, Alaska 99725

Dear Mr. Fineberg:

This letter is in response to your request during our telephone conversation of February 15th, that I confirm in writing that BP does not intend to respond to your last set of questions regarding the company's accounting for its Alaskan profits for the 1977-93 period.

The financial information included in John Morgan's "Open Letter to the People of Alaska" was derived from the published financial statements of the Standard Oil Company and the British Petroleum Company plc for the period 1977-93. It was necessary to restate some of these data because Sohio and BP's results from Alaska operations are not reported separately in the companies' published financial statements. For the most part this restatement involved the separate identification the profits, cash flow and tax payments associated with BP's share of TAPS and the separation of the companies' financial results from exploration and production in Alaska from those results in the rest of the world. This source data was derived in accordance with generally accepted accounting principles and we believe it provides a fair basis for comparison with the financial results of other enterprises.

We appreciate your interest in BP. However, we believe we have provided to you all the public information available to our investor and public constituencies and do not intend to provide additional information.

Sincerely,

A handwritten signature in dark ink, appearing to read "Paul D. Wessells".

Paul D. Wessells
Director of Tax

PDW/jp

cc: John Morgan
Jim Palmer

Table V-4.

Research Associates 2/95

1985 North Slope Production Forecast for 1986-94 v. Actual Production (ADNR)

(000 Barrels)

1985 Production Forecast (1)

Barrels per day:

Field:	Prudhoe	Kuparuk	Lisburne	Pt. McIntyre	Endicott	Milne Pt.	Other	W.Sak	Beaufort	Total
1986	1,500	180	0	0	0	0	0	<=====		1,680 000 bpd
1987	1,475	180	75		0	30	30	<=====		1,790 000 bpd
1988	1,325	200	100		50	30	30	<=====		1,735 000 bpd
1989	1,175	200	120		100	25	50	<=====		1,670 000 bpd
1990	1,050	200	120		100	20	50	<=====		1,540 000 bpd
1991	950	200	120		100	15	50	<=====		1,435 000 bpd
1992	850	200	90		100	15	50	<=====		1,305 000 bpd
1993	750	200	75		85	10	50	<=====		1,170 000 bpd
1994	650	170	70		75	10	50	<=====		1,025 000 bpd
Total Barrels:	3,549,625	631,450	281,050	0	222,650	56,575	131,400	<=====		4,872,750 000 Bbl. (Forecast)

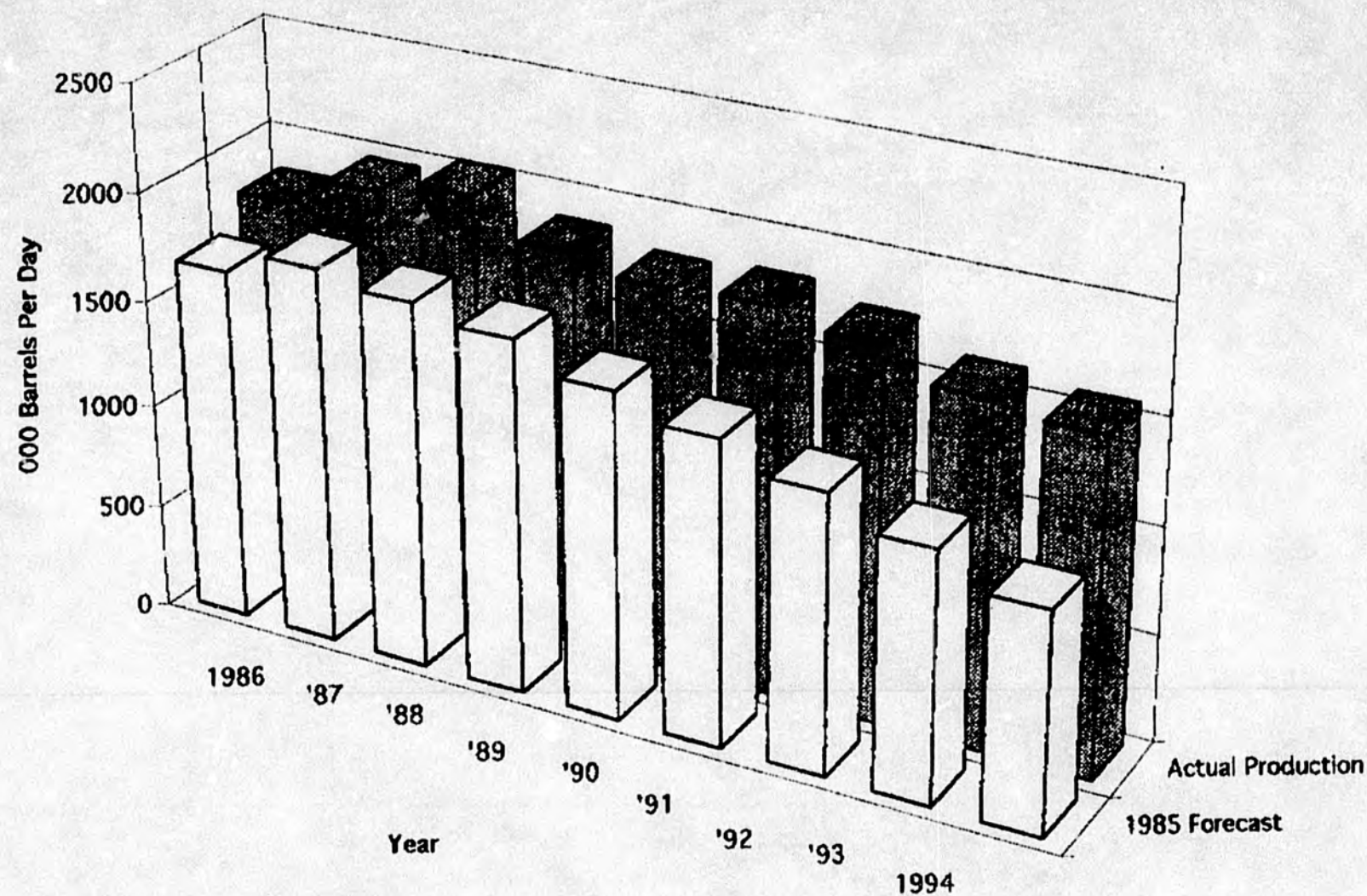
Actual Production (2)

Field:	Prudhoe	Kuparuk	Lisburne	Pt. McIntyre	Endicott	Milne Pt.	Other	W.Sak	Beaufort	Total
1986	1,539	260	10		0	13		<=====		1,822 000 bpd
1987	1,608	284	46		24	0		<=====		1,962 000 bpd
1988	1,585	304	40		103	0		<=====		2,033 000 bpd
1989	1,427	297	41		98	5		<=====		1,868 000 bpd
1990	1,340	294	43		106	18		<=====		1,801 000 bpd
1991	1,333	311	40		117	20		<=====		1,822 000 bpd
1992	1,251	325	38	0	118	19		<=====		1,751 000 bpd
1993	1,126	316	27	21	112	19	0	<=====		1,619 000 bpd
1994	1,024	305	22	97	97	18	9	<=====		1,572 000 bpd
Total Barrels:	4,465,457	983,919	111,941	42,857	282,405	40,899	3,463	<=====		5,930,941 000 Bbl. (Actual)

(1) Alaska Dept. of Natural Resources, "Historical and Projected Oil & Gas Consumption," January 1985, p. 13 (Table 2.2: Estimated Availability of N. Slope Oil For Sale).

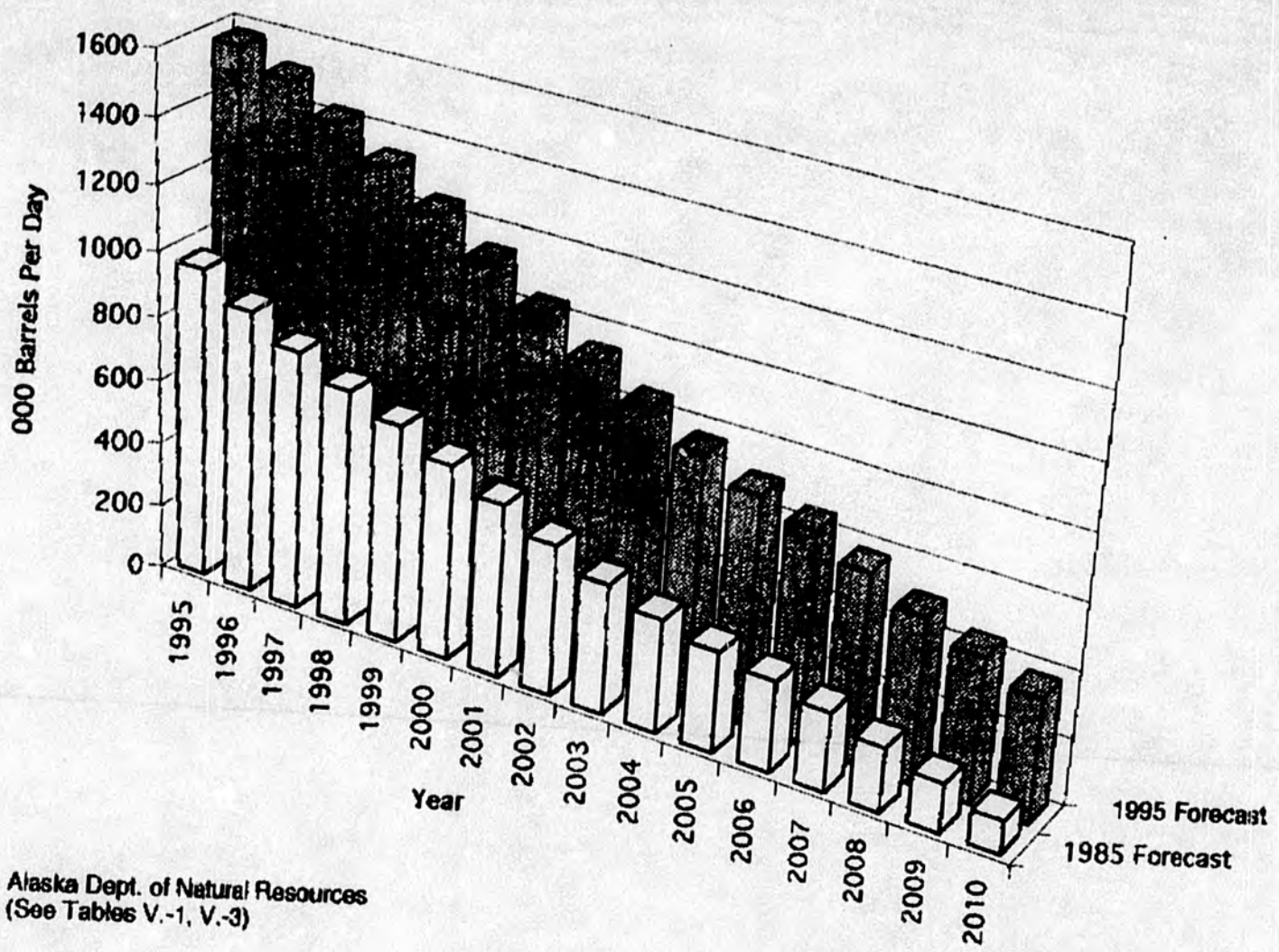
(2) Alaska Dept. of Natural Resources, "Historical and Projected Oil & Gas Consumption," February 1995 (in press), (Table 3: Historical Oil Production).

North Slope Production, 1986-1994: 1985 Forecast v. Actual



Source: Alaska Dept. of Natural Resources
(See Table V.-4)

North Slope Production Forecasts, 1995-2010 (1985 v. 1995 Forecast)



Source: Alaska Dept. of Natural Resources
(See Tables V.-1, V.-3)

03.16.1995 09:11

Table V-1.

Research Associates 2/95

1985 Production Forecast for 1995-2010 (Alaska Dept. of Natural Resources)
(000 bbls)

000 Barrels per day:

Year	Field =>	Prudhoe	Kuparuk	Lisburne	Pt. McIntyre	Endicott	Milne Pt.	Other	W.Sak	Beaufort	Total
1995		575	145	65		70	10	100	<=====		965 000 bpd
1996		510	120	60		65	0	125	<=====		880 "
1997		460	100	55		60		125	<=====		800 "
1998		420	80	50		55		125	<=====		730 "
1999		380	75	40		50		125	<=====		670 "
2000		340	65	30		45		120	<=====		600 "
2001		300	55	20		40		115	<=====		530 "
2002		270	50	10		20		110	<=====		460 "
2003		240	40	0		10		105	<=====		395 "
2004		210	35			0		100	<=====		345 "
2005		180	30					95	<=====		305 "
2006		160	25					90	<=====		275 "
2007		140	20					80	<=====		240 "
2008		110	15					70	<=====		195 "
2009		80	10					60	<=====		150 "
2010		50	0					50	<=====		100 "
Total Barrels:		1,615,125	315,725	120,450	0	151,475	3,650	582,175	<=====		2,788,600 (000 bbls.)

Source: Alaska Dept. of Natural Resources, "Historical and Projected Oil & Gas Consumption," January 1985, p. 13 (Table 2.2: Estimated Availability of N. Slope Oil For Sale).

Table V-2

Research Associates 2/95

1990 Production Forecast for 1995-2010 (Alaska Dept. of Natural Resources)
(000 bbls)

000 Barrels per day:											
Year	Field =>	Prudhoe	Kuparuk	Lisburne	Pt. McIntyre	Endicott	Milne Pt.	Niakuk	W Sak	Beaufort	Total
1995		857	190	37	60	65	10	20	12		1,251 000 bpd
1996		789	175	34	54	60	8	17	12		1,149 "
1997		726	150	31	49	55	7	14	25		1,057 "
1998		668	125	28	44	50	6	12	25		958 "
1999		614	105	25	39	45	5	10	50	0	893 "
2000		553	90	21	35	40	5	9	50	60	863 "
2001		498	75	19	32	20	5	7	75	54	785 "
2002		448	65	13	29	10	0	6	75	49	695 "
2003		403	55	9	26	0		5	100	44	642 "
2004		363	45	5	23			5	100	39	580 "
2005		326	35	0	21			0	150	35	567 "
2006		284	30		19				150	32	515 "
2007		247	25		17				150	29	468 "
2008		215	20		15				150	26	426 "
2009		187	15		14				140	23	379 "
2010		163	10		12				120	21	326 "
Total Barrels:		2,679,465	441,650	81,030	178,485	125,925	16,790	38,325	505,160	150,380	4,217,210 (000 bbls.)

Source: Alaska Dept. of Natural Resources, "Historical and Projected Oil & Gas Consumption," January 1990, p. 10 (Table 2.2: Production Forecast and Available Royalty Oil).

Table V.-3

Research Associates 2/95

1995 Production Forecast for 1995-2019 (Alaska Dept. of Natural Resources)

(000 bbls)

000 Barrels per day:

Year	Field =>	Prudhoe	Kuparuk	Lisburne	Pt. McIntyre	Indicott	Milne Pt.	Other	W.Sak	Beaufort	Total
1995		980	310	20	115	94	30	23		0	1,572 000 bpd
1996		921	305	20	115	83	40	23			1,507 "
1997		857	300	20	109	72	40	22			1,420 "
1998		788	300	18	98	63	45	22			1,334 "
1999		717	295	15	88	55	50	19	0		1,239 "
2000		646	285	13	79	47	45	16	6		1,137 "
2001		581	256	10	71	40	40	14	21		1,033 "
2002		523	231	10	64	34	36	11	27		936 "
2003		471	208	10	61	29	33	10	25		847 "
2004		423	187	10	54	24	30	9	26		763 "
2005		381	168	10	46	21	27	7	35		695 "
2006		343	143	10	39	18	24	6	59		642 "
2007		309	122	9	33	16	20	5	58		572 "
2008		278	103	8	28	13	17		49		496 "
2009		250	88	7	24	10	15		41		435 "
2010		225	75	6	21		12		35		374 "
Total Barrels:		3,172,945	1,232,240	71,540	381,425	225,935	183,960	68,255	139,430	0	5,475,730 (000 bbls.)

Source: Alaska Dept. of Natural Resources, "Historical and Projected Oil & Gas Consumption," February 1995 (in press), (Table 2A: Estimated Availability of N. Slope Oil For Sale).

Representative Norman Rokeberg

MEMORANDUM

TO: House Oil & Gas Committee Members

FROM: Representative Norman Rokeberg

DATE: March 7, 1995

SUBJECT: Royalty Reduction Incentive

How has 38.05.180 changed since statehood? Have royalty reductions been done in the past on old fields? Senator Leman has introduced legislation that reinstates a royalty provision that used to be on the books.

Explain what a delineated field is and what would be an acceptable measure? Do we need a definition?

It is clear from comments and legal reviews by three previous Commissioners of Natural Resources that the commissioner does not have the authority to reduce royalty on new fields until they have been in production for 2 years.

Should we delete what appears to be a Permanent Fund Hold Harmless provision which is a detriment to the revenues of the general fund? No

Is there any legal reason it is in the bill?

HB 207 is not clear as to whether it covers old and new fields, Section 2 Page 2, Lines 28-31? Yes both are covered

Why do we want a royalty reduction?

What kind of royalty reduction - sliding scale reduction that is tied to the price of oil?

Should the formula be stated in the bill?

Is the process of royalty reductions the stumbling block?

Page 2

What is the effect of royalty reduction on the income stream of the State of Alaska? Can the state afford to reduce its royalty share? Is the benefit of reducing Alaska's royalty share greater than the loss of revenue to the State?

Is tax clarity and tax stability a greater incentive? (All industry representatives in their presentations 2/1/95 to the Senate Resources Committee reiterated their concerns over and over again regarding tax stability and tax clarity, as well as the state getting its budget under control.)

Would it be better to decrease the severance tax?

Which is more important eliminating or reducing the State's royalty on old field marginal properties that are at an economic crossroads or reducing up front royalties on new, unknown fields?

Should the decision to grant a royalty reduction be accomplished by Commissioners of DNR, REV and Law? With the appeal oversight resting with the AGOCC?

What about a sunset provision?

Should the royalty formula be evaluated every 5 years?

Should the royalty formula be indexed?

How do we protect the integrity of the bid leasing program? We do not want successful bidders coming back later for a royalty reduction? (How do we protect bidding procedures?)

How does is an application reviewed by the commissioner on a unitized field, will all the partners get the same royalty reduction or does each partner has to submit an application? In section 2 of HB 207 will all partners on a unitized application be considered one application and have to present confidential data?

Is there a way to retain some of the current language in section 2 or conform it to HB 207? Reasonable Rate of Return on page 2

Should we put criteria in the bill that outlines the types of items that should be covered in the commissioner's best interest finding?

Ogan's questions:

Is there a fee for making a royalty reduction application? If not, could one be devised to offset the costs to the state for the extra work involved in a royalty reduction request?

The Fiscal Note attached to the bill indicates that one new person will be required?

Page 3

Do any of the other incentive programs require a fee for processing the applications?
In Section 2, page 3, line 9: the bill says that the commissioner may require the lessee to pay the costs of a 3rd party contractor to evaluate the application - should the bill be changed to require the lessee to pay the costs?

**ALASKA SUPPORT INDUSTRY ALLIANCE
TESTIMONY ON
HB 207, ADJUSTMENTS TO OIL AND GAS ROYALTIES
TO THE
HOUSE OIL AND GAS COMMITTEE
MARCH 15, 1995**

Good afternoon Chairman Rokeberg and members of the House Oil and Gas Committee. My name is Keith Burke. I am General Manager of the Alaska Support Industry Alliance. I have been a participant in Alaska's oil industry for the past 20 years. I am here today to represent The Alliance, myself and my family. I am here to encourage you to support HB 207.

This legislation will be a great step forward in reversing the downward trend in oil and gas exploration and development activities in Alaska. It also would encourage continued investment in development of Alaska resources by many major multi-national oil companies, the very companies who allow members of The Alliance to provide many quality jobs to our Alaskan employees.

Since 1990, four oil and gas companies have closed their offices and have suspended upstream operations in Alaska: Chevron, Conoco, Amoco, and Texaco.

Downturn in Labor Force/Loss of Jobs

Oil and gas companies have downsized and consolidated operations in an effort to affect maximum cost savings to remain competitive.

With the completion of GHX2, the last major construction project currently planned on the North Slope, job levels are anticipated to continue a slow and steady decline.

According to Neil Fried, Dept. of Labor, producers will probably experience a statewide decrease of 20 percent or more in 1995 over 1994. Producer employment from February, 1994 to February, 1995 shows a decrease of 18 to 19 percent. The combined downturn, factoring in support industry jobs, will probably be around 10 to 11 percent.

Since its peak in 1991 of more than 10,541 jobs, industry employment has declined substantially and is predicted to be approximately 8,000 in 1995, about the same level of employment as in 1987. Attached to copies of my testimony is a graph from the Dept. of Labor titled "Alaska's Oil Industry Employment is on the Wane".

According to the University of Alaska, Institute of Social and Economic Research, oil revenues provide 30 percent of Alaskans' personal income and account for one in every three jobs. As oil production and revenues decline, so too will the number of Alaska jobs supported by petroleum revenues.

Alaska Production/Revenue Decline

Alaska's revenue future closely tracks the continued depletion of petroleum reserves. (Table 1. (attached to my testimony) shows the Dept. of Revenue's Base Case projected petroleum revenues as a percent of total projected state unrestricted revenues.)

Current forecast scenarios project total Alaska oil production to decline at an average annual rate of 6 percent Fiscal Year 95 to Fiscal Year 2000, falling to one-half of current production levels by 2006, in the base case scenario. Although higher oil prices would offset some of the negative impact of lower production levels, ultimately revenues will fall barring some unforeseen oil discovery. (Table 2. (attached to my testimony) shows current and projected oil production through FY 2010.

Half of the oil production projected for the year 2000 and beyond depends on investments yet to be made. This means the fiscal outlook could be worse than current projections unless the state acts to ensure that the new investments implicit in Dept. of Revenue projections are actually made. If the industry is forced to cut back on investment, we'll not only sacrifice significant future growth, but near-term production could plummet as well.

Downturn in Exploration Indicative of Alaska's Lack of Competitive Edge

Lease sale activity is a first indication of industry interest - and exploration interest - in Alaska. It's one way to tell how well Alaska is competing with other areas around the world. Although the number of sales varies from year to year and areas offered varies, data indicate some long term trends. The most notable is that fewer companies are bidding, fewer rigs are active and fewer wells are being drilled.

Alaska Oil and Gas Association statistics indicate that the amount of acreage under lease for potential exploration has declined by nearly 40 percent since 1990.

The Key--Implement a strategy to make Alaska competitive in the world market to encourage capital investment to provide a sustainable economic base for future revenues and jobs.

Throughout the world, relationships between governments and companies are much more positive and creative than only a few years ago. Most governments understand that investors deserve a fair return on capital investment--returns that are comparable with what they could earn elsewhere with similar risk. They realize that investment resources are scarce and they realize there are significant mutual benefits to working cooperatively to develop their resources and share the rewards equitably.

Alaska is competitively disadvantaged:

- High transportation costs;

- Crude oil characteristics that discount North Slope oil compared to other crudes in the market;

- High exploration and development costs, long lead times;

- A state revenue structure that takes a bigger share of profits and no clear tax rules.

World oil prices plummeted in 1986 and, with the exception of a short-lived spike caused by the gulf war, have remained low. Adjusted for inflation, prices are about the same today as they were in the late sixties. Considering the distance to market and crude quality, Alaska North Slope crude averages only \$10 per barrel at the wellhead.

The bottom line is that returns on Alaska investments are at least \$1-2 per barrel lower than in similarly mature oil provinces.

The ability of the industry to bring investment capital into Alaska and the performance of investments also determine the flow of revenues to the state. This, in turn, increases or decreases state revenues.

New exploration is important for long term development, however, development of existing reserves is crucial to the state in the near term. There are a number of undeveloped North Slope oil accumulations, many of which would be on production if they were located in the Lower 48. (Attached, for your reference, is a listing of the accumulations and dates discovered.) Here, low oil prices, high development costs and high transportation costs make them uneconomic.

Alaska Support Industry Alliance
Testimony on HB 207
March 15, 1995
Page 4

If the state and the industry can work together to change the economic equation for marginal fields, Alaska's ability to compete for oil industry investment capital will improve and the common goal of sustained economic development that leads to stabilized revenues and stabilized jobs...for the industry and for Alaska...could become reality.

The three hundred Alliance member companies and their thousands of employees urge you to pass HB 207.

Thank you.

Attachments

B:ag5.NR.stats

FISCAL OUTLOOK **STATE OF ALASKA**

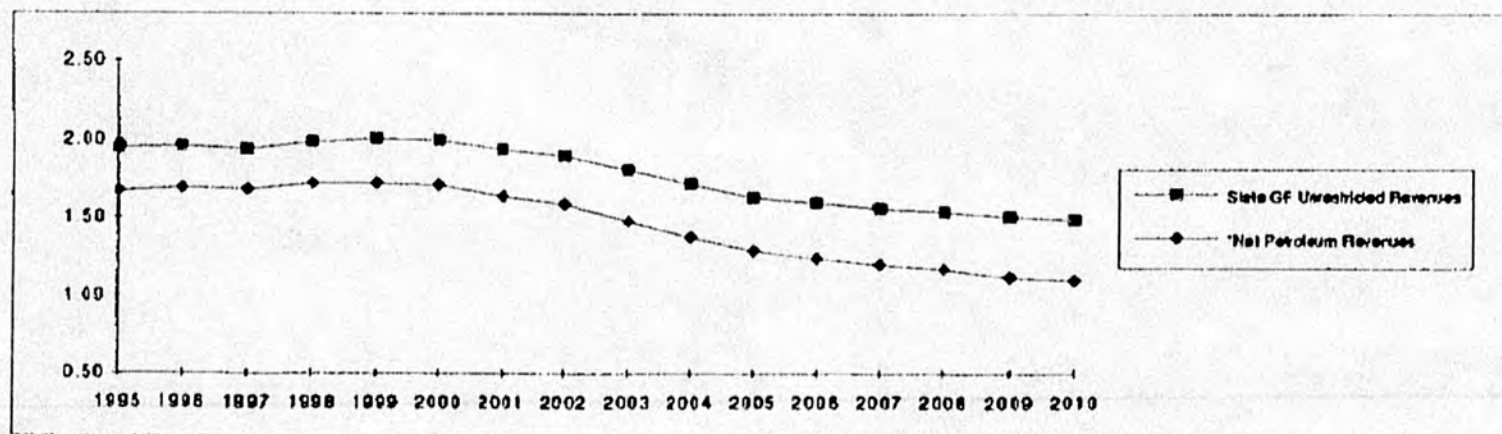
Alaska's revenue future closely tracks the continued depletion of petroleum reserves. Table 1. shows Dept. of Revenue's Base Case projected petroleum revenues as a percent of total projected state unrestricted revenues. Petroleum revenues are projected to account for approx. 80 % of state unrestricted revenues through 2010. Current forecast scenarios project total Alaska oil production to be one-half current levels (approx. .8 million bbl/day) by FY 2006 in the base case scenario.

Although higher oil prices would offset some of the negative impact of anticipated lower production levels, ultimately revenues will fall barring some unforeseen oil discovery.

For the base case scenario, oil prices are assumed to increase at .5 percent per year with inflation increasing from 3.86% in FY 96 to 4.38% FY 1997-FY 2000, and to 4.58% FY 2001- FY 2010.

Table 1.
**Projected Net General Fund
Unrestricted Revenues/ Projected Net-Petroleum Revenues
(Billions of Dollars)**

	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
State GF Unrestricted Revenues	1.95	1.96	1.94	1.99	2.01	2.00	1.94	1.90	1.81	1.72	1.63	1.60	1.56	1.54	1.51	1.49
*Net Petroleum Revenues	1.67	1.69	1.68	1.72	1.72	1.71	1.64	1.59	1.48	1.38	1.29	1.24	1.20	1.17	1.12	1.10
	86%	86%	86%	86%	85%	85%	84%	84%	82%	80%	79%	77%	77%	75%	74%	74%



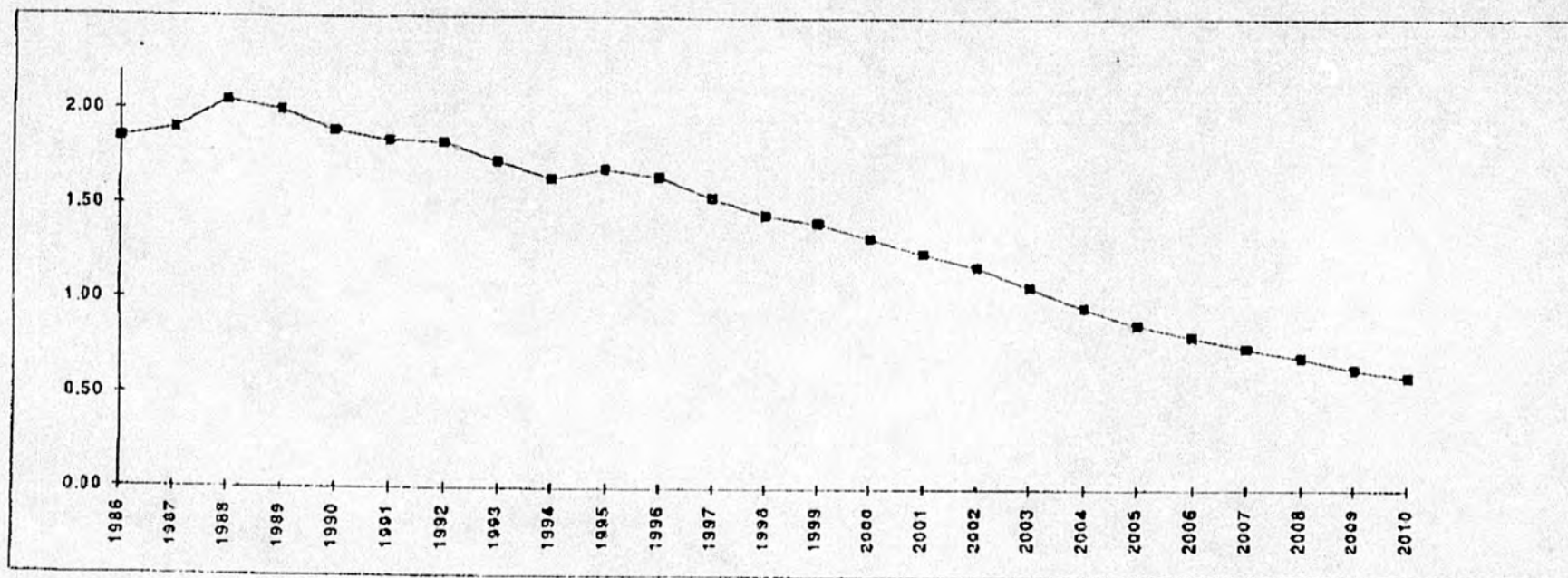
Source: Ak. Department of Revenue
*Net of Permanent Fund Contribution

As production from existing fields continues to decline, state revenues will decline accordingly. Table 2 shows current and projected oil production through 2010. Production is projected to decline 43% in the next 10 years, falling to 1978 production levels of .8 million barrels per day by FY 2006.

Table 2

**STATE OF ALASKA
PRODUCTION FORECAST 1986-2010
(MILLIONS BARRELS PER DAY)**

1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
1.85	1.87	2.05	2.00	1.89	1.84	1.83	1.73	1.64	1.69	1.65	1.54	1.45	1.41	1.33	1.25	1.18	1.07	0.95	0.87	0.81	0.75	0.70	0.64	0.60



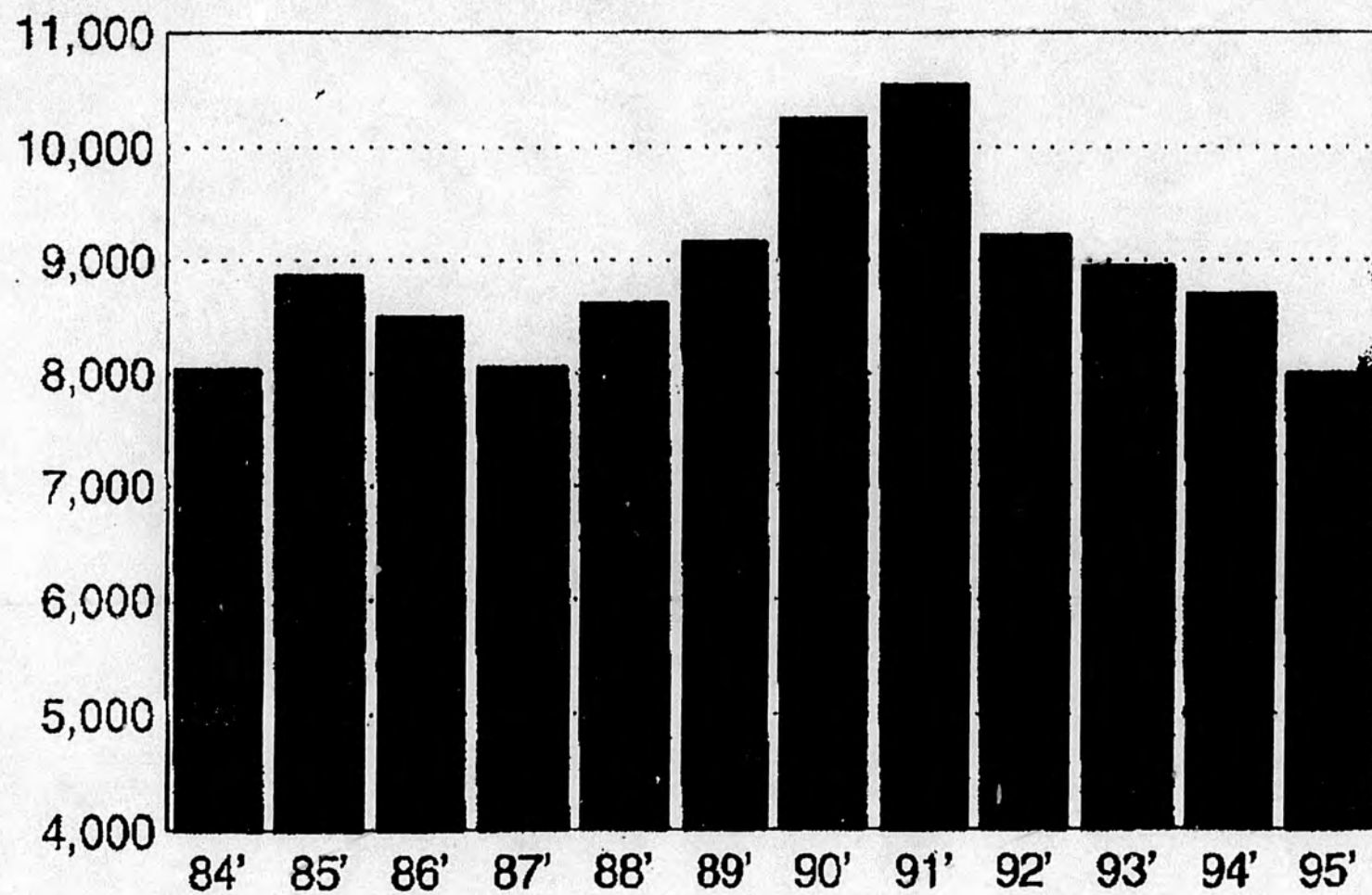
Source:

AK. Department of Revenue FY 1986-2010

Undeveloped North Alaska Hydrocarbons

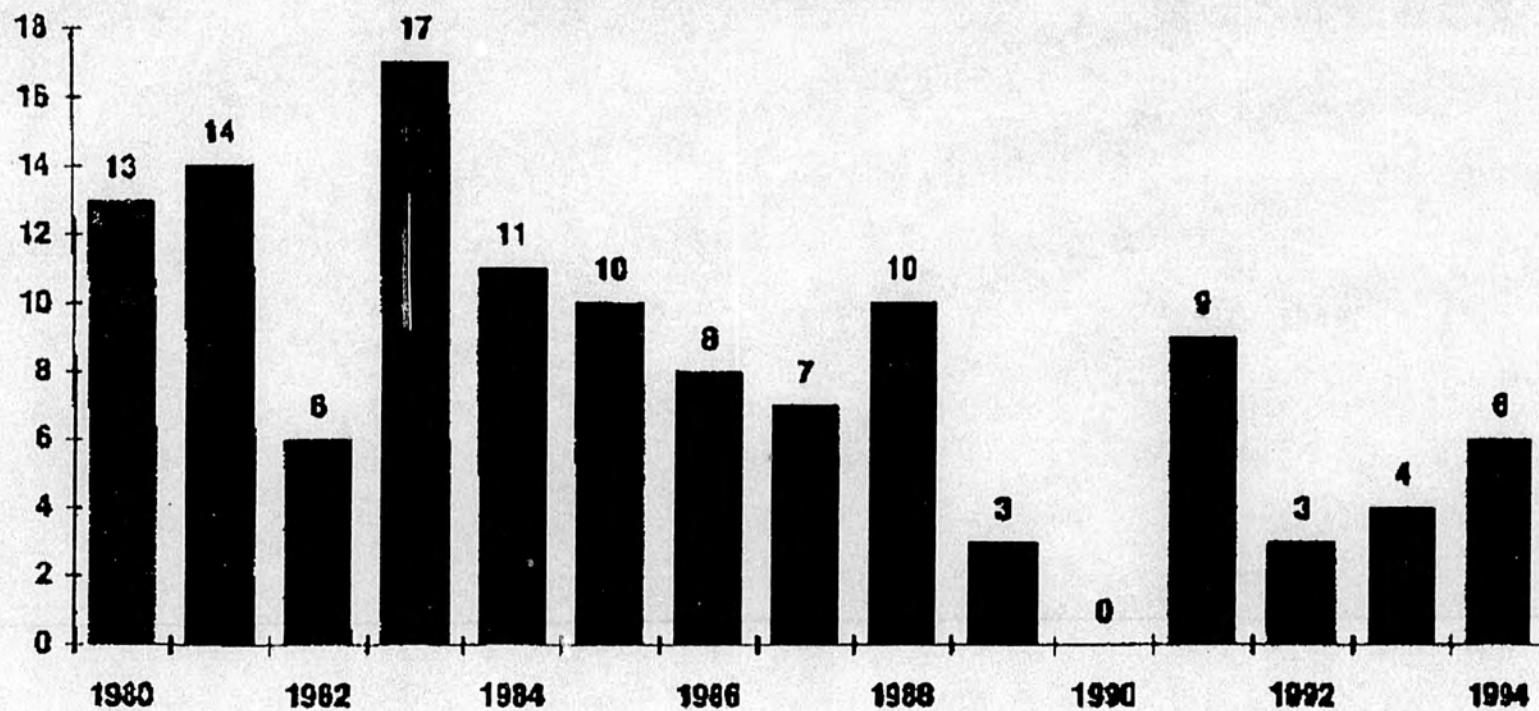
Umiat	1946	Point Thomson	1977
Fish Creek	1949	Tern Island	1982
Simpson	1950	North Star	1982
NS Natural Gas	1968	Hammerhead	1985
West Sak	1969	Colville Delta	1985
Ugnu	1969	Sandpiper	1986
Gwyder Bay	1969	Badami	1990
Flaxman Island	1975	Kuvlum	1992

Alaska's Oil Industry Employment Is On The Wane



Alaska Oil & Gas Lease Sales

Average Number of Bidders per Sale



3/10/95

ALASKA WELLS SPUDDED BY YEAR

YEAR SPUD	TALLY
70	68
71	30
72	28
73	38
74	46
75	73
76	82
77	72
78	98
79	109
80	138
81	197
82	229
83	183
84	213
85	311
86	200
87	121
88	149
89	139
90	161
91	151
92	148
93	193
94	140
95	2
	4332

Union Oil Company of California
Testimony on HB207
House Committee on Oil and Gas
March 16, 1995

Mr. Chairman and members of the Oil and Gas Committee—My name is Kevin A. Tabler, Land Manager for Union Oil Company of California (Unocal) in Alaska. I appreciate this opportunity to be heard today and to present Unocal's comments on House Bill 207. First I'd like to say, we are very encouraged with the positive atmosphere and effort expended, thus far, by the Legislature and Administration in trying to develop incentive legislation to enhance and stimulate further exploration and development throughout the State. We recognize and appreciate the concerted in-depth effort being made by your committee to fully assess the utilization and applicability of this Bill prior to subsequent referral. This time, spent early on, understanding the implications of the Bill, and providing the opportunity for intended users to clarify and augment specific sections, will greatly enhance its acceptability and help ensure its passage into legislation.

By broadening the applicability of AS 38.05.180 (j), we believe this Bill is a step in the right direction toward revising existing Statutes. This approach provides additional opportunity for certain marginally economic fields to compete both, internally within a company and externally on a global basis. But, before I address specifics under Section 2., I would like to make a brief comment about Section 1.

Unocal is taking a neutral position on the appropriateness or need to revise the funding mechanism previously established for the Alaska permanent fund under AS 37.13.010(a). The sharing of revenues and proceeds derived through leasing, exploration and development of the States mineral wealth, split between the permanent fund and general fund, is not the focus of our analysis of this Bill. Our focus and concern of the Bill is one of clarification, administration and utilization as it pertains to our Cook Inlet operations.

Section 2.

Last Thursday, I listened to a discussion during the first hearing on this Bill regarding the need to define the term "field". Bill Van Dyke did an excellent job of explaining the differences between fields, pools, horizons, and the delineation of same, in the context of the applicability of each, regarding this Section. To help clarify and more accurately describe the aerial extent of an accumulation for which this Section would apply, we offer the following suggestions. On line 29, page 2 after the word field, insert ", pool or portion of a field or pool". On line 30, we would suggest that the word "an" be eliminated and the words "a producing" be inserted between "of" and "oil". The same wording suggested on line 29,

would apply after the word "field" on line 30. The application here is that the AOGCC has clearly defined pools and separate horizons or zones associated with any recognized field. Similar testimony was provided Tuesday by DNR and we support their modification.

Our second comment is related to lines 8 thru 10 on page 3. As a condition of evaluating an application and data, the commissioner may require the lessee to pay the costs of contractors selected by the commissioner to assist in the evaluation. We feel all attempts should be made to utilize existing DNR staff wherever possible to reduce costs. On Thursday, the commissioner indicated the intent of this subsection was to have mutual agreement between the applicant and the commissioner as to the selection of contractors. We believe it is important to spell this out in the Bill. Equally important is the need to mutually agree on the costs contemplated for expenditure by lessee, prior to the hiring of a contractor. For extremely marginal properties, such as our Stump Lake Unit, the cost of hiring a consultant (at say \$20,000 -- a likely amount) could eliminate most of the benefit derived from royalty reduction. This Bill currently has no control over costs. Alternatively we heard from commissioner Dave Johnston of AOGCC on Tuesday, recommending that the applicant hire and pay for the contractor in support of its application to control costs. The commissioner of DNR would provide a list of contractors that would be acceptable to DNR and the applicant would then have the ability to select one for the analysis. This approach makes the most sense, in that the company would then be able to negotiate the best price possible and thereby have some control on costs. We would support this concept. This preferred approach would also eliminate the need for the costly and time consuming RFP process DNR would have to employ.

The elimination of the reasonable rate of return criteria on lines 13 thru 17 page 3 is a positive step in cleaning up the Statute. This determination is too subjective and open to debate. It is unrealistic to think that common agreement will ever be reached by any two parties. This requirement is unnecessary and therefore is better left out.

We need a very clear understanding that modifications made to existing Statutes do not inadvertently have a debilitating or limiting effect on the mature, marginally economic future development of Cook Inlet. There is a monumental difference between the exhausted fields typically found in Cook Inlet as opposed to those on the North Slope.

The next two comments are very important to Unocal and its operations in Cook Inlet, but first, let me give you an example of one economic scenario involving our platform operations:

Four (4) of the ten (10) Unocal operated producing platforms produce less than 2,000 BOPD each. One (1) produces less than 900 BOPD. Expenses on all of these properties make them marginally profitable. In an effort to increase production, Unocal committed over \$80 million in capital investments over the last two years, with the potential to spend an additional \$31 million in 1995 on these four (4) platforms. At this point, it is difficult to commit additional capital to develop these properties due to their short remaining platform lives and marginal profitability. Reducing or eliminating the state's royalty on these marginal properties could make the projects economically viable and significantly increase the economic life of the platforms, thereby maintaining employment and the associated community benefits. For fields or platforms facing abandonment today, such as a platform with less than 1000 BOPD, complete royalty relief is warranted. These properties provide minimal income to the state and complete royalty relief will extend field life and employment by about years.

Lines 17 thru 21 provide for a modification and change to the existing Statue, limiting the commissioners ability to reduce royalty by specifying certain limits. We propose this additional language and limitation be taken out in its entirety. We believe it is in the state's best interest for the commissioner to have the flexibility to reduce royalty down to 0, as currently provided, given a finding on the part of the commissioner, supported by financial and technical data which demonstrates the benefits of such action is warranted.

Lines 23 and 24 need revisions to eliminate the unilateral right of the commissioner to increase royalty beyond the state's original royalty share prior to any reduction on a previously producing mature field or re-establishment of commercial production of shut-in oil or gas. The big upside potential of a field, as discussed last Thursday and again at Tuesday's hearing, only applies to delineated but not previously produced fields where one may reasonably expect a pleasant surprise. A previously negotiated change in royalty at the time of the initial reduction, under strict criteria, may be warranted in the case of a delineated but not previously produced field. Bids were made on leases and evaluated on known parameters and an economic analysis at the time of bidding. Companies need the opportunity to evaluate any royalty change upward in light of field economics and overall company economics, and agree to any royalty modifications prior to committing manpower and capital to a project. It's not realistic to anticipate that mature producing fields hold the same type of promise. For the commissioner to have unilateral authority to increase the royalty rate to whatever level beyond the royalty originally specified in the lease, is not warranted in these mature fields. For mature fields, the impact of price only effects extending field life. If we are opening ourselves to the possibility of higher future royalty by applying for a reduction today, we may be eliminating the incentive to apply. Companies need certainty for planning and capital commitment purposes.

Line 1 on page 4 indicates the commissioner's decision regarding a request is final and not appealable. This really is no change from the current Statute. If this provision is of concern to the committee or the Legislature, then perhaps a peer review of the decision could be conducted. In Tuesday's hearing, the AOGCC provided a couple of alternative approaches to address the concern of oversight and appealability, both of which are acceptable to Unocal.

In conclusion, We believe this Bill has the potential to add certain attractive parameters to the administration of the royalty reduction process. For Unocal, at this time, this Bill has application only to our existing producing fields. Page 3 changes proposed in the bill, further restrict Unocal's ability to seek royalty relief beyond what is currently in Statute and make it difficult to support in its current form. With the changes we have proposed, we believe the interests of all parties are protected while at the same time afford the commissioner the discretion he is entitled under current Statute.

Unocal already has in place a vehicle under current Statute to address the concerns of its marginal fields in Cook Inlet, as they reach their economic limit. Albeit not an ideal vehicle, at least one which is less onerous than that which is proposed. Although we like the ability to expand the applicability of this Statute, and eliminate the requirement for a subjective reasonable rate of return determination, the potential for increased royalty beyond that which was originally agreed and an arbitrary floor placed on the amount royalty may be reduced, eliminates flexibility and hurts our efforts toward field life extension in Cook Inlet.

We look forward to working with the Legislature as this Bill progresses through the legislative process.

Thank You

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(907) 248-5078

MAR 10 1995

March 6, 1995

Senator Loren Leman
State Senate - Resources Committee
Alaska Legislature
Mail Stop 3100
State Capitol
Juneau, Alaska 99801-1182

✓ Representative Norman Rokeberg
State House - Oil and Gas Committee
Alaska Legislature
Mail Stop 3100
State Capitol
Juneau, Alaska 99801-1182

Re: SB 101/HB 207 - Royalty reduction for non-producing oil and gas leases.

Dear Senator Leman and Representative Rokeberg:

I am very much opposed to the substance of Governor's proposed changes to AS 38.05.180(j) and (p), embodied in SB 101/HB 207. If enacted, the changes would signal the abandonment of the open and fair competitive bidding framework that has successfully guided exploitation of our natural resources since statehood. The changes would also entirely preclude any public questioning of DNR commissioner decisions that are of the greatest importance to the development of Alaska oil and gas reserves and to future state revenues.

Under current law in AS 38.05.180(j), the DNR commissioner is allowed to reduce royalties "(t)o prolong the economic life of an oil and gas field or to reestablish commercial production of shut-in oil or gas that would not otherwise be economically feasible." *Id.* Royalty reduction is not permitted, however, unless the lessee makes a "clear showing" that the lessee's revenue from the field "is and is likely to continue to be insufficient to produce a reasonable rate of return with respect the lessee's total investment in the field." Long ago, the commissioner was directed by law to adopt regulations implementing subsection (j), regulations which are now at 11 AAC 83.185. These regulations require a lessee seeking a royalty reduction to make a formal application to the commissioner that contains all the relevant facts needed for an informed commissioner decision, including such elementary information as the "expenses and costs" of operating the lease. See 11 AAC 83.185(a)(1) - (4). The regulations further require the commissioner to give notice of and hold a public hearing concerning the application, to make a formal written finding, and to give the public notice of it. The commissioner decision is subject to court review, via 11 AAC 02 and settled principles of law, including AS 44.62 (the Alaska Administrative Procedure Act).

The substantive and procedural provisions of current law strike a delicate balance. They allow the commissioner to make mutually advantageous adjustments to leases in older, faltering oil and gas fields, but only if there is adequate public notice and the potential for judicial review. Public notice and the potential of judicial review are needed to prevent the unfair treatment of a lessee's competitors, to prevent any unnecessary decline in state revenues, and to insure that the commissioner will not make a decision for corrupt or otherwise illicit reasons.

The Governor's proposed changes to AS 38.05.180(j) (in section 2 of both the House and Senate bill) strip away many, if not most, of the foregoing substantive and procedural protections. The bill adds to the existing reasons for royalty reduction a new one: "(t)o allow for production from a delineated but not previously produced field that would not otherwise be economically feasible...." The proposal does not expressly define "delineated" or "field," but clearly a field can be bigger, or smaller, than the boundaries of a lease. Moreover, it is the obvious intent of the bill that the changes be broadly encompassing, since section 3 of the bill also proposes changes to AS 38.05.180(p) which would allow the commissioner to "reduce royalty on leases in connection with a cooperative or unit plan ... as provided in (j) of this section." The effect of all this creates the potential of a general re-opener for all non-producing leases, no matter how new or old, and perhaps even for those non-producing leases in "fields" of otherwise high continuing production.

Even under the narrowest of constructions, however, if enacted the Governor's proposal would represent a major change in how the state leases its oil and gas lands. The state has always relied on free market forces, operating through open competitive bidding, to determine the best value for its resources. Under existing law and standard lease terms, a lessee which has not produced paying quantities of oil and gas during the lease term may assign the lease to another or let the lease expire instead of making further investment in the leased lands. If the lease expires, the state may re-offer the lands for lease and gain whatever economic benefit that competitive, open, and fair bidding will produce. The economic benefit may turn out to be the same, a different, a lower, or a higher royalty, but this is a result produced by free market forces, not through the guesswork of government bureaucrats.

The Governor's bill would substitute for free market forces an entirely private process open to outright skullduggery, to the subtleties of political favoritism and influence peddling, or to just plain stupid decision-making. This is because the proposed changes include deletion of the command under existing law that commissioner "shall adopt regulations," thus creating the clear implication that the existing regulations would no longer operate. It is these regulations which now require that the lessee submit a factually detailed application, that the public, including competing bidders and competing lessees, be notified, and that a public hearing be held, all protections designed to make sure the commissioner's decision has solid grounding in the public interest. 11 AAC 83.185. I urge you to inquire whether it is the intent of the drafters of the bill to abandon the existing regulations, or whether they believe that public notice and hearing would be required by other provisions in AS 38.05, particularly AS 38.05.035.

Under the Governor's proposal, the lessee is required "to disclose financial and technical data that demonstrate that the requirements of this subsection for a reduction are

met." However, there are no additional or special "requirements of this subsection" set out, unless the vague mandate that the royalty reduction be in the "best interests of the state" is deemed a "requirement," or unless one views the one of the justifications for royalty reduction, delineated in existing law and the opening clause of the Governor's proposed version of AS 38.05.180(j), as establishing "requirements." By the way, the "best interests" language of the Governor's proposal merely restates a mandate already on the books. See AS 38.05.035(e).

While the "best interests" language adds nothing new, the Governor's bill would eliminate restrictions expressly designed to protect the state's --- as opposed to a pleading lessee's --- best interests. The bill proposes the deletion of the existing statutory requirement that the commissioner find that "the state has obtained the maximum possible economic return that is compatible with allowing a reasonable rate of economic return for the lessee." AS 38.05.180(j). While the Governor's proposal would put side bars on the amount of royalty reduction allowed (extremely generous side bars at that, 50% to 75%, depending on the age of the lease), and would allow the royalty to rise if the conditions changed, the royalty can never go higher than that called for in the original lease. This obviously is very one sided; the state can get less royalty than it originally bargained for, but it never can get more. Certainly, if bad times are to be shared with a lessee, shouldn't good times should be shared as well?

While the defects in the Governor's bill might not be so bad if the important, paramount value of public notice and oversight was clearly preserved, under the Governor's proposal the lessee can demand that the data submitted in connection with a royalty reduction application be kept completely confidential. Wholesale confidentiality would effectively preclude any real legislative, much less public, review and oversight. And what lessee won't demand confidentiality?! It is almost a sham, then, for the Governor's proposal to add the requirement that the commissioner "make public a written finding that the reduction meets the requirements of this subsection and is in the best interests of the state."

(Underscored material proposed by section 2 of the Governor's bill.) What good does a publicized finding do a public not allowed to see the data supporting the decision? Why suddenly can't the public be trusted with the lessee's supporting data, as has been allowed in the past under existing law?

Of equal concern is the fact that the Governor's proposal forbids any judicial review of a commissioner decision: "The commissioner's decision regarding a request for reduction under this subsection is final and not appealable to the court." [Second to the last sentence, section 2 of the bill, amending AS 38.05.180(j).] It may make sense to forbid a lessee denied a royalty reduction the right to appeal, but why shouldn't a member of the public --- and in particular, other lessees --- be allowed to challenge the fairness of a royalty reduction? Why shouldn't such an important public policy decision be subject to judicial review? And what good does it do the public to find out, after the fact, about a decision it is then forbidden to challenge? The Legislature should be gravely concerned about the lack of appeal rights in the Governor's bill. The concept raises serious legal questions concerning the amount of authority that can be delegated to an appointed official, and concerning the extent of the Legislature's power to prohibit a court from taking jurisdiction of a challenge to a natural resource disposal alleged to be consistent with the Alaska Constitution.

It is very distressing that responsible public officials might so quickly buy into certain oil and gas companies' arguments that existing leases or fields may not be "economic." Milne

Point serves to illustrate the important point that each oil company has a different set of abilities and motivations, economic and otherwise, and government bureaucrats and politicians are ill advised to try and sort them out. Conoco could not make a go of Milne Point --- for whatever reason --- and traded it out to BP. While Conoco was the operator, many would have called Milne Point a marginal area, perhaps not "economically feasible." BP, however, with a different set of abilities and motivations, is now going great guns with Milne Point, and will pay the same royalty rate, 20%, that Conoco's lease called for. Who would have predicted this five years ago? The point is that the best remedy for a non-producing lease that the lessee claims cannot be made economic is not an amended lease, negotiated behind closed doors, but a new lessee selected by the free market forces.

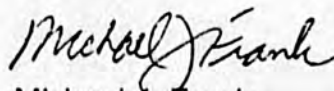
Ironically, if enacted the Governor's proposal might actually induce bidders for oil and gas leases to overbid lease royalties, knowing that there always exists the possibility that the DNR commissioner might later rescue them from their imprudence. This will encourage unreliable speculators into the market for oil and gas leases, the kind of companies least able and least likely to explore successfully for oil and gas and produce it for market when found.

There are a couple of items in the Governor's bill I support, such as clarifying the burden of proof on the applicant for a royalty reduction, and giving the commissioner the authority to require the applicant to pay the state's costs in retaining experts to evaluate the application. As it stands, however, the existing law already provides the commissioner sufficient latitude, acting subject to important safeguards of the public's interest, to reduce royalties in situations of severely declining or shut-in production. This latitude should not be broadened. The Governor's bill would grant appointed state officials too much power to do what government bureaucrats routinely prove they are unable to do well --- second guess the free market system.

I have an interest, but no expertise, in Alaska oil and gas law, so I can't guarantee that my statutory and bill analysis is correct. I also am not sufficiently familiar with the lease and royalty array in Alaska's oil and gas fields to understand what the Governor's bill might portend in terms of revenue loss to the state, both in the near and long term. I therefore urge you to skeptically and critically examine the Governor's bill with the help of *objective* experts, and in particular analyze the monetary implications of what is being proposed, field by field.

Thank you for considering my comments.

Sincerely,


Michael J. Frank

cc: Governor Tony Knowles

9-GH0039AK
Chenoweth
3/23/95

CS FOR HOUSE BILL NO. 207()
IN THE LEGISLATURE OF THE STATE OF ALASKA
NINETEENTH LEGISLATURE - FIRST SESSION

BY

Offered:
Referred:

Sponsor(s): HOUSE RULES COMMITTEE BY REQUEST OF THE GOVERNOR
A BILL

FOR AN ACT ENTITLED

1 "An Act relating to adjustments to royalty reserved to the state to encourage
2 otherwise uneconomic production of oil and gas; and providing for an effective
3 date."

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

5 * Section 1. LEGISLATIVE INTENT. In amending AS 38.05.180(j) in sec. 2 of this Act
6 to permit the commissioner of natural resources to initiate a reduction of royalty to encourage
7 otherwise uneconomic production of oil and gas from marginal fields and pools upon a finding
8 that the royalty reduction is in the best interests of the state, it is the intent of the legislature
9 that the commissioner of natural resources shall determine, in all cases, that the person or
10 persons app'ying for the royalty reduction would not make the additional investments that are
11 necessary to develop or prolong the economic life of the oil or gas field without the approval
12 of the royalty reduction.

13 * Sec. 2. AS 38.05.180(j) is amended to read:

14 (j) The [TO PROLONG THE ECONOMIC LIFE OF AN OIL AND GAS

1 FIELD OR TO REESTABLISH COMMERCIAL PRODUCTION OF SHUT-IN OIL
2 OR GAS THAT WOULD NOT OTHERWISE BE ECONOMICALLY FEASIBLE,
3 THE] commissioner

4 (1) may [SHALL ADOPT REGULATIONS TO] allow reduction of
5 royalty on individual leases or leases unitized as described in (p) of this section or
6 subject to an agreement described in (s) or (t) of this section

7 (A) to allow for production from an oil or gas field, pool, or
8 portion of a field or pool if

9 (i) the oil or gas field, pool, or portion of the field or
10 pool has been sufficiently delineated to the satisfaction of the
11 commissioner;

12 (ii) the field, pool, or portion of the field or pool has
13 not previously produced commercial quantities of oil or gas; and

14 (iii) oil or gas production from the field, pool, or
15 portion of the field or pool would not otherwise be economically
16 feasible;

17 (B) to prolong the economic life of an oil or gas field, pool,
18 or portion of a field or pool as per barrel or barrel equivalent costs
19 increase or as the sale value of oil or gas decreases, and the increase or
20 decrease is sufficient to make future production no longer economically
21 feasible; or

22 (C) to reestablish commercial production of shut-in oil or
23 gas that would not otherwise be economically feasible;

24 (2) [. THE COMMISSIONER] may not grant a reduction of royalty
25 unless the lessee or lessees requesting the reduction make [MAKES] a clear and
26 convincing showing that a reduction of royalty meets the requirements of this
27 subsection and is in the best interests of the state;

28 (3) shall, if the royalty reduction agreement is approved, [THE
29 REVENUE FROM THE LESSEE'S SHARE OF ALL HYDROCARBONS
30 PRODUCED FROM THE FIELD IS AND IS LIKELY TO CONTINUE TO BE
31 INSUFFICIENT TO PRODUCE A REASONABLE RATE OF RETURN WITH

1 RESPECT TO THE LESSEE'S TOTAL INVESTMENT IN THE FIELD. THE
2 COMMISSIONER MAY] condition the [A] royalty reduction granted under this
3 subsection in any way necessary to protect the state's best interests; under this
4 subsection, the commissioner shall include provisions to modify the state's royalty
5 share by a sliding scale royalty or other mechanism upon a showing, by clear and
6 convincing evidence, that, because of a sufficient change in one or more of the
7 following factors, further development or continued production of the field, pool,
8 or portion of the field or pool is not economically feasible: [INTEREST,
9 INCLUDING RESTORATION OF THE STATE'S ROYALTY SHARE IN THE
10 EVENT OF AN INCREASE IN] the sale price of oil or gas, proved reserves, field
11 productivity, or capital investment in the oil or gas field, pool, or portion of the
12 field or pool;

13 (4) shall, as part of the royalty reduction application, require the
14 lessee or lessees to submit, with the application for the royalty reduction, financial
15 and technical data that demonstrates that the requirements of this subsection are
16 met; the commissioner

17 (A) may require disclosure of only the financial and
18 technical data relating to production that is reasonably available to the
19 applicant; and

20 (B) shall keep the data confidential under AS 38.05.035(a)(9)
21 upon the lessee's request;

22 (5) shall give notice of the written findings and determination to the
23 lessee and to any other person who has filed a written request for it; subject to
24 (7) of this subsection, the commissioner's determination of royalty reduction is
25 final and not appealable to the court;

26 (6) may require the lessee or lessees making application for the
27 royalty reduction to retain and pay for the services of a contractor, selected by
28 the lessee or lessees from a list of nationally recognized consultants in
29 hydrocarbon production and economics provided by the commissioner, to assist
30 the commissioner in evaluating the application and financial and technical data;
31 when the commissioner requires the lessee or lessees to retain the services of a

1 contractor under this paragraph, the commissioner shall determine the relevant
2 scope of the work to be performed by the contractor;

3 (7) may not make a determination that gives final approval to an
4 application for a royalty reduction under this subsection unless the commissioner
5 first

6 (A) requests and receives the recommendation of the Alaska
7 Oil and Gas Conservation Commission, which shall, within 30 days of
8 submission of the proposed royalty reduction decision by the commissioner,
9 determine whether the proposed royalty reduction meets the requirements
10 of this subsection and is in the best interests of the state;

11 (B) transmits copies of the commissioner's final approval
12 determination and of the determination made by the Alaska Oil and Gas
13 Conservation Commission, if any, to

14 (i) the presiding officer of each house [. BEFORE
15 APPROVING A ROYALTY REDUCTION, THE COMMISSIONER
16 SHALL MAKE A WRITTEN FINDING THAT THE STATE HAS
17 OBTAINED THE MAXIMUM POSSIBLE ECONOMIC RETURN
18 THAT IS COMPATIBLE WITH ALLOWING A REASONABLE
19 RATE OF ECONOMIC RETURN FOR THE LESSEE, AND SEND
20 COPIES OF THE FINDING TO ALL MEMBERS] of the legislature;

21 (ii) the chairs of the legislature's standing committees
22 on resources; and

23 (iii) the chairs of the legislature's special committees
24 on oil and gas, if any;

25 (8) is not limited by the provisions of AS 38.05.134(3) or (f) of this
26 section in the commissioner's determination under this subsection.

27 * Sec. 3. AS 38.05.180(p) is amended to read:

28 (p) To conserve the natural resources of all or a part of an oil or gas pool,
29 field, or like area, the lessees and their representatives may unite with each other, or
30 jointly or separately with others, in collectively adopting or operating under a
31 cooperative or a unit plan of development or operation of the pool, field, or like area,

1 or a part of it, when determined and certified by the commissioner to be necessary or
2 advisable in the public interest. The commissioner may, with the consent of the
3 holders of leases involved, establish, change, or revoke drilling, producing, and royalty
4 requirements of the leases and adopt regulations with reference to the leases, with like
5 consent on the part of the lessees, in connection with the institution and operation of
6 a cooperative or unit plan as the commissioner determines necessary or proper to
7 secure the proper protection of the public interest. The commissioner may not
8 reduce royalty on leases in connection with a cooperative or unit plan except as
9 provided in (j) of this section. The commissioner may require oil and gas leases
10 issued under this section to contain a provision requiring the lessee to operate under
11 a reasonable cooperative or unit plan, and may prescribe a plan under which the lessee
12 must operate. The plan must adequately protect all parties in interest, including the
13 state.

14 * Sec. 4. This Act takes effect immediately under AS 01.10.070(c).

CS FOR HOUSE BILL NO. 207(O&G)

IN THE LEGISLATURE OF THE STATE OF ALASKA

NINETEENTH LEGISLATURE - FIRST SESSION

BY THE HOUSE SPECIAL COMMITTEE ON OIL AND GAS

Offered:

Referred:

Sponsor(s): HOUSE RULES COMMITTEE BY REQUEST OF THE GOVERNOR

A BILL

FOR AN ACT ENTITLED

1 "An Act relating to adjustments to royalty reserved to the state to encourage
2 otherwise uneconomic production of oil and gas; and providing for an effective
3 date."

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

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

6 (j) The [TO PROLONG THE ECONOMIC LIFE OF AN OIL AND GAS
7 FIELD OR TO REESTABLISH COMMERCIAL PRODUCTION OF SHUT-IN OIL
8 OR GAS THAT WOULD NOT OTHERWISE BE ECONOMICALLY FEASIBLE,
9 THE] commissioner

10 (1) may [SHALL ADOPT REGULATIONS TO] allow reduction of
11 royalty on individual leases or leases unitized as described in (p) of this section

12 (A) to allow for production from an oil or gas field, pool, or
13 portion of a field or pool if

14 (i) the oil or gas field, pool, or portion of the field or

1 pool has been sufficiently delineated to the satisfaction of the
2 commissioner;

3 (ii) the field, pool, or portion of the field or pool has
4 not previously produced oil or gas; and

5 (iii) production from the field, pool, or portion of the
6 field or pool would not otherwise be economically feasible;

7 (B) to prolong the economic life of an oil or gas field, pool,
8 or portion of a field or pool, as per barrel or barrel equivalent costs
9 increase in the later stages of production decline; or

10 (C) to reestablish commercial production of shut-in oil or
11 gas that would not otherwise be economically feasible;

12 (2) [THE COMMISSIONER] may not grant a reduction of royalty
13 unless the lessee or lessees requesting the reduction make [MAKES] a clear and
14 convincing showing that a reduction of royalty meets the requirements of this
15 subsection and is in the best interests of the state;

16 (3) shall, if the royalty reduction agreement is approved, in the
17 royalty reduction agreement, [THE REVENUE FROM THE LESSEE'S SHARE OF
18 ALL HYDROCARBONS PRODUCED FROM THE FIELD IS AND IS LIKELY TO
19 CONTINUE TO BE INSUFFICIENT TO PRODUCE A REASONABLE RATE OF
20 RETURN WITH RESPECT TO THE LESSEE'S TOTAL INVESTMENT IN THE
21 FIELD. THE COMMISSIONER MAY] condition a royalty reduction granted under
22 this subsection in any way necessary to protect the state's best interests; under this
23 subsection, the commissioner shall include provisions to increase or otherwise
24 modify the state's royalty share by a sliding scale royalty or other mechanism
25 upon the occurrence of a change [INTEREST, INCLUDING RESTORATION OF
26 THE STATE'S ROYALTY SHARE IN THE EVENT OF AN INCREASE] in the price
27 of oil or gas, and may consider other relevant factors, such as proved reserves,
28 well productivity, or capital investment in the oil or gas field, pool, or portion of
29 the field or pool;

30 (4) may not grant a royalty reduction for a field, pool, or portion
31 of a field or pool under (1)(A) of this subsection that exceeds 75 percent of the

1 royalty originally specified in a lease entered into under the provisions of (f) of
2 this section or AS 38.05.134;

3 (5) shall, as part of the royalty reduction application process,
4 require the lessee or lessees to submit, with the application for the royalty
5 reduction, financial and technical data that demonstrates that the requirements
6 of this subsection are met; the financial and technical data required by the
7 commissioner

8 (A) may not require disclosure of data relating to
9 production before the lessee or lessees obtained ownership of the lease if
10 the reduction application involves a lease described in (1)(B) or (C) of this
11 subsection; and

12 (B) shall be kept confidential under AS 38.05.035(a)(9) upon
13 the lessee's request;

14 (6) shall give notice of the written findings and determination to the
15 lessee and to any other person who has filed a written request for it; subject to
16 (8) of this subsection, the commissioner's determination is final and not appealable
17 to the court;

18 (7) may require the lessee or lessees making application for the
19 royalty reduction to retain and pay for the services of a contractor, selected by
20 the lessee or lessees from a list provided by the commissioner, to assist the
21 commissioner in evaluating the application and financial and technical data; when
22 the commissioner requires the lessee or lessees to retain the services of a
23 contractor under this paragraph, the commissioner shall determine the relevant
24 scope of the work to be performed by the contractor;

25 (8) may not make a determination that gives final approval to an
26 application for a royalty reduction under this subsection unless the commissioner
27 first

28 (A) submits the proposed royalty reduction decision to and
29 obtains the approval of at least three of the five members of the Alaska
30 Royalty Oil and Gas Development Advisory Board other than the
31 commissioner of natural resources; for purposes of this subparagraph,

1 after submission of the proposed royalty reduction under this
2 subparagraph, the Alaska Royalty Oil and Gas Development Advisory
3 Board has 30 days in which to evaluate the commissioner's submission and
4 to determine that the proposed royalty reduction meets the requirements
5 of this subsection and is in the best interests of the state;

6 (B) transmits copies of the determination made by the
7 Alaska Royalty Oil and Gas Development Advisory Board to

8 (i) the presiding officer of each house [. BEFORE
9 APPROVING A ROYALTY REDUCTION, THE COMMISSIONER
10 SHALL MAKE A WRITTEN FINDING THAT THE STATE HAS
11 OBTAINED THE MAXIMUM POSSIBLE ECONOMIC RETURN
12 THAT IS COMPATIBLE WITH ALLOWING A REASONABLE
13 RATE OF ECONOMIC RETURN FOR THE LESSEE, AND SEND
14 COPIES OF THE FINDING TO ALL MEMBERS] of the legislature;

15 (ii) the chairs of the legislature's standing committees
16 on resources; and

17 (iii) the chairs of the legislature's special committees
18 on oil and gas, if any;

19 (9) is not limited by the provisions of AS 38.05.134(3) or (f) of this
20 section in the commissioner's determination under this subsection.

21 * Sec. 2. AS 38.05.180(p) is amended to read:

22 (p) To conserve the natural resources of all or a part of an oil or gas pool,
23 field, or like area, the lessees and their representatives may unite with each other, or
24 jointly or separately with others, in collectively adopting or operating under a
25 cooperative or a unit plan of development or operation of the pool, field, or like area,
26 or a part of it, when determined and certified by the commissioner to be necessary or
27 advisable in the public interest. The commissioner may, with the consent of the
28 holders of leases involved, establish, change, or revoke drilling, producing, and royalty
29 requirements of the leases and adopt regulations with reference to the leases, with like
30 consent on the part of the lessees, in connection with the institution and operation of
31 a cooperative or unit plan as the commissioner determines necessary or proper to

1 secure the proper protection of the public interest. The commissioner may not
2 reduce royalty on leases in connection with a cooperative or unit plan except as
3 provided in (j) of this section. The commissioner may require oil and gas leases
4 issued under this section to contain a provision requiring the lessee to operate under
5 a reasonable cooperative or unit plan, and may prescribe a plan under which the lessee
6 must operate. The plan must adequately protect all parties in interest, including the
7 state.

8 * Sec. 3. This Act takes effect immediately under AS 01.10.070(c).

9-GH0039F ✓

Chenoweth

3/21/95

CS FOR HOUSE BILL NO. 207(O&G)

IN THE LEGISLATURE OF THE STATE OF ALASKA

NINETEENTH LEGISLATURE - FIRST SESSION

BY THE HOUSE SPECIAL COMMITTEE ON OIL AND GAS

Offered:

Referred:

Sponsor(s): HOUSE RULES COMMITTEE BY REQUEST OF THE GOVERNOR

A BILL

FOR AN ACT ENTITLED

1 "An Act relating to adjustments to royalty reserved to the state to encourage
2 otherwise uneconomic production of oil and gas; and providing for an effective
3 date."

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

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

6 (j) The [TO PROLONG THE ECONOMIC LIFE OF AN OIL AND GAS
7 FIELD OR TO REESTABLISH COMMERCIAL PRODUCTION OF SHUT-IN OIL
8 OR GAS THAT WOULD NOT OTHERWISE BE ECONOMICALLY FEASIBLE,
9 THE] commissioner

10 (1) may [SHALL ADOPT REGULATIONS TO] allow reduction of
11 royalty on individual leases or leases unitized as described in (p) of this section

12 (A) to allow for production from an oil or gas field, pool, or
13 portion of a field or pool if

14 (i) the oil or gas field, pool, or portion of the field or

pool has been sufficiently delineated to the satisfaction of the commissioner;

(ii) the field, pool, or portion of the field or pool has not previously produced oil or gas; and

(iii) production from the field, pool, or portion of the field or pool would not otherwise be economically feasible;

(B) to prolong the economic life of an oil or gas field, pool, or portion of a field or pool, as per barrel or barrel equivalent costs increase in the later stages of production decline; or

(C) to reestablish commercial production of shut-in oil or gas that would not otherwise be economically feasible;

(2) [THE COMMISSIONER] may not grant a reduction of royalty unless the lessee or lessees requesting the reduction make [MAKES] a clear and convincing showing that a reduction of royalty meets the requirements of this subsection and is in the best interests of the state;

(3) shall, if the royalty reduction agreement is approved, in the royalty reduction agreement, [THE REVENUE FROM THE LESSEE'S SHARE OF ALL HYDROCARBONS PRODUCED FROM THE FIELD IS AND IS LIKELY TO CONTINUE TO BE INSUFFICIENT TO PRODUCE A REASONABLE RATE OF RETURN WITH RESPECT TO THE LESSEE'S TOTAL INVESTMENT IN THE FIELD. THE COMMISSIONER MAY] condition a royalty reduction granted under this subsection in any way necessary to protect the state's best interests; under this subsection, the commissioner shall include provisions to increase or otherwise modify the state's royalty share by a sliding scale royalty or other mechanism upon the occurrence of a change [INTEREST, INCLUDING RESTORATION OF THE STATE'S ROYALTY SHARE IN THE EVENT OF AN INCREASE] in the price of oil or gas, and may consider other relevant factors, such as proved reserves, well productivity, or capital investment in the oil or gas field, pool, or portion of the field or pool;

(4) may not grant a royalty reduction for a field, pool, or portion of a field or pool under (1)(A) of this subsection that exceeds 75 percent of the

1 royalty originally specified in a lease entered into under the provisions of (f) of
2 this section or AS 38.05.134;

3 (5) shall, as part of the royalty reduction application process,
4 require the lessee or lessees to submit, with the application for the royalty
5 reduction, financial and technical data that demonstrates that the requirements
6 of this subsection are met; the financial and technical data required by the
7 commissioner

8 (A) may not require disclosure of data relating to
9 production before the lessee or lessees obtained ownership of the lease if
10 the reduction application involves a lease described in (1)(B) or (C) of this
11 subsection; and

12 (B) shall be kept confidential under AS 38.05.035(a)(9) upon
13 the lessee's request;

14 (6) shall give notice of the written findings and determination to the
15 lessee and to any other person who has filed a written request for it; subject to
16 (8) of this subsection, the commissioner's determination is final and not appealable
17 to the court;

18 (7) may require the lessee or lessees making application for the
19 royalty reduction to retain and pay for the services of a contractor, selected from
20 a list provided by the commissioner, to assist the commissioner in evaluating the
21 application and financial and technical data; when the commissioner requires the
22 lessee or lessees to retain the services of a contractor under this paragraph, the
23 commissioner shall determine the relevant scope of the work to be performed by
24 the contractor;

25 (8) may not make a determination that gives final approval to an
26 application for a royalty reduction under this subsection unless the commissioner
27 first

28 (A) obtains the concurrence of the attorney general;

29 (B) submits the proposed royalty reduction decision to and
30 obtains the approval of at least three of the five members of the Alaska
31 Royalty Oil and Gas Development Advisory Board other than the

1 commissioner of natural resources; for purposes of this subparagraph,
2 after submission of the proposed royalty reduction under this
3 subparagraph, the Alaska Royalty Oil and Gas Development Advisory
4 Board has 30 days in which to evaluate the commissioner's submission and
5 to determine that the proposed royalty reduction meets the requirements
6 of this subsection and is in the best interests of the state;

7 (C) transmits copies of the determination made by the
8 Alaska Royalty Oil and Gas Development Advisory Board to

9 (i) the presiding officer of each house [. BEFORE
10 APPROVING A ROYALTY REDUCTION, THE COMMISSIONER
11 SHALL MAKE A WRITTEN FINDING THAT THE STATE HAS
12 OBTAINED THE MAXIMUM POSSIBLE ECONOMIC RETURN
13 THAT IS COMPATIBLE WITH ALLOWING A REASONABLE
14 RATE OF ECONOMIC RETURN FOR THE LESSEE, AND SEND
15 COPIES OF THE FINDING TO ALL MEMBERS] of the legislature;

16 (ii) the chairs of the legislature's standing committees
17 on resources; and

18 (iii) the chairs of the legislature's special committees
19 on oil and gas, if any;

20 (9) is not limited by the provisions of AS 38.05.134(3) or (f) of this
21 section in the commissioner's determination under this subsection.

22 * Sec. 2. AS 38.05.180(p) is amended to read:

23 (p) To conserve the natural resources of all or a part of an oil or gas pool,
24 field, or like area, the lessees and their representatives may unite with each other, or
25 jointly or separately with others, in collectively adopting or operating under a
26 cooperative or a unit plan of development or operation of the pool, field, or like area,
27 or a part of it, when determined and certified by the commissioner to be necessary or
28 advisable in the public interest. The commissioner may, with the consent of the
29 holders of leases involved, establish, change, or revoke drilling, producing, and royalty
30 requirements of the leases and adopt regulations with reference to the leases, with like
31 consent on the part of the lessees, in connection with the institution and operation of

1 a cooperative or unit plan as the commissioner determines necessary or proper to
2 secure the proper protection of the public interest. The commissioner may not
3 reduce royalty on leases in connection with a cooperative or unit plan except as
4 provided in (j) of this section. The commissioner may require oil and gas leases
5 issued under this section to contain a provision requiring the lessee to operate under
6 a reasonable cooperative or unit plan, and may prescribe a plan under which the lessee
7 must operate. The plan must adequately protect all parties in interest, including the
8 state.

9 * Sec. 3. This Act takes effect immediately under AS 01.10.070(c).

9-GH0039\C✓
Chenoweth
3/20/95

CS FOR HOUSE BILL NO. 207(O&G)
IN THE LEGISLATURE OF THE STATE OF ALASKA
NINETEENTH LEGISLATURE - FIRST SESSION

BY THE HOUSE SPECIAL COMMITTEE ON OIL AND GAS

Offered:
Referred:

Sponsor(s): HOUSE RULES COMMITTEE BY REQUEST OF THE GOVERNOR

A BILL

FOR AN ACT ENTITLED

1 "An Act relating to adjustments to royalty reserved to the state to encourage
2 otherwise uneconomic production of oil and gas and relating to the treatment of
3 net profit shares of oil and gas leases as it relates to certain oil and gas lease
4 royalty; and providing for an effective date."

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

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

7 (g) The share of the net profit derived from a lease reserved to the state under
8 (f) of this section is royalty [SALE PROCEEDS] for purposes of (f), (j), and (p) of
9 this section, and for the purposes of the Alaska permanent fund under AS 37.13.010.

10 * Sec. 2. AS 38.05.180(j) is amended to read:

11 (j) The [TO PROLONG THE ECONOMIC LIFE OF AN OIL AND GAS
12 FIELD OR TO REESTABLISH COMMERCIAL PRODUCTION OF SHUT-IN OIL
13 OR GAS THAT WOULD NOT OTHERWISE BE ECONOMICALLY FEASIBLE,
14 THE] commissioner

1 (1) may [SHALL ADOPT REGULATIONS TO] allow reduction of
2 royalty on individual leases, leases in a participating area formed under a unit
3 agreement for a single area of oil or gas productivity, or leases unitized as
4 described in (p) of this section

5 (A) to allow for production from an oil or gas field, pool, or
6 portion of a field or pool if

7 (i) the oil or gas field, pool, or portion of the field or
8 pool has been sufficiently delineated to the satisfaction of the
9 commissioner;

10 (ii) the field, pool, or portion of the field or pool has
11 not previously produced oil or gas; and

12 (iii) production from the field, pool, or portion of the
13 field or pool would not otherwise be economically feasible;

14 (B) to prolong the economic life of an oil or gas field, pool,
15 or portion of a field or pool, as per barrel or barrel equivalent costs
16 increase in the later stages of production decline; or

17 (C) to reestablish commercial production of shut-in oil or
18 gas that would not otherwise be economically feasible;

19 (2) [. THE COMMISSIONER] may not grant a reduction of royalty
20 unless the lessee or lessees requesting the reduction make [MAKES] a clear and
21 convincing showing that a reduction of royalty meets the requirements of this
22 subsection and is in the best interests of the state;

23 (3) shall, if the royalty reduction agreement is approved, in the
24 royalty reduction agreement, [THE REVENUE FROM THE LESSEE'S SHARE OF
25 ALL HYDROCARBONS PRODUCED FROM THE FIELD IS AND IS LIKELY TO
26 CONTINUE TO BE INSUFFICIENT TO PRODUCE A REASONABLE RATE OF
27 RETURN WITH RESPECT TO THE LESSEE'S TOTAL INVESTMENT IN THE
28 FIELD. THE COMMISSIONER MAY] condition a royalty reduction granted under
29 this subsection in any way necessary to protect the state's best interests; under this
30 subsection, the commissioner shall include provisions to increase or otherwise
31 modify the state's royalty share by a sliding scale royalty or other mechanism

1 upon the occurrence of a change [INTEREST, INCLUDING RESTORATION OF
2 THE STATE'S ROYALTY SHARE IN THE EVENT OF AN INCREASE] in the price
3 of oil or gas, proved reserves, well productivity, or capital investment in the oil or
4 gas field, pool, or portion of the field or pool;

5 (4) may not grant a royalty reduction for a field, pool, or portion
6 of a field or pool under (1)(A) of this subsection that exceeds 75 percent of the
7 royalty originally specified in a lease entered into under the provisions of (f) of
8 this section or AS 38.05.134;

9 (5) shall, as part of the royalty reduction application process,
10 require the lessee or lessees

11 (A) to apply for the reduction; an application for a royalty
12 reduction must

13 (i) state all the facts entitling the applicant to a
14 royalty reduction;

15 (ii) state the location and status of all past and
16 present activities on the lease;

17 (iii) include a detailed report of all production during
18 the six months preceding the filing of the royalty reduction
19 application; and

20 (iv) include an agreement by the applicant to defray
21 the cost of publishing the notice as provided by (6) of this
22 subsection;

23 (B) to submit, with the application for the royalty reduction,
24 financial and technical data that demonstrates that the requirements of
25 this subsection are met; the financial and technical data required by the
26 commissioner

27 (i) may not require disclosure of data relating to
28 production before the lessee or lessees obtained ownership of the
29 lease;

30 (ii) must, if the reduction application involves a lease
31 described in (1)(B) or (C) of this subsection, include at least five

1 years of the lease's production history; and

2 (iii) shall be kept confidential under

3 AS 38.05.035(a)(9) upon the lessee's request;

4 (6) shall, upon receipt of an application complying with (5) of this
5 subsection, publish a notice of public hearing on the application; the notice must

6 (A) state the time and place of hearing;

7 (B) describe the land involved;

8 (C) state the name of the royalty reduction applicant and
9 the nature of the reduction applied for; and

10 (D) be published at least once a week for at least two
11 consecutive weeks in advance of the hearing date, which must be at least
12 15 days after the last date of publication, in at least one newspaper of
13 general circulation in the vicinity of the principal office of the department,
14 and must be posted at the principal office for the same period;

15 (7) shall,

16 (A) at the time and place specified in the notice published
17 under (6) of this subsection, hear evidence offered by the applicant and
18 any other interested person;

19 (B) within a reasonable time following the hearing or any
20 continuation of it, make written findings together with the commissioner's
21 determination as to the reduction that should be granted;

22 (C) give notice of the findings and determination to the
23 lessee and to any other person who has filed a written request for it;
24 subject to (9) of this subsection, the commissioner's determination is final
25 and not appealable by the royalty reduction applicant to the court;

26 (8) may require the lessee or lessees making application for the
27 royalty reduction to retain the services of a contractor, selected from a list
28 provided by the commissioner, to assist the commissioner in evaluating the
29 application and financial and technical data; when the commissioner requires the
30 lessee or lessees to retain the services of a contractor under this paragraph, the
31 commissioner shall determine the relevant scope of the work to be performed by

1 the contractor;

2 (9) may not make a determination that gives final approval to an
3 application for a royalty reduction under this subsection unless the commissioner
4 first

5 (A) obtains the concurrence of the attorney general;

6 (B) submits the proposed royalty reduction decision to and
7 obtains the approval of at least three of the five members of the Alaska
8 Royalty Oil and Gas Development Advisory Board other than the
9 commissioner of natural resources; for purposes of this subparagraph,
10 after submission of the proposed royalty reduction under this
11 subparagraph, the Alaska Royalty Oil and Gas Development Advisory
12 Board has 30 days in which to evaluate the commissioner's submission and
13 to determine that the proposed royalty reduction meets the requirements
14 of this subsection and is in the best interests of the date;

15 (C) transmits copies of the determination made by the
16 Alaska Royalty Oil and Gas Development Advisory Board to

17 (i) the presiding officer of each house [BEFORE
18 APPROVING A ROYALTY REDUCTION, THE COMMISSIONER
19 SHALL MAKE A WRITTEN FINDING THAT THE STATE HAS
20 OBTAINED THE MAXIMUM POSSIBLE ECONOMIC RETURN
21 THAT IS COMPATIBLE WITH ALLOWING A REASONABLE
22 RATE OF ECONOMIC RETURN FOR THE LESSEE, AND SEND
23 COPIES OF THE FINDING TO ALL MEMBERS] of the legislature;

24 (ii) the chairs of the legislature's standing committees
25 on resources; and

26 (iii) the chairs of the legislature's special committees
27 on oil and gas, if any;

28 (10) may not adopt regulations to implement this subsection;

29 (11) is not limited by the provisions of AS 38.05.134(3) or (f) of this
30 section in the commissioner's determination under this subsection.

31 * Sec. 3. AS 38.05.180(p) is amended to read:

1 (p) To conserve the natural resources of all or a part of an oil or gas pool,
2 field, or like area, the lessees and their representatives may unite with each other, or
3 jointly or separately with others, in collectively adopting or operating under a
4 cooperative or a unit plan of development or operation of the pool, field, or like area,
5 or a part of it, when determined and certified by the commissioner to be necessary or
6 advisable in the public interest. The commissioner may, with the consent of the
7 holders of leases involved, establish, change, or revoke drilling, producing, and royalty
8 requirements of the leases and adopt regulations with reference to the leases, with like
9 consent on the part of the lessees, in connection with the institution and operation of
10 a cooperative or unit plan as the commissioner determines necessary or proper to
11 secure the proper protection of the public interest. The commissioner may not
12 reduce royalty on leases in connection with a cooperative or unit plan except as
13 provided in (j) of this section. The commissioner may require oil and gas leases
14 issued under this section to contain a provision requiring the lessee to operate under
15 a reasonable cooperative or unit plan, and may prescribe a plan under which the lessee
16 must operate. The plan must adequately protect all parties in interest, including the
17 state.

18 * Sec. 4. 11 AAC 83.185 is annulled.

19 * Sec. 5. This Act takes effect immediately under AS 01.10.070(c).

HOUSE BILL NO. 207

IN THE LEGISLATURE OF THE STATE OF ALASKA

NINETEENTH LEGISLATURE - FIRST SESSION

BY THE HOUSE RULES COMMITTEE BY REQUEST OF THE GOVERNOR

Introduced: 2/27/95

Referred: House Special Committee on Oil and Gas, Resources, Finance

A BILL

FOR AN ACT ENTITLED

1 "An Act relating to adjustments to royalty reserved to the state to encourage
2 otherwise uneconomic production of oil and gas; relating to the depositing of
3 royalties and royalty sale proceeds in the Alaska permanent fund; and providing
4 for an effective date."

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

6 * Section 1. AS 37.13.010(a) is amended to read:

7 (a) Under art. IX, sec. 15 of the state constitution, there is established as a
8 separate fund the Alaska permanent fund. The Alaska permanent fund consists of

9 (1) 25 percent of

10 (A) all mineral lease rentals, royalties, royalty sale proceeds, net
11 profit shares under AS 38.05.180(f) and (g), and federal mineral revenue
12 sharing payments received by the state from mineral leases issued on or before
13 December 1, 1979, except that, regarding royalties and royalty sale
14 proceeds, for leases for which the royalty is reduced or modified under

1 AS 38.05.180(j), the permanent fund shall receive the greater of

2 (i) the royalties and royalty sale proceeds that the
3 fund would have received if a reduction under AS 38.05.180(j) had
4 not been granted; or

5 (ii) 25 percent of the royalties and royalty sale
6 proceeds received by the state under a modified royalty under
7 AS 38.05.180(j); and [25 PERCENT OF]

8 (B) all bonuses received by the state from mineral leases issued
9 on or before February 15, 1980;

10 (2) 50 percent of

11 (A) all mineral lease rentals, royalties, royalty sale proceeds, net
12 profit shares under AS 38.05.180(f) and (g), and federal mineral revenue
13 sharing payments received by the state from mineral leases issued after
14 December 1, 1979, except that, regarding royalties and royalty sale
15 proceeds, for leases for which the royalty is reduced or modified under
16 AS 38.05.180(j), the permanent fund shall receive the greater of

17 (i) the royalties and royalty sale proceeds that the
18 fund would have received if a reduction under AS 38.05.180(j) had
19 not been granted; or

20 (ii) 50 percent of the royalties and royalty sale
21 proceeds received by the state under a modified royalty under
22 AS 38.05.180(j); and [50 PERCENT OF]

23 (B) all bonuses received by the state from mineral leases issued
24 after February 15, 1980;

25 (3) any other money appropriated to or otherwise allocated by law
26 to the Alaska permanent fund.

27 * Sec. 2. AS 38.05.180(j) is amended to read:

28 (j) To allow for production from a delineated but not previously produced
29 field that would not otherwise be economically feasible, to [TO] prolong the
30 economic life of an oil and gas field as per barrel or barrel equivalent costs
31 increase in the later stages of production decline, or to reestablish commercial

production of shut-in oil or gas that would not otherwise be economically feasible, the commissioner ~~may~~ ^{SHALL} ADOPT REGULATIONS TO allow reduction of royalty on individual leases or leases unitized as described in (p) of this section. As part of an application for a reduction under this subsection, the commissioner shall require the lessee ^{or lessees} requesting the reduction of royalty to disclose financial and technical data that demonstrate that the requirements of this subsection for a reduction are met. Such data shall be kept confidential upon the lessee's request. As a condition of evaluating an application and data, the commissioner may require the lessee to pay the costs of ^{a mutually agree} contractors selected by the commissioner to assist in the evaluation. The commissioner may not grant a reduction of royalty unless the lessee requesting the reduction makes a clear and convincing showing that a reduction meets the requirements of this subsection and is in the best interests of the state ^{because} [THE REVENUE FROM THE LESSEE'S SHARE OF ALL HYDROCARBONS PRODUCED FROM THE FIELD IS ~~AND IS~~ ^{is an} ~~LIKELY TO CONTINUE~~ TO BE INSUFFICIENT TO PRODUCE A REASONABLE RATE OF RETURN WITH RESPECT TO THE LESSEE'S TOTAL INVESTMENT IN THE FIELD]. The commissioner may not grant a reduction that exceeds 75 percent of the royalty originally specified in a lease issued on or before December 1, 1979 under the provisions of (f) of this section, or 50 percent of the royalty originally specified in a lease issued after December 1, 1979 under the provisions of (f) of this section or AS 38.05.134. The commissioner ^{she} may condition a royalty reduction granted under this subsection in any way necessary to protect the state's best interests [INTEREST], including increasing or otherwise modifying [RESTORATION OF] the state's royalty share ^{in the new royalty} if any relevant factor, such as [IN THE EVENT OF AN INCREASE IN] the price of oil or gas, changes. Before approving a royalty reduction, the commissioner shall make public a written finding that the reduction meets the requirements of this subsection and is in the best interests of the state [THE STATE HAS OBTAINED THE MAXIMUM POSSIBLE ECONOMIC RETURN THAT IS COMPATIBLE WITH ALLOWING A REASONABLE RATE OF ECONOMIC RETURN FOR THE LESSEE], and send copies of the finding to all members of the legislature. The commissioner's decision

will provide
1 regarding a request for reduction under this subsection is final and not appealable
2 *by the applicant.* ~~to the court.~~ The provisions of this subsection are not limited by the provisions
3 of (f) of this section or AS 38.05.134(3).

4 * Sec. 3. AS 38.05.180(p) is amended to read:

5 (p) To conserve the natural resources of all or a part of an oil or gas pool,
6 field, or like area, the lessees and their representatives may unite with each other, or
7 jointly or separately with others, in collectively adopting or operating under a
8 cooperative or a unit plan of development or operation of the pool, field, or like area,
9 or a part of it, when determined and certified by the commissioner to be necessary or
10 advisable in the public interest. The commissioner may, with the consent of the
11 holders of leases involved, establish, change, or revoke drilling, producing, and royalty
12 requirements of the leases and adopt regulations with reference to the leases, with like
13 consent on the part of the lessees, in connection with the institution and operation of
14 a cooperative or unit plan as the commissioner determines necessary or proper to
15 secure the proper protection of the public interest. The commissioner may not
16 reduce royalty on leases in connection with a cooperative or unit plan except as
17 provided in (j) of this section. The commissioner may require oil and gas leases
18 issued under this section to contain a provision requiring the lessee to operate under
19 a reasonable cooperative or unit plan, and may prescribe a plan under which the lessee
20 must operate. The plan must adequately protect all parties in interest, including the
21 state.

22 * Sec. 4. This Act takes effect immediately under AS 01.10.070(c).