ALASKA LEGISLATURE COMMITTEE FILES 1995-1996 8672
9009 SENATE RESOURCES

CS FOR HOUSE BILL NO. 207(FIN) am

IN THE LEGISLATURE OF THE STATE OF ALASKA

NINETEENTH LEGISLATURE - FIRST SESSION

BY THE HOUSE FINANCE COMMITTEE

Amended: 4/19/95
Offered: 4/18/95

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

A BILL

FOR AN ACT ENTITLED

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

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

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

(j) The [TO 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, THE] commissioner

(1) may [SHALL ADOPT REGULATIONS TO ALLOW REDUCTION] provide for modification of royalty on individual leases, leases unitized as described in (p) of this section, leases subject to an agreement described in (s) or (t) of this section, or interests unitized under AS 31.05

(A) to allow for production from an oil or gas field, pool, or

New Text Underlined [DELETED TEXT BRACKETED]

portion of a field or pool if

(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 for sale; and

(iii) oil or gas 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 or as the price of oil or gas decreases, and the increase or decrease is sufficient to make future production no longer economically feasible; or

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

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

(3) shall [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 any [A] royalty modification [REDUCTION] granted under this subsection in any way necessary to protect the state's best interests; the commissioner shall provide for an increase or decrease or other modification of the state's royalty share by a sliding scale royalty or other mechanism that shall be based on 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 also be based on other relevant factors such as a change in production rate, projected ultimate recovery, development costs, and operating costs;

New Text Underlined [DELETED TEXT BRACKETED]

(4) may not grant a royalty reduction for a field, pool, or portion of a field or pool

(A) under (1)(A) of this subsection that exceeds 75 percent of the royalty originally specified in a lease entered into under the provisions of (f) of this section or AS 38.05.134;

(B) under (1)(B) or (1)(C) of this subsection that exceeds 90 percent of the royalty originally specified in a lease entered into under the provisions of (f) of this section or AS 38.05.134;

(5) shall require the lessee or lessees to submit, with the application for the royalty reduction, financial and technical data that demonstrates that the requirements of this subsection are met; the commissioner

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

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

(6) may require the lessee or lessees making application for the royalty reduction to retain and pay for the services of a contractor, selected by the lessee or lessees from a list of qualified consultants in hydrocarbon production and economics provided by the commissioner, to assist the commissioner in evaluating the application and financial and technical data; when the commissioner requires the lessee or lessees to retain the services of a contractor, the commissioner shall determine the relevant scope of the work to be performed by the contractor;

(7) shall make and publish a preliminary findings and determination on the royalty reduction application, give reasonable public notice of the preliminary findings and determination, and invite public comment on the preliminary findings and determination during a 30-day period for receipt of public comment;

(8) shall offer to appear before the Legislative Budget and Audit Committee on a day that is not earlier than 10 days and not later than 20 days after giving public notice under (7) of this subsection, to provide the committee a review of the commissioner's preliminary findings and determination on the royalty reduction application and administrative process; if the Legislative Budget and

Audit Committee accepts the commissioner's offer, the committee shall give notice to all members of the legislature of the committee's meeting;

(9) shall make copies of the preliminary findings and determination available to

(A) the presiding officer of each house [. BEFORE APPROVING A ROYALTY REDUCTION, THE COMMISSIONER SHALL MAKE A WRITTEN FINDING THAT 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;

(B) the chairs of the legislature's standing committees on resources; and

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

(10) shall, within 30 days after the close of the public comment period under (7) of this subsection,

(A) prepare a summary of the public response to the commissioner's preliminary findings and determination;

(B) make a final findings and determination; the commissioner's final findings and determination prepared under this subparagraph regarding royalty reduction is final and not appealable to the court;

(C) transmit a copy of the final findings and determination to the lessee;

(D) with the applicant's consent, amend the applicant's lease or unitization agreement consistent with the commissioner's final decision and;

(E) make copies of the final findings and determination available to a person who submitted comment under (7) of this subsection and who has filed a request for the copies;

(11) is not limited by the provisions of AS 38.05.134(3) or (5) of this

section in the commissioner's determination under this subsection.

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

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

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

(s) When separate tracts cannot be individually developed and operated in conformity with an established well-spacing or development program, a lease, or a portion of a lease, may be pooled with other land, whether or not owned by the state, under a communitization or drilling agreement providing for an apportionment of production or royalties among the separate tracts of land comprising the drilling or spacing unit when determined by the commissioner to be in the public interest. Operations or production under the agreement are considered as operations or production as to each lease committed to the agreement. **The commissioner may not reduce royalty on leases in connection with a communitization or drilling agreement except as provided in (j) of this section.**

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

(t) The commissioner may prescribe conditions and approve, on conditions, drilling, or development contracts made by one or more lessees of oil or gas leases, with one or more persons, when, in the discretion of the commissioner, the conservation of natural resources or the public convenience or necessity requires it or the interests of the state are best served. All leases operated under approved drilling or development contracts and interests under them, are excepted in determining holding or control under AS 38.05.140. **The commissioner may not reduce royalty on a lease or leases that are subject to a drilling or development contract except as provided in (t) of this section.**

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

HB

207

(File 2)

CITY OF KENAI

" Oil Capital of Alaska "

210 FIDALGO AVE., SUITE 200 KENAI, ALASKA 99611-7794
TELEPHONE 907-283-7535
FAX 907-283-3014

May 4, 1995

Senator Loren Leman
State of Alaska
Capitol Building, Room 113
Juneau, AK 99801-1182

RE: *MODIFICATION OF OIL AND GAS ROYALTY RATES*
HOUSE BILL 207

At their regular meeting of May 3, 1995, the Kenai City Council discussed the above-referenced bill and its merits. The Council feels strongly that this bill will give the Commissioner of Natural Resources greater authority to modify oil and gas royalty rates to help open up marginal oil fields to development.

HB 207, as passed by the House of Representatives by a significant margin, provides the flexibility in setting royalty terms for marginal fields. This flexibility will encourage the State and the industry to work together to change the economic equation for marginal fields, bring on new fields, extend the life of existing fields and build a stronger economic base for the future.

The Kenai City Council fully supports HB 207 (as passed by the House) as it is a tool which the State can use to enhance competitiveness of projects in the world market, attracting investments necessary to develop its oil and gas potential. Alaska will benefit from new jobs, long-term revenues and increased economic activity associated with the development of new fields.

This bill, as passed by the House of Representatives, should not be significantly amended or substituted as suggested by the Senate Resources Committee and needs to be passed this year.

CITY OF KENAI

John J. Williams
Mayor

JJW/clf

KENAI PENINSULA BOROUGH
144 N. BINKLEY • SOLDOTNA, ALASKA 99669
PHONE (907) 262-4441

DON GILMAN
MAYOR

Ltr prepared (updated)

May 3, 1995

The Honorable Loren Leman
Senate Resources Chair
State of Alaska Senate
Capital Building
Juneau, AK 99801-1182

Dear Senator Leman:

The Kenai Peninsula Borough Assembly supports the concept of oil and gas royalty adjustments as embodied in HB 207.

It is our understanding the bill would give the Commissioner of Natural Resources greater authority to modify oil and gas royalty rates to help open up marginal oil fields to development. Further, that it would provide the necessary flexibility in setting the royalty terms for marginal field and encourage the state and industry to work together to change the economic equation for the marginal fields.

The Kenai Peninsula Borough depends in large part on the economic viability of the oil industry and to that extent we would strongly encourage the development of a long-term stable financial plan which would include the royalty oil issue.

Sincerely,

Andrew P. Scalzi /kf

Andrew P. Scalzi, President
Kenai Peninsula Borough Assembly

cc: Senate Resources Committee: Senators Pearce, Frank, Halford, Taylor, Lincoln, Hoffman
Senators Torgerson and Salo

FORUM / LETTERS

Debate for royalty relief centers on empty rhetoric

By RICHARD A. FINEBERG

ESTER — Lost in the wrangling over the current state budget is this important fact about the state's spring revenue forecast: Between the current year and 2010, the state now estimates the North Slope will produce 740 million barrels of oil more than it forecasted six months ago.

This 10 percent increase in future production equates to one added year of oil pumped at the peak TAPS throughput of 2 million barrels per day. This forecast increase was accomplished without the aid of the royalty relief measure the governor and a few oil companies are pushing.

This added production is the latest in a trend that has been operating steadily for a decade. Look back to the state's spring 1985 forecast. Then, oil prices were in the high $20s and the state's forecasters thought North Slope production would fall below 1 million barrels per day in 1994. Although oil prices soon plummeted and stayed relatively low, the North Slope in 1994 was in fact producing 1.6 million barrels per day and the forecasters said we wouldn't drop below 1 million until 2003. Six months later, that landmark has moved back to 2006.

If increased production (i.e., slowed production decline) is an established fact, why all the hurry to enact new royalty relief?

The answer is simple: If the state wants to make it easier to give away your money and mine, what corporate official would turn it down?

The debate over whether the public should forego its ownership share of oil production on behalf of private developers is characterized by a curious absence of facts. When the oil industry fought the closing of a tax loophole known as the ELF (economic limit factor) in 1989, Juneau was flooded with detailed and sometimes conflicting spreadsheets as legislators struggled to apprehend the significance of the proposal to end the tax break for large fields.

That year, the industry's arguments collapsed late in the session when a tough-minded Senate Finance Committee called for an explanation of the conflicting numbers. The industry was revealed to be stretching the truth beyond the limits of recognition; the legislature voted to close the loophole. Despite dire predictions in 1989 that future production would suffer if the bill passed, subsequent forecasts and production records consistently have reflected increases in total North Slope production.

This time, the industry is not putting any numbers on the board for review. Instead, the debate in Juneau is couched entirely in rhetoric. And that rhetoric is empty, as the recent forecast indicates.

Even more surprising is the administration's willingness to destroy current procedures that require the industry to make its case for royalty relief public. Some observers of oil and gas policy contend that the public always loses when the industry is allowed to make and keep its arguments behind closed doors. That's precisely what the administration's proposals would do.

Opponents of the current proposal do not say that royalty relief will never be necessary. Rather, they argue that before the stewards of the public's resource give up a portion of our ownership share of production, the industry should be required to make a substantive showing that should be reviewed carefully, and insofar as possible, in the open.

The clear trend established by the state's forecasts demonstrates that world supply and demand and technological improvements successfully are stoking the North Slope's fires without new procedures that would jettison the existing, carefully crafted and effective public safeguards. Since 1985, the state's forecasted and actual production from the North Slope for the 1986-2010 period has increased more than 6.2 billion barrels. This increase equates to the annual addition of one year more of production at current levels than forecasted each preceding year.

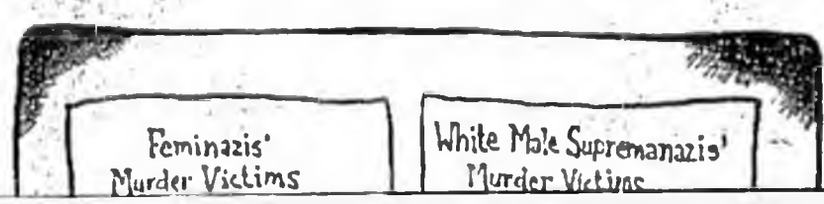
If this issue must be argued with oversimplified generalities, the following maxims must be kept in mind:

1. Those who don't learn from history are doomed to repeat it.
2. Money talks.

Richard A. Fineberg has looked at North Slope economic and environmental issues as a reporter, public official and consultant for nearly 20 years. He lives in Ester.

Let's make our roads safe

If ever there has been an incident-driven example in the argument in favor of capital punishment, the story about the eight-time drunken driver April 15 warrants an award in public awareness education.



crime. I think I have an old solution. I suggest stocks in combination with a park bench. History tells us insects were annoying but taunting crowds were devastating. So few would come forward to give the prisoner some stale bread or a

HB27

Official Business

COMMITTEE:
SENATE RESOURCES

DATE: 5/1/95

Subject of meeting:
HB 207 Adjustments to Oil and Gas Royalties

SIGN-IN

PLEASE PRINT!

NAME	ADDRESS (MAILING) & (ZIP)	PHONE	REPRESENTING	DO YOU WANT TO TESTIFY?
✓ MICHAEL O'CONNOR	7141 MONTAGNE ANCH AK	561-3200 337-6536	ARCO OILFIELD SER. CO	YES
✓ KEITH BURKE	4220 B St. Suite 200 Anch. AK	563-2226	The Alliance	YES
✓ JOE B. MATHIS	1001 E. BENSON ANCH 99508	265-4147 345-5764	NANA Develop. CORP	Yes
CARL MARRS	2525 'C' ST Suite 500 ANC 99509	3445079 2748678	CIRI	YES
General Manager Oilfield Operations				

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To Senator Torgerson | From [illegible]

Co./Dept. ADL | Co. Senate Natural Resources

Phone # | Phone # 465-4967

Fax # 258-7197 | Fax #

JNU INFO ☎4652884 05/02/95 10:36 001

ARCO Alaska, Inc.
Testimony for Senate Resources
05/01/95
RE: HB207

Mr. Chairman, for the record, my name is George Findling. I am the Manager of Government Relations for ARCO Alaska, Inc. I am here to testify in support of HB - 207, Version J, which passed the House, and in opposition to the working draft Version B, dated 4/29/95.

The overarching issue here is Alaska's response to the world wide competition for oil investment. Alaska's leaders have told us that it is in the State's best interest to compete successfully for more capital. We have been very busy responding to requests from the State on ways to do this. We see a simple, three step strategy.

The first step is to quickly signal to investors that the State has the desire and the ability to change. If passed, this is what Version J would do. The second step is to harvest the major opportunities to increase industry investment. This should be an early outcome of the Oil and Gas policy council. The third step is to implement a long term process that would give the State the flexibility to have a competitive position, even if world-wide competition or market conditions change rapidly.

Alaska is facing 1990's competition using statutes drafted in the 1970's. Back then, little competition for investment existed, since oil was perceived to be running out and prices were expected to always go up. But now, competition for investment is worldwide and fierce and the indicators show that Alaska is losing. Alaska production is down, and many major oil companies have withdrawn from the state.

When we saw Version S on Friday we felt very disappointed, because it meant that important state leaders appear to be questioning whether even the most modest first step should be taken to increase Alaska's competitiveness. Although a slight improvement, Version B would still water down the effectiveness of the bill. It introduces new concepts that have received little public discussion. In fact, we find this version to be less helpful than current law and can not support its passage.

Let me mention a few examples of the shortfalls of this working draft by comparing it to what Alaska's competitors are doing. Internationally, greater descretion is being given to oil ministers to make arrangements that will attract investment. In the working draft, the focus on legislative approval would work in the opposite direction. Even more confusing, is the criteria for legislative oversight. By definition royalty adjustments can only be given if the new field would not otherwise be produced: in other words, it seems that there could never be a royalty reduction, if the base case is zero royalty dollars.

Internationally, greater certainty is being given that investors can count on getting the benefits enumerated in the law. Under the working draft, the added procedures and limitations would be so bureautic and onerous that it is unlikely that anyone would apply under these conditions. Finally, oil provinces are making agreements that share risk but give reasonable certainty. They establish prospectively, a method that retains a higher share when economic conditions are good and a reduced share when they are not. The wording on page 3, which apparently gives the Commissioner the ability to reopen this agreement is a fatal flaw.

We support the House Version J, not because it's a "giveaway" to the industry, but because it withstands comparisons to other oil provinces. ARCO has no specific projects to propose today which will use HB-207 provisions. Yet with Version J's passage we would answer our Corporate decision makers, that Alaska has turned the corner and is truly vying in the international arena for capital. Each of us at ARCO wants the tools to get a larger share of capital for Alaska investments.

Version J enjoys many strengths. It is a modest, but real first step. It sets the stage for Alaska both to really begin a return to international competitiveness and to partner with its most important natural resource industry. It also has broad consensus because the bill merits that support.

Therefore, Mr. Chairman, we respectfully register, for the record, our opposition to working draft version B and our support of the House Passed Version J originally referred to your committee.

Anchorage,
Alaska

George R. Findling
Phone 263-4174

5/1/95

Senator Loren Leman

Re: 5/1/95 Resources Hearing: HB-207

I was unable to remain at the Anchorage LIO for your hearing. Please add the attached testimony from ARCO to the record.

Thankyou

George
cc

Testimony

by

Eric M. Luttrell

for

BP Exploration (Alaska) Inc.

to the Senate Resources Committee

May 1, 1995

Mr. Chairman, Members of the Committee, good afternoon. My name is Eric Luttrell, and I am Vice President of Exploration and New Developments for BP Exploration (Alaska) Inc. Thank you for this opportunity to testify to the Committee today on behalf of BP.

I have come here today to testify on legislation that would encourage the development of marginal fields, fields like Badami and Northstar, fields of moderate size away from existing infrastructure. Many of these prospects would not have been considered for development only a few years ago. Because the development of these fields within BP is directly under my control, I have taken a special interest in this legislation.

In particular, I would like to talk to you about the version of this bill that passed the House and the differences between that version and the draft Senate Resources Committee Substitute that we received Sunday evening. We have a number of concerns with the proposed language of the Senate bill, but I only want to address a few of the main ones here today.

Let me begin by briefly reviewing the context for this legislation. In looking at our business in Alaska and our opportunities to develop the business and make it grow, we in BPX Alaska see a number of situations in which the State's present royalty terms may impair our ability to compete within the BP Group for the capital funds to make the investments needed to keep our business sound and healthy for the future. Although BP is a large corporation, it still has only a finite amount of money available each year for capital investments worldwide. Naturally, in allocating these capital funds, priority is given to those investments that are most attractive. So if BP's capital funds are all allocated to more attractive investment opportunities elsewhere before we get down to our Alaskan projects, then the Alaskan projects simply don't get funded even though they may still be quite attractive and feasible economically on their own terms.

This is a fact of life for us, and in this, BP is no different from any of the other oil companies still active in Alaska. The state and those of us who work for BP in Alaska are engaged in a global competition for investment dollars. It is, of course, of great personal concern to those of us working here, because in large part our jobs here are on the line if we don't compete successfully. It is also of concern to us as Alaskans, because the continued oil and gas development of this state is essential for its future economic well-being. So it is extremely important that whatever "economic feasibility" test that is applied to an application for royalty adjustment recognize this global competition.

We have repeatedly stated that we believe this type of legislation is important for two reasons. First, it helps us to successfully compete for investment funds for Alaska. Second, it allows the State to share the risk of low oil prices and to share in the benefits of higher oil prices with us. In fact, the State of Alaska could under a sliding scale royalty scheme based on oil prices receive higher royalty revenue than under the current structure. This is an important point to remember by sharing the low price risk, the State gains increased revenues at higher prices.

There may be some confusion over how a sliding scale royalty mechanism may operate. The royalty rate would be determined by the price of crude oil. For instance, at a $16 crude oil price (the approximate current State forecast), the royalty rate could be 12.5%, which is the current royalty rate. If, for example, the price of oil increased to $18, the royalty rate could increase, say to 15%. On the other hand, if the price of crude oil drops to $12 a barrel, the rate could drop to 10%. This mechanism would allow the royalty rate to follow oil price. The higher the price, the higher the rate - The lower the price, the lower the rate.

The House-passed version of HB 207 would give the commissioner of Natural Resources clear authority to modify the terms of the State's oil and gas royalties in a variety of ways in order to facilitate and encourage the new investments that need to be made in order to bring marginal new fields into production and to sustain production from existing fields that are in decline. At the same time, it contains safeguards to protect the State's best interests. By protecting those interests while allowing our Alaskan opportunities to be made more competitive against the opportunities elsewhere, the House version embodies a win-win approach for the State and its oil industry. It is a good bill, and BP fully supports it.

Unfortunately, the same cannot be said of the draft Senate Resources Committee Substitute for the bill. It is badly flawed, and seriously out of touch with the realities of a mature oil industry in Alaska.

Problem number one is the requirement that any royalty adjustment be ratified by the legislature. This, combined with the extensive findings that the Commissioner must make, is an invitation for long delays in final approval and litigation. It is entirely possible that it would be six months to a year before an applicant would know whether a project would have a revised royalty arrangement. This process will also compromise any ability to keep sensitive proprietary information confidential. All of this adds up to additional uncertainty. We recognize the importance of appropriate oversight, but we need to devise something that would not unduly burden the State's and industry's ability to get

these marginal projects developed. We think the oversight provisions in the house version of HB 207 would be effective.

There is another point that is relevant to the whole question of oversight of the Commissioner's decisions, and that comes in the form of a question: What incentive does BP have to make a deal that is not in the best interest of the State? We will be doing business in Alaska for a long time. Since the nature of the deal will be examined many times after it is made, any undue advantage that we may have gained will become readily apparent. We would fully expect the State to try to recover that advantage in some other way, e.g. increased taxation. In short, it is not in BP's, or any other company's long term interest to make a deal that is bad for the State.

My second major concern is that of encouraging development of new pools within existing fields. Here again, the Senate version could have the effect of discouraging investment and development by carefully removing the words "pool, or portion of a field or pool" everywhere they occur in the House version, leaving only references to "field."

This reflects a fundamental misunderstanding about how investment decisions are made. Fields are not economic monoliths, nor do we view them that way. Each new investment in a field has to be justified at the margin, on its own merits. The profitability (or economic failure, for that matter) of prior investments in a field has no bearing on the decision to make the new investment or not. The plain truth is that there are investment opportunities that are truly marginal in all fields. In terms of competing for limited capital funds, it is just as important to recognize this fact for opportunities in large fields as it is to recognize it in the context of little fields.

A third problem is we do not understand what the State gains by providing that all of the provisions of this bill terminate at the end of March 15, 1999. As a practical matter, if future legislatures and administrations believe that this bill is not in the best interest of the State, it will be repealed. In this sense, the bill and all of the royalty adjustments that are made under its authority will be constantly under review. Nevertheless, if the Committee would be more comfortable with a sunset provision, it should allow a reasonable period for this set of proposals to work. We believe this is a minimum of five years.

What is at stake in the near term? We believe that effective legislation can have a big impact on our decision to develop Badami, and on our decision to develop Northstar. We expect that both of these decisions could be made in 1995 and lead to significant production and revenue by 1998.

Badami: I will tell you candidly, I don't know whether we would request royalty adjustment for Badami. That request awaits complete review of our drilling results and the engineering cost estimates. I can tell you that we have a group of experts working diligently on both issues to get us answers to these questions by mid-summer. Then we will run the economic analyses and take a decision to make a request to DNR, if we believe the field is developable but marginally economic under low price conditions. And if enabling legislation passes this year.

That is a lot of ifs in a row, but that is the nature of our decision at this time. If we defer the decision to develop out of 1995, we, and the State will lose the opportunity to start production and revenues in 1997. We both loose; Production and Revenue... I fail to see how deferral is in the best interest of either of us.

Northstar: Simply stated, development of Northstar in the foreseeable future requires passage of legislation including net profit share adjustments as a part of the negotiation with the State. We had hoped that we would be talking with the Senate about extending the terms of the House bill to net profit share leases. Now, we are in doubt as to whether there will be a royalty adjustment bill that has any practical effect. This means that we are two steps away from any plan to develop this significant prospect. Pretty strong words, but I could not recommend to BPX proceeding with Northstar development without a change in the NPSL terms.

We have been very open with the DNR on our concerns about Northstar and have even proposed some possible agreements that would protect the interests of both the State and BP. But they require legislation. With legislation, we believe we would be negotiating with the State before year end. Delay of legislation or failure to include NPSL would defer the development of Northstar by 1-2 years and, because of that , delay production and revenue from Northstar by 1-2 years. I fail to see how that is in the best interest of the State.

Are there other marginal accumulations on the North Slope that could be developed in the near term? Absolutely. Will their development be encouraged by this legislation? I don't know, they are not mature enough for us to have a clear view of their economic value. I certainly do not expect that all will.

What is in it for the State of Alaska? The State of Alaska stands to benefit greatly from these developments, and from their timely development. At Badami, we project State revenues (using current State price forecasts) of upwards of $350 mm (royalty, severance, ad valorem, income taxes), plus jobs and the infusion of

several hundreds of millions of dollars of additional investment during development. Investment in, and revenues from Northstar are similar.

When we look beyond the specifics for Badami and Northstar, the proposed legislation has the potential of sending a strong message to the Industry, to Houston, to Los Angeles and to London, a message that Alaska wants to work cooperatively with Industry to encourage investment and new development; that Alaska wants to compete. Not passing legislation this year or passing the wrong legislation will send the opposite message. We believe that this bill is both necessary and beneficial to the state and to industry, but it must be in a useful format. The House version was carefully considered and would work. The Senate version would not work very well.

I have tried to be open, direct and candid with you here today, just as we would be with the State in a negotiation. Those of you who know me, know that it is my style and it is BP's style. Like it or not, the State and the industry have much to gain by improved openness and cooperation and we look forward to a long and mutually beneficial relationship.

Thank you for the opportunity to testify.

Testimony of
James F. Branch
On House Bill 207 and the Business and the Investment Climate in Alaska
Before the Senate Resources Committee
May 1, 1995

Mr. Chairman, members of the Committee, my name is Jim Branch. I am the Production Manager with responsibility for Exxon's interests here in Alaska. I appreciate the opportunity to follow-up on my comments of last Wednesday about the need to send a positive signal that our state is trying to improve the investment climate for the oil and gas industry.

We have supported efforts by the Administration and the legislature that attempt to provide clarity, predictability and a reasonable balance to the Commissioner of Natural Resources' existing authority to grant royalty relief. The Administration's original bill and the substitute reported out of the House had that intention. However, the current Senate Resources version appears to send a very negative signal to our industry.

The changes made to the final House bill are significant and numerous. Rather than go line by line through the bill, let me return to some principles for a well designed incentive, which I offered in my testimony of early February. An incentive is ineffective if an investor concludes it can be taken away over time, it has a hidden price tag, or creates an environment for future disputes. This version of the bill would do all of that. The suggestion of reopeners, sunset provisions, legislative review and repeated references to "value" and marketing of oil and gas are enough to discourage any serious investor These conditions send the opposite message to the one I hope you ultimately intend to communicate

Investors are keenly aware of the poor investment climate in this state, relative to other opportunities available to them, and are looking for indications that change is possible. The results of the debate on this bill and more importantly progress on fiscal reform, primarily through spending reductions, are measures by which we will be judged. Until spending is brought more in line with revenues, oil and gas investors will be wary of placing significant new funds in the state. Our industry already provides 85% of the state's funding, and there is a history of looking to us to fill revenue gaps. I applaud the leadership this legislature has demonstrated in beginning to address the fiscal situation.

Investors are prepared to assume the traditional risks associated with finding and developing oil and gas, but not those created by the state in the form of concerns over increased taxes or uncertainty over an incentive granted under this version of HB 207. With their versions of this bill, the Governor and House demonstrated their intention to attempt to provide clarity, predictability, and reasonable balance to the DNR Commissioner's current authority to revise royalty. I urge you to join this effort.

Senator Loren Leman, Chairman
Senate Resources Committee
State Capitol
Juneau, Alaska 99801

May 1, 1995

Dear Senator Leman:

While I am not able to be present at the Senate Resources Committee hearing on House Bill 207 today, I would like to offer this letter to the Committee on behalf of Lynden, Inc. Lynden is vitally interested in the outcome of House Bill 207 because of the extensive amount of our work that is directly related to oil and gas development through Lynden Transport, Alaska West Express/Frontier, Lynden Air Freight, and Lynden Logistics.

Lynden supports the final passage of House Bill 207 this session. We are pleased that the House passed a reasonable bill after extensive public testimony. Even though it is now relatively late in the session, we urge you to adopt the same or very similar bill as arrived in the Senate.

We have reviewed the proposed Senate CS for CS for HB 207 (Res.) and feel that some of the changes will defeat the purposes for which the bill was introduced. In particular, we believe that the decision to adjust a royalty should be made by the Administration - be it Republican, Democrat, or Independent. Legislative approval or review will delay a decision and drag it into the political arena.

Also, the suggested sunset and termination provisions are neither necessary, nor do they send the "signals" to the oil industry that we thought both members of the legislature and the Governor promoted during their recent election campaigns.

Last, because the royalty adjustments may already go both up and down in the House Bill, it is unreasonable to require the State to maintain the power to unilaterally change the terms of the royalty adjustment during the development of the field.

We have watched with dismay and downsized with the oil industry during the past several years of relative polarization between the State and our biggest industry partners. We hope to see a new, more positive attitude. Passage of HB 207 would offer the first concrete steps in this new relationship.

Sincerely,

Dave Haugen

Dave Haugen, Vice President
Lynden, Inc.

Peak
Oilfield Service Co.

FAX

DATE:	05/02/95	
COVER PLUS	2	PAGE(S) TO FOLLOW
TO (COMPANY):		
ATTENTION:	SENATOR LOREN LEMAN	
FAX NO. :	465-3810	
FROM:	M.R. O'CONNOR	
OPERATOR:	SONDRA	PHONE: (907)561-3200

OUR FAX NUMBER: (907) 562-5860

Dear Senator Leman:

The following commentary was prepared for the Senate Resources Committee meeting on HB207 scheduled for May 1, 1995 at 3:30 p.m.

Because of Senate delays, I was unable to stay in Juneau to deliver this testimony. I wanted all members to be advised of my feelings towards HB 207.

Sincerely,

M. R. O'Connor

TESTIMONY
OF
MR. MIKE O'CONNOR

PRESIDENT AND CEO
PEAK OILFIELD SERVICES CORPORATION

TO THE

SENATE RESOURCES COMMITTEE

ON

HB207

JUNEAU, ALASKA

MAY 1, 1995

Mr. Chairman, members of the Committee, for the record my name is Mike O'Connor, President and CEO of Peak Oilfield Services Corporation. We're an Alaskan corporation, employing over 600 employees with offices in Prudhoe Bay, Anchorage, Kenai and Valdez.

I am appearing before you today in support of the royalty reduction bill that was introduced by the Governor and passed overwhelmingly by the House. This legislation will have a demonstrative impact on the future of our company and our employees. Without it, I see a significant loss of revenue and subsequent job losses. Bottom line-I'm here to promote and protect the working class Alaskans who would rather have employment than unemployment.

Quite frankly, I'm somewhat confused and disheartened with the previous version and latest drafts prepared by the Senate Resource Committee. While I understand and certainly respect this committee's prerogative in issuing a new draft, I do not understand the need or motivation for such sweeping changes ~~about~~ without public comment

As I am sure you are aware, the House had a considerable number of hearings and worked diligently in developing a draft that was embraced by the administration, the oil companies and its service contractors, as evidenced by the 35-2 vote in the House. I would strongly urge you to reflect on their deliberations and attempt to draft your version as similar to the House version as possible.

The purpose of this legislation was to encourage additional investment for the benefit of all Alaskans. It is imperative that Alaska be perceived globally as a fair and competitive environment in which to invest. The Senate Resources Committee version stops short of achieving this goal. You've already heard from several folks about deficiencies in the draft before us today.

One specific concern that I would like to add in Section 2, paragraph B (Page 2, line 19). My comment is simple: Industry needs to project a reasonable rate of return. The proposed language in this section requires that a loss be projected prior to application. This does not and will not create the perception that Alaska is a good place to invest.

I'm also concerned about the legislative oversight requirements. The potential delays could result in the entire loss of a construction season. Remember, time is money.

I recently read that the Senate is contemplating adjourning early and find it incomprehensible that this issue not be faced head-on by the Senate floor. I urge all pro-business, pro-development, pro-Alaskan Senate representatives to study and understand this legislation.

In closing, I would like to thank you for this opportunity to testify and again encourage you to reflect on the language passed by the House of Representatives.

★ 1975 *Serving Alaska for 20 years* 1995 ★

Resource Development Council for Alaska, Inc.

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

Post-it™ brand fax transmittal memo 7671 | # of pages > 2

To Sen. Kerttula	From Carl Portman	Phone # 276-0700	Fax # 276-3887
Co.	Co. RDC		
Dept.			
Fax # 465-3810			

Testimony of Resource Development Council
on CS HB 207
An Act relating to the reduction of royalties reserved to the state to encourage production of oil and gas from marginal fields
Senate Resources Committee
May 1, 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 CS for HB 207.

RDC strongly supports HB 207, as passed by the House. The House version of this legislation provides the flexibility needed for the State and industry to work together to change the economic equation for marginal fields. It provides flexibility for working with investors on a case-by-case basis to overcome Alaska's unique challenges and make new development and production a reality. Alaskans will benefit from new jobs, long-term revenues and increased economic activity associated with the development of new fields.

HB 207 is a tool the State can use to enhance the competitiveness of projects whose funding might otherwise go abroad. It sends a clear signal that Alaska aims to be competitive in the world market to attract the investments necessary to develop its oil and gas potential.

The Committee Substitute, however, risks undermining the original purpose of the initiative. It opens the door to potential delays and more uncertainty. Its complexity sends a negative signal and it may, in the end, have no practical effect.

RDC does not believe the latest CS fixes the problems expressed last week with the initial Senate draft. The March 1999 deadline for royalty adjustments on new fields still puts us back to square one as far as future discoveries are concerned. It may be a partial fix for marginal fields that are ready to go forward in the near term, but it doesn't do anything for companies considering investments over the long term. Some of those companies may not even be operating in Alaska today, but are waiting for a clear signal before they invest in prospects that are beyond the short term.

RDC also takes exception to the requirement that a field's operating costs must exceed revenues before a royalty adjustment can be considered. How does a one or two percent rate of return compare with investment returns elsewhere? If Alaska is to be truly competitive, it must be willing to take the necessary steps to ensure that marginal fields here pay as well or better than investments that oil companies could make in other parts of the world.

Other issues of concern include the provisions for legislative oversight beyond what is called for in the House version and the basing of royalty adjustments upon the economic feasibility of production from an entire field as opposed to a pool or portion of the field or pool.

HB 207, as passed by the House, is a good piece of legislation which should not be changed significantly. It protects the State's best interests if a marginal field turns out to be more profitable than anticipated.

RDC believes the House version will send a clearer signal to investors and will do more to strengthen Alaska's competitive position. We believe it is a stronger and more effective royalty adjustment bill.

Thank you.

Union Oil Company of California
Testimony on CS HB 207
Senate Resources Committee
May 1, 1995

Mr. Chairman and members of the Resources 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 CSHB 207. I would like to begin my testimony by saying that the Sectional Analysis provided with the Bill is particularly helpful in making a more informed analysis of the Bill. Some of the concerns I expressed in last Wednesday's Hearing have been clarified by the Analysis and therefore the enclosed testimony more accurately reflects Unocal's view and opinion of the Bill today.

Subsection (j)(1)

From purely a Unocal perspective, based on its present acreage position, Unocal is not directly impacted by paragraph (A). Most of the Unocal leases held today are located within producing fields, some of which are nearing the end of their economic viability. We have however, testified in earlier hearings on this Bill that we have not endorsed the concept of Sunset Provisions.

Subsection (j)(4)

We believe the requirement for legislative approval under paragraph (A) will be a time consuming and unnecessary requirement resulting in an administratively burdensome process. Under the House Finance version of the Bill, adequate Commissioner oversight is provided under Subsection (j)(6).

In reading the provisions of paragraph (B) of this Subsection, it is unclear to me as to the intent of the language "in amount or value of the Production". If this is to mean a net 3% floor or a maximum 76% reduction of the current royalty rate, then Unocal is opposed to this revision. Under the House Finance version of the Bill, the floor established for producing and shut-in fields is 90%. There needs to be clarification on this point. Any increase in the floor reducing flexibility would be inconsistent with our position and prior testimony.

Subsection (j)(5)

Although we appreciate the attempt in this CS to address the assignability question, we believe a strong argument still exists for elimination of this restriction all together. The assignment of all right, title and interest in a lease is a fundamental principle in the oil industry. Property trades will be greatly restricted if assignability of a royalty adjustment is not allowed. Because of the confidential nature of property transactions, companies are not going to disclose their intent to the public in asking for permission to assign until negotiations are complete and commitments have been made. Prior approval does not work in this situation. A negative response to a request for assignment could jeopardize

a potentially beneficial trade to the state. The ability and desire to acquire a lease that has favorable royalty terms may be the catalyst and incentive for a company to invest capital and employ new ideas in fields where the current owners may be less inclined. Companies are rationalizing properties and focusing investments in core areas to take advantage of their particular operational, infrastructure or informational strengths. Lost opportunity for additional development of a lease or field is sure to occur if this unecessary limitation is imposed. The intent of this legislation should be to create opportunity with certainty, not further limit the creativity of the industry. The state's best interest will not be served with this restriction.

Subsection (j)(7)

This issue of contractor selection was thoroughly discussed in prior hearings with what we thought was an equitable compromise and consensus opinion of the parties testifying. We see no advantage to changing this Subsection and would prefer tc see Subsection (6) of the House Finance version reinstated.

Subsection (j)(9)

Reviewing and addressing all the requirements under this Subsection will be very expensive, time consuming and may not bo applicable in all circumstances. We believe the Commissioner should have the discretion to provide for the contents of the best interests finding and determination. The Department of Natural Resources is well equipped for this process. The degree to which each of these conditions are to be investigated will be the subject of much debate. If the committee and legislature feel the need to include the details of the finding and determination in this Bill, then paragraphs (A) through (D) should only be suggestions of issues the Commissioner may consider not requirements in a royalty adjustment application.

Subsection (j)(12)

We have a similar comment in this Subsection as in Subsection (j)(4) in that legislative approval is unnecessary, time consuming and administratively burdensome. We contend that Subsection (j)(10) of the House Finance Bill is more appropriate and should replace this Subsection.

In conclusion, we want and need a Bill and process that is, clear ,fair, flexible and equitable, otherwise we will end up with a piece of legislation that is under utilized.

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

Thank You

Union Texas Petroleum

May 1, 1995

Union Texas Petroleum Alaska Corporation

1330 Post Oak Boulevard
P. O. Box 2120
Houston, Texas 77252-2120
Telephone: (713) 968-3500

Bruce S. Hamilton
Director, Business Development

VIA FAX

The Honorable Senator Loren Leman,
Chairman, Senate Resources Committee
Capitol Building
Juneau, AK 99811

RE: **SCS CSHB 207 (version B 4/29)**

Dear Senator Leman:

We thank you for being given the opportunity to comment on the Senate Resources Committee's draft substitute for CSHB 207. We reviewed the draft SCS CSHB 207 (version S) and SCS CSHB 207 (version B) which we received this morning. Our comments go toward the intent of the bill.

Union Texas Petroleum Alaska is an indirect wholly owned subsidiary of Union Texas Petroleum Holdings, Inc., one of the largest independent producers located in the United States. Union Texas explores for and produces oil and gas overseas, primarily in the U.K. North Sea, Indonesia and other strategic areas. Our 1995 exploration plans include exploration wells in Alaska, Argentina, Indonesia, Ireland, North Sea, Pakistan, Tunisia, and Vietnam.

During the past four years, Union Texas Petroleum Alaska has increased its exploration activity in Alaska which included participation in ten wells plus three sidetracks in the Colville River Delta area, one well in the Jones Island State Exploration Unit, three wells in the Kuvlum Federal Unit in the Beaufort Sea, and the Diamond #1 well in the Chukchi Sea. Additionally, in late 1993 Union Texas entered into a Kenai Peninsula exploration venture with Cook Inlet Region, Inc.

Internally, Alaska projects compete with international projects for funds. Union Texas has funded Alaska exploration based on its perception of an opportunity as the majors move to the former Soviet Union and on the expectation that the State will perceive and adjust to the world market. Currently, we are experiencing a willingness of countries throughout the world to reduce government take to be more competitive and to entice additional exploration and development risk capital investment within their provinces. With the passage of CSHB 207 by an overwhelming majority in the House, we were encouraged that Alaska was serious in its efforts to move toward competition in a world arena, and is beginning to provide incentives to further investment and exhibit the needed flexibility demanded of all competing oil and gas provinces.

Union Texas Petroleum Alaska supports CSHB 207 as passed by the House.
Union Texas Petroleum Alaska opposes SCS CSHB 207 (version B).

Our optimism with the introduction and overwhelming passage of CSHB 207 in the House was quickly dampened when we read the Senate Resource Committee's redrafts of CSHB 207 (version S) and recently (version B). Not only did both redrafts of CSHB 207 take away from a proposed bill that seemed to provide flexibility, certainty and timeliness, it introduced a sunset clause, legislative approval and many other limiting provisions which are clear, negative signals to Union Texas Petroleum Alaska. This version may negatively impact our long-term strategic exploration investment planning for this province when being measured against other world wide exploration areas.

Among other concerns with SCS CSHB 207 (version B) we offer the following:

- The deletion of the words "pool, or portion of a field or pool" everywhere they occur in the House version, leaving only references to "field", discourages development of new pools within existing fields and should be restored.
- The sunset provision should be deleted in its entirety.
- Legislative approval is unnecessary, burdensome and infuses needless uncertainty in a process that needs flexibility.
- The unconditional ability to assign rights is an absolute necessity.
- Clarify royalty may only be adjusted if agreed to by Lessor and Lessee.

In summary, Union Texas Petroleum Alaska Corporation believed CSHB 207 provided an alternative for companies who expend risk capital over long periods of time with no apparent opportunity for a return on investment. In our view, the major enticement of CSHB 207 for the State and to the investor company was to create a new revenue stream for both.

Very truly yours,

UNION TEXAS PETROLEUM ALASKA CORPORATION

BS Hamilton

Bruce S. Hamilton
Director, Worldwide Business Development

/mw

facsimiie
TRANSMITTAL

to:	Ms. Annette Kreitzer, Senate Resources Staff
fax #:	907-465-3810
re:	CS HB 207 (B)
date:	May 1, 1995
pages:	3, including cover sheet.

Dear Ms. Kreitzer:

Please forward the attached comments from Union Texas Petroleum Alaska Corporation concerning CS HB 207 (B) to Senator Leman.

Your assistance is appreciated.

Please call me at 713-968-2594 if you have any questions.

Union Texas Petroleum Alaska Corporation

Steven R. Fly

EXTRA copy attached.

From the desk of...

S. R. Fly
Manager Business Development
Union Texas Petroleum Alaska Corporation
1330 Post Oak Blvd.
Houston, TX 77056

713-968-2594
Fax 713-968-2593

Testimony of

Paul Wessells
Director of Tax

BP Exploration (Alaska) Inc.

to the

Senate Resources Committee

Juneau, Alaska
April 21, 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 year. 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 for individual leases, rather than solely as part of a unit application, and allows for adjustments with respect to individual pools of oil and gas within a lease.

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 must 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.

BP also believes the bill should allow the Commissioner of Natural Resources to modify state net-profit share interests in the same way that it allows the Commissioner to adjust state royalties. Net-profit payments and royalty payments are similar forms of economic rent

that the State receives from leasing its lands for oil and gas exploration and development. We think giving the Commissioner flexibility to address the full economic picture when reviewing an application for adjustment is a good idea, and so it does not seem appropriate to us to give the Commissioner that flexibility with respect to one form of the economic rent and not the other. Just as the State may gain by modifications of the royalty obligation under a sliding scale royalty mechanism, so it should gain in similar circumstances by allowing appropriate modifications of a net-profits interest.

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.

NANA DEVELOPMENT CORPORATION
1001 E. BENSON BOULEVARD, ANCHORAGE, ALASKA 99508
TELEPHONE (907) 265-4100

April 28, 1995

MAY 1 1995

Senator Loren Leman,
Resource Committee Chair
Alaska State Legislature
State Capitol (MS 3100)
Juneau, AK 99801-1182

Dear Senator Leman;

I want to express NANA Development Corporations support of the **original** HB 207. It is imperative that the State of Alaska and Industry work together in the development of marginal fields. As you know, NANA has been a supporter of not only mineral development but also has a small ownership in the Endicott Oilfield.

NANA has seen a severe economic impact on its oilfield subsidiaries. Due to the downturn in oilfield development, NANA was forced to sell it's drilling company Alaska United Drilling Inc. and closed down the oldest operating hotel at Prudhoe Bay, the "NANA Oilfield Hotel". The shut down of these businesses cost Alaska and NANA over 200 jobs in addition to several million dollars in losses.

We cannot survive if we continue to do business the old way. New thinking is needed. HB 207 is new thinking. HB 207 is good legislation and should not be changed. Please lend your support and vote for the **original** HB 207.

Sincerely,

Joe B. Mathis
General Manager
Oilfield Operations
JBM/sb/187

Hawk CONSTRUCTION CONSULTANTS, INC.

Senator Loren Leman
Chairman -- Senate Resource Committee
Alaska State Legislature
State Capital (ms 3100)
Juneau, Alaska -- 99801-1182

27 April 1995

Subject: HB207

Dear Senator Leman, et al.:

Please, don't kill the goose that lays the golden eggs.

We (all the citizens of Alaska) are competing for a very limited resource -- Capital investment funds. The current oil companies in Alaska are all part of an international community who have responsibility to their "stakeholders" and stockholders. As responsible businesspersons they must deliver the best bang for their investment buck. Alaskan's are competing with oil development countries where the cost of doing business is significantly less than in Alaska. Because of this fact, capital investments in other areas of the world offer more potential for profit, the life blood of any business.

My small company has been supporting the oil industry for the past 10 years since being founded here in Alaska in 1985. No other industry so greatly affects my business as does the fortunes of oil. We are small but our existence supports many other local industries and businesses. We spend our profits here in Alaska.

Please pass HB207 in the same form as passed by the House of Representatives. I believe this will give the Commissioner of Natural Resources the flexibility to assess and negotiate with the oil companies a fair and attractive package with the State of Alaska.

As with any business, regardless of the potential for profit, all factors must be considered in choosing to do business anywhere. If a business is constantly confronted with an ever-changing business environment, eventually the business will go where life is easier. The cost trend line and the revenue potential line must run, at a minimum, parallel. If there is any sign where these lines will intersect, the business will not wait for losses to occur, they will eventually leave for a more productive business environment outside Alaska, (e.g., Chevron, Conoco and Shell).

As responsible citizens of this state we must support, and make welcome, those industries that best support our Alaskan quantity and quality of life. As responsible citizens of the United States we must make available and attractive those future opportunities (e.g., ANWR) protecting our strategic independence in an increasingly competitive and unstable world.

Very truly yours,

Maynard V. Tapp -- President
HAWK CONSTRUCTION CONSULTANTS, INC.

cc: Senators:, Drue Pearce; Steve Frank; Rick Halford; Lyda Green; Tim Kelly; Steve Rieger; Randy Phillips; Judy Salo; and John Torgerson.

The Chez Braun Building • 1407 W. 31st Ave. • Suite 800 • Anchorage, Alaska 99503 • (907) 278-1877 • Fax (907) 278-1849

Alaska Support Industry Alliance

Testimony on

Senate CS for CS for House Bill NO.207 (Res)

Adjustments to Oil And Gas Royalties

To The

Senate Resourseso Committee

April 27,1995

DRAFT

The Senate version of house bill 207 (CS for CS HB 207) is completely unacceptable for the following reasons:

Section 1 AS 38.05.180 (j) 1 (A) after the effective date of this Act and not later than January 31,1998 to allow for production from an oil or gas field if etc.

This provision only allows for a three year window for application, which means that it would only apply to fields that are known of today.

(4)may not grant a royalty adjustment for a field
(A) under (1)(A) of this subsection
(i) if the anticipated aggregate value of the proposed royalty adjustment is a reduction that would exceed $5,000,000. or if the royalty adjustment is a reduction that exceeds 50 percent of the royalty originally specified in ---------- unless approved by the legislature.

This is not what was intended with the original house bill. The original bill was intended to be expeditious and have an effective degree of confidentality. This provision with the $5,000,000.00 threshold means that every application will require legislative approval. We disagree with the need for legislative approval, but if you are going to impose a threshold at least make it a reasonable one, such as $100,000,000.

(4) (ii) that allows a royalty adjustment that is a reduction to extend beyond December 31, 2002: for royalty that has been reduced by the commissioner for the reason set out in(1)(A) of this subsection,on and after January 1, 2003, the lessee or lessees shall pay the royalty rate that was in effect immediately before reduction of the rate

This means that if you apply for and get a royalty adjustment in 1995 and the field starts producing in 1997, it is only good for 5 years. It is not acceptable to expect global investors to sign on with that short of a commitment.

Post-it® Fax Note 7671	Date 2	# of pages ▶
To SEN. LEMAN'S OFFICE	From KEITH
Co. Annette K.	Co.
Phone #	Phone #
Fax # 907-465-4307 3870	Fax # 561-8870

I can continue to examine this legislation , but the point is that the bill was passed out of the house 35 to 2. This is the bill that the Senate needs to pass out of the Resourses Committee.

We at the Alliance have always had a positive pro-business working relationship with the Senate Resourses. With the opportunities that have been presented to us by the 1994 November election, we have been very optomistic about this legislative session and the future of oil and development in Alaska

The legislature has stated throughout this session that they are collectively in support of marginal field development. But, the amendments that they have added to the HB 207 are contrary to that position of development.

During the public hearings of House Bill 207 the issure of Sunset Provisions, Legislative Review and Approval were discussed . In fact, there was over 30 hours of public testimony.

It is the position of The Alliance and it's membership that HB 207 should be passed by the Senate without amendments as passed by the House 35 to 2.

DRAFT

ALASKA SUPPORT INDUSTRY ALLIANCE
TESTIMONY ON
HB 207, ADJUSTMENTS TO OIL AND GAS ROYALTIES
TO THE
SENATE RESOURCES COMMITTEE
APRIL 26, 1995

Good afternoon Chairman Leman and members of the Senate Resources 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 competively 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.

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.

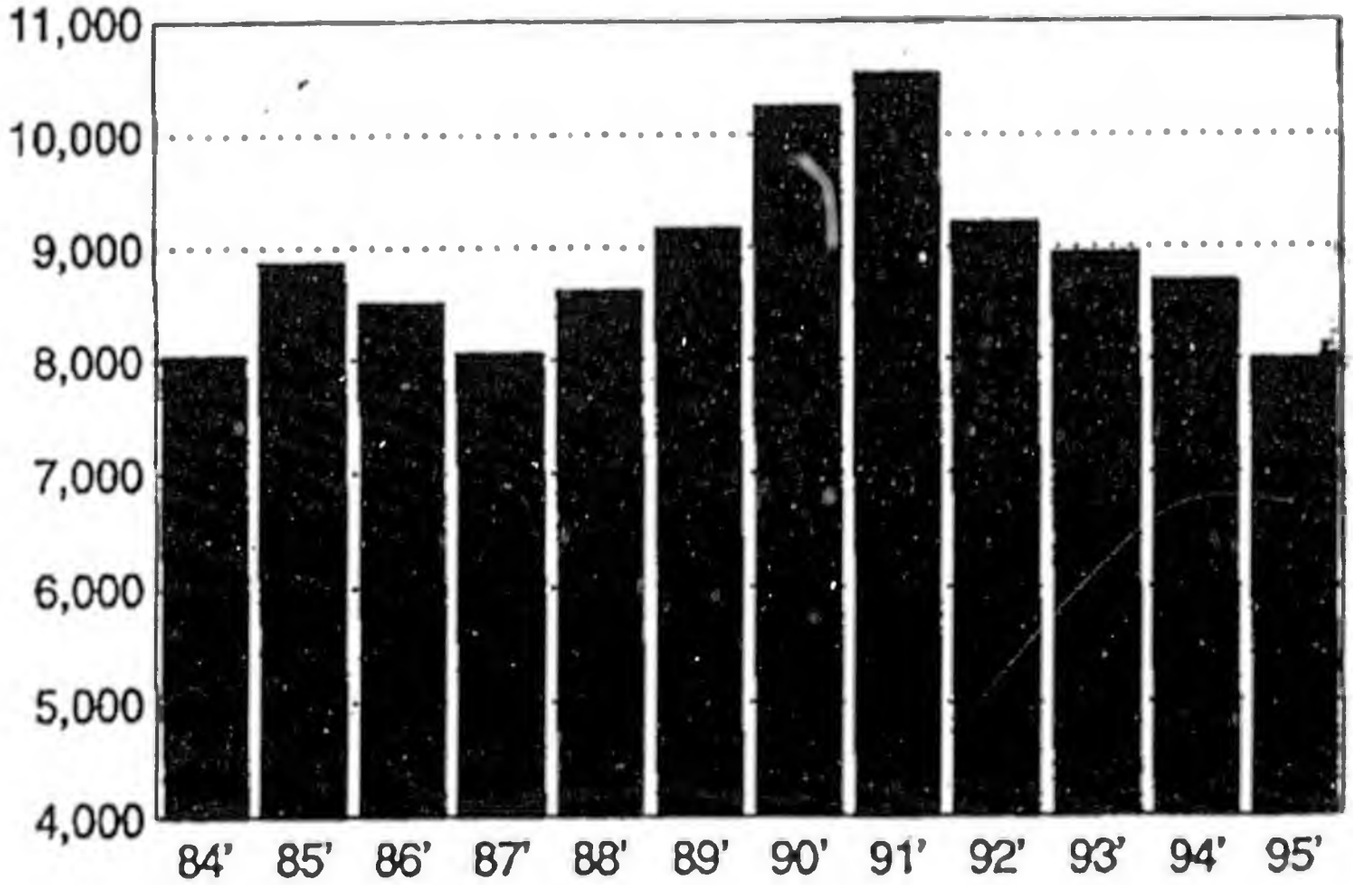
The three hundred Alliance member companies and their thousands of employees urge you to pass HB 207.

Thank you.

Attachments

B 4S.NR.rua

Alaska's Oil Industry Employment Is On The Wane



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 appox. 80 % of state unrestricted revenues through 2010. Current forecast senarios project total Alaska oil production to be one-half current levels (approx. .8 million bl/day) by FY 2006 in the base case scenario.

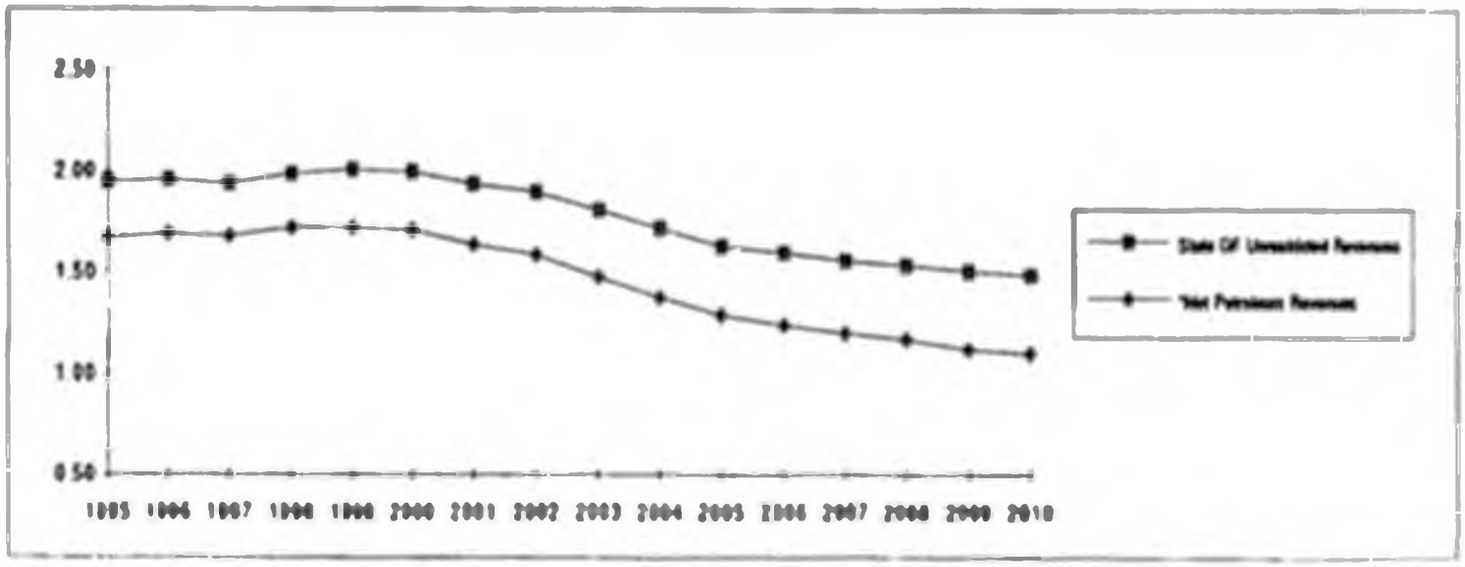
Although higher oil prices would offset some of the negative impact of anticipated lower production levels, ultimately revenues will fall barring some unforeseen oil discovery.

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 Revenue	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 Revenue	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%



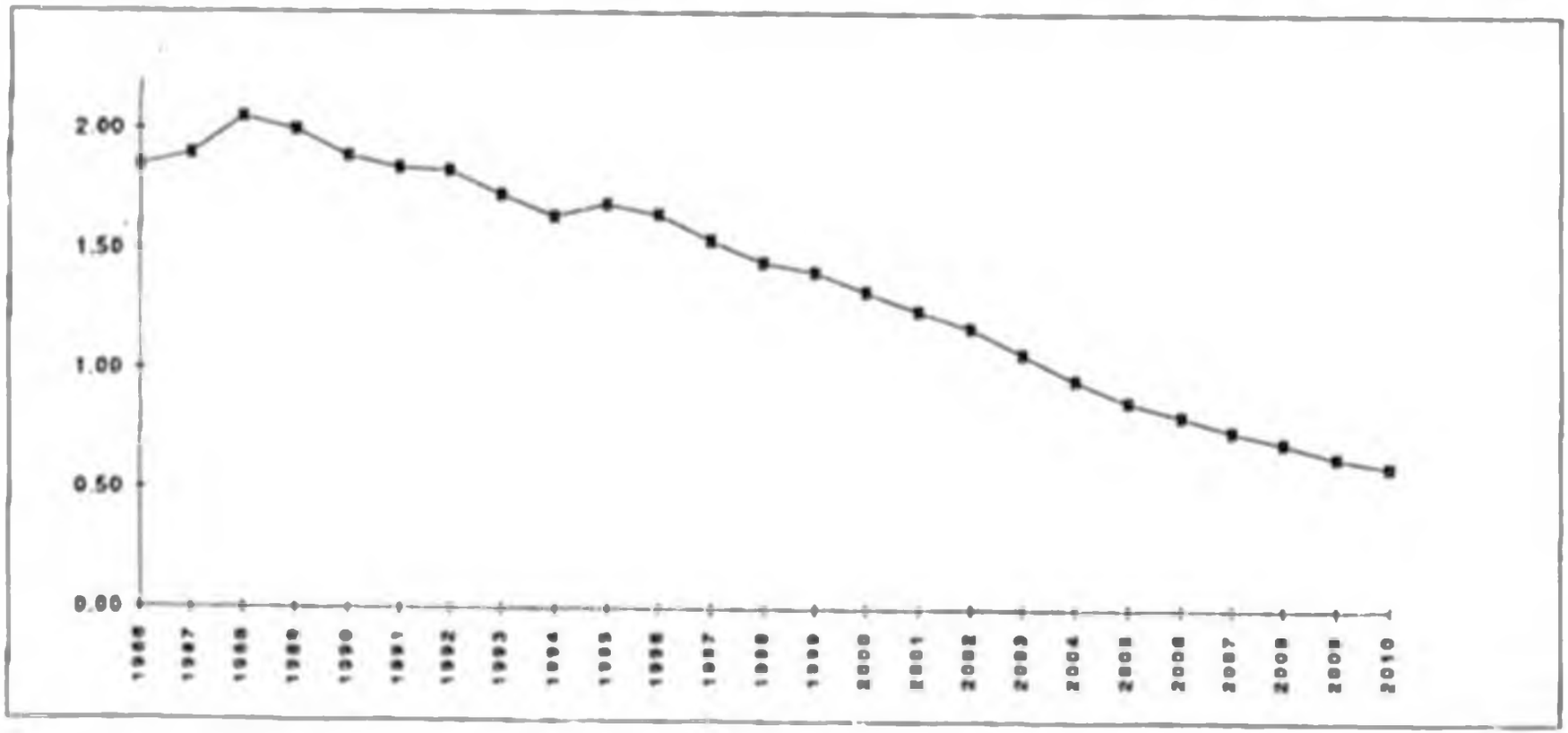
Source AA Department of Revenue
*Net of Permanent Fund Contribution

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 1578 production levels of .8 million barrels per day by FY 2006.

Table 2

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

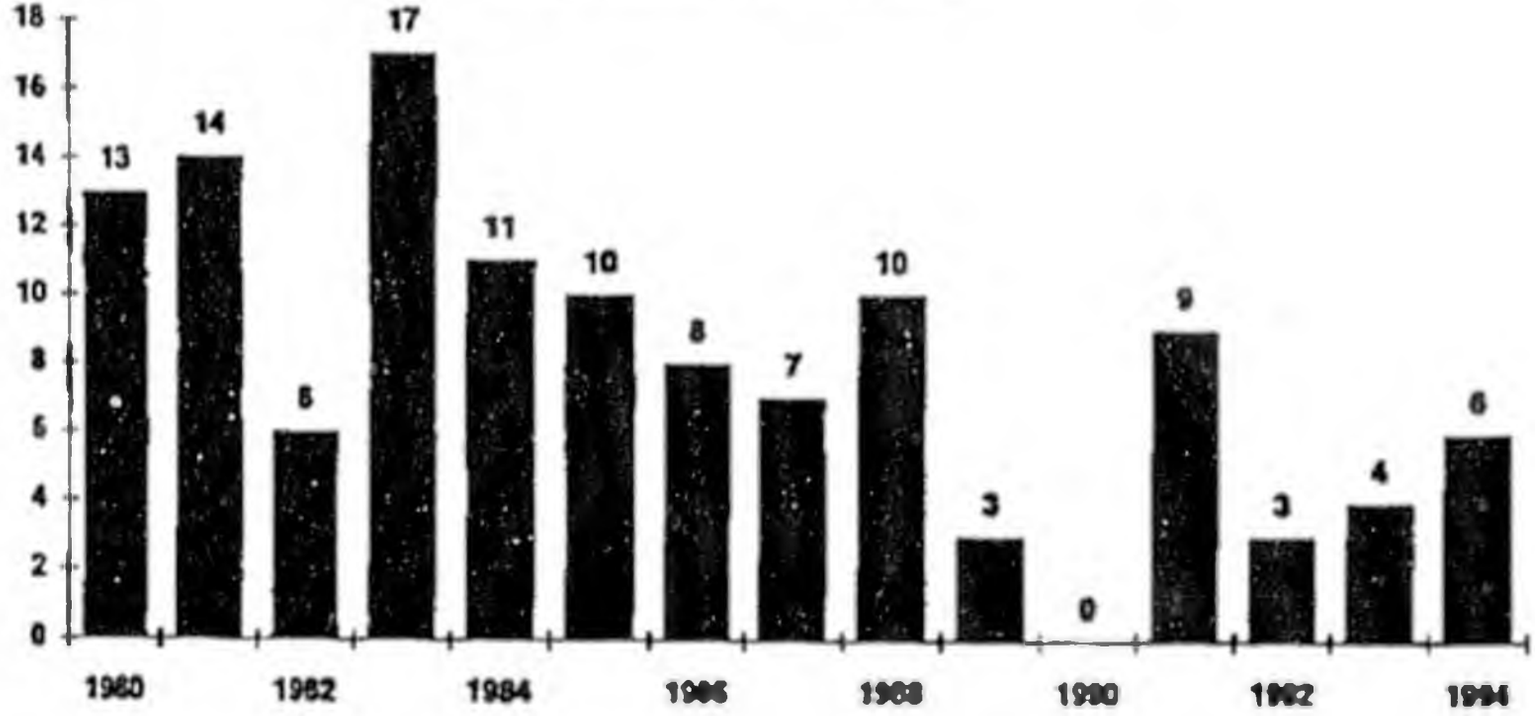
1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
1.85	1.90	2.05	2.00	1.89	1.84	1.83	1.73	1.64	1.69	1.65	1.54	1.45	1.41	1.33	1.25	1.18	1.07	0.96	0.87	0.81	0.75	0.70	0.64	0.60



Source:
Alaska Department of Revenue FY 1986-2010

Alaska Oil & Gas Lease Sales

Average Number of Bidders per Sale



3/10/95

ALASKA WELLS SPUDDED BY YEAR

YEAR SPUD	TALLY
70	69
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	160
95	2
	4332

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

TESTIMONY
BY: GERALD G. BOOTH
VICE PRESIDENT, ENERGY AND MINERALS
COOK INLET REGION, INC.
ON CS FOR CS FOR HB 207
APRIL 28, 1995

DRAFT
OUTLINE
4/28/95
These points need to be put into text.

Good afternoon Mr. Chairman, members of the Committee. My name is Gerald Booth and I'm Vice President of Energy and Minerals for Cook Inlet Region, Inc. CIRI is owned by 6,700 Native shareholders of Athabascan, Eskimo and Aleut descent. The company's principal lines of business are real estate, broadcast communications and natural resource development. I am here today to talk about the latter.

CIRI owns and manages 924,000 acres of surface and 1.6 million acres of subsurface estate in Alaska. CIRI holds various royalty and working interests in several producing and prospective oil and gas fields.

The development of CIRI's lands and resources will play a significant role in the future economic growth and development of south-central Alaska, especially its oil and gas interests on Kenai Peninsula.

CIRI has been marketing its lands on the Kenai Peninsula for oil and gas exploration and has been successful in bringing new exploration of our lands and adjoining State lands.

HB 207 is important to our Company and our shareholders' future and we ask the Committee to passHB 207 as it was adopted by the House of Representatives. Here's why.

My remaining testimony will focus on specific areas of CS for CS for HB 207 that are major concerns to CIRI. All references are to the work draft of CS for CS for HB 207 dated April 26, 1995.

Page 2, line 1 - the recommendation is to change the effective date to an open date. If the State is offering an incentive for long range exploration and development of our oil and gas resources, the legislation should not have a sunset clause.

Page 2, line 9 - "environmentally feasible". If this type of language is required, care needs to be taken to include any and all feasibility based on the world price of oil. EXPAND

Page 2, line 27 - We suggest that the language (concept) use that of the House version ~~in that the process is~~ based on a sliding scale royalty method based on the price of oil. EXPAND.

Page 3, line 3(i) - For any and all developments, a proposed royalty adjustment would be for more than $5,000,000, then all projects would go for legislative review. EXPAND

Page 3, line 12 (ii) - If we are ~~setting~~ adopting an incentive, why is it sunsetted. If the program is not needed due to good profits and high oil prices, no applications will be submitted and if the program is not needed the legislature can terminate the concept. As presently written, the whole royalty concept would be of little value to CIRI in its potential development.

Page 3, Line 18 (B) - Current law permits the Commissioner to go lower than 3% for potential operations in Cook Inlet. I don't see why it is proposed that a floor be established.

Page 3, line 22 (5) - By adding the non-assignable clause, limits investments especially by independents, those companies that are important to Alaska's future development in areas like Cook Inlet. These companies, like the majors, share risk in exploration and development and require new players to come into ventures at different times. The concept as presented in CS for HB 207 is not considered a good one.

Page 3, line 27 (6A) - ~~Here again, by statute you are trying~~ Attempting to identify what may be needed for the Commissioner to make a decision. CIRI does not feel it necessary that this type of guideline to be put in place for the Commissioner. EXPAND

Page 4, line 4 (7) - The concept of selecting the independent contractor as outlined in HB 207 is fair to both parties and is becoming accepted practice at the federal level. We recommend the Senate version adopt the concept in HB 207.

Page 4, line 9 (8) - The comment period should be as reasonable as possible and we suggest that 30 days is sufficient especially when considering all the time constraints that fall into putting projects together.

Page 4, line 14 (9) - The listing of what should or should not be in any findings and determinations should be reserved to regulation. Here again, unnecessary sideboards are added to the legislation that provides openings for future litigation.

Page 5, line 2 (10) - We fail to see the necessity for the Legislative Budget and Audit Committee to be required to go to executive session or whatever to do their work. The time frames suggested again to extend the process. We suggest the time periods go back to those in the House version. In fact, the HB 207 version on the oversight provision by the Legislature is acceptable to CIRI. confidentiality of data.

The objective of all of us is to get more exploration and development in Alaska. We recommend that the Senate reconsider the changes it made to HB 207 and find common ground for the passage of the legislation. The royalty reduction concept is an excellent one and those of us in the business of marketing Alaska resources see it as mandatory to the future development of Prudhoe Bay and more important to us, Cook Inlet.

On behalf of Cook Inlet Region, Inc., I urge you to support HB 207 and reconsider the limiting issues of CS to HB 207. Thank you.

Testimony of John Ellsworth
in support of House Bill 207

Good afternoon Mr. Chairman and members of the committee. My names is John Ellsworth and I'm President and owner of Alaska Interstate Construction, a firm that provides construction services to the mining and oil industries, as well as the State of Alaska. During the construction season Alaska Interstate employs over 200 Alaskans throughout the state. I'm here today on their behalf to tell you why House Bill 207 should be adopted by this committee, and in essentially the same form as it was passed by the House of Representatives last week.

In the past few years we've seen a dramatic shift in the investment activities of international oil companies. A shift away from investment in the United States and a shift towards investing in other areas of the world. This is due, in part, to changing international politics, development of new technologies, and the development of more cooperative relationships with host governments in other oil regions. But what really drives this change in oil company investment strategies is their potential return on investment. And in Alaska, Mr. Chairman, the potential for realizing a reasonable return on investment is growing smaller every year.

The oil industry in Alaska has done everything possible to rein in their costs to remain competitive in the world market. They've downsized their operations, started sharing services, and invested heavily in new technologies. It's a far different industry than when I got my first contract on the North Slope. It's leaner and certainly a whole lot meaner. But the steps the industry has already taken resulted in their remaining reasonably competitive for further investment in the short term.

But there is an obvious limit on how much more they can reduce their costs. Alaskan oil development is inherently expensive. The remoteness of the fields, the high transportation costs and the fact that the oil can only be sold to in the U.S. market, makes oil production here more costly than in other oil provinces.

If we are to attract more investment in the state, particularly in the development of marginal fields, we have to find a way of reducing those costs even further. I submit that it's time for the state to begin acting as a participating partner in this effort, rather than as a dissatisfied spectator. House Bill 207, as passed by the House, helps accomplish this. It helps clarify the law that allows the state to reduce royalties on marginal fields to help spur their development. Otherwise, this oil may never come to market--and Alaska could lose the chance at any royalties at all.

The Committee substitute before you today does not accomplish this. It drags out the royalty adjustment decision process and has the real potential of introducing political wrangling into what should be a strictly economic decision. Furthermore, adoption of this substitute could set the stage for preventing any legislation from being passed this session. And that, in turn, could spell disaster for investments decisions due to be made during the coming year.

On behalf of my 200 employees and their families, I strongly urge you to adopt the version of the bill the House of Representatives passed. Give the state the ability to make a timely decision on these royalty adjustment applications. And help Alaska truly become a partner in the development of its resources.

I thank the committee for its time and I would be happy to answer any questions.

Union Oil Company of California
Testimony on CS HB 207
Senate Resources Committee
April 28, 1995

Mr. Chairman and members of the Resources 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 CSHB 207. I would like to begin my testimony by saying that the Sectional Analysis provided after the April 26, 1995 Hearing was particularly helpful in making a more informed analysis of the Bill. Some of the concerns I expressed in Wednesday's Hearing have been clarified by the Analysis and therefore the enclosed testimony more accurately reflects Unocal's view and opinion of the Bill.

Subsection (j)(1)

From purely a Unocal perspective, based on its present acreage position, Unocal is not directly impacted by paragraph (A). Most of the Unocal leases held today are located within producing fields, some of which are nearing the end of their economic viability. We have however, testified in earlier hearings on this Bill that we have not endorsed the concept of Sunset Provisions.

Subsection (j)(3)

Paragraph (B) appears to be a reopener. As long as it is clear the conditions of any future adjustments are determined at the time of royalty reduction and not intended to be a unilateral determination on the part of the Commissioner, we don't have an objection. I believe the wording should be changed to make this point absolutely clear.

Subsection (j)(4)

We believe the requirement for legislative approval under paragraph (A) will be a time consuming and unnecessary requirement resulting in an administratively burdensome process. Under the House Finance version of the Bill, adequate Commissioner oversight is provided under Subsection (j)(8).

In reading the provisions of paragraph (B) of this Subsection, it is unclear to me as to the intent of the language "in amount or value of the Production". If this is to mean a net 3% floor or a maximum 76% reduction of the current royalty rate, than Unocal is opposed to this revision. Under the House Finance version of the Bill, the floor established for producing and shut-in fields is 90%. There needs to be clarification on this point. Any increase in the floor reducing flexibility would be inconsistent with our position and prior testimony.

Subsection (j)(5)

The assignment of all right, title and interest in a lease is a fundamental principle in the oil industry. Property trades will be greatly restricted if assignability of a royalty adjustment is not allowed. The ability and desire to acquire a lease that has favorable royalty terms may be the catalyst and incentive for a company to invest capital and employ new ideas in fields where the current owners may be less inclined. Companies are rationalizing properties and focusing investments in core areas to take advantage of their particular operational, infrastructure or informational strengths. Lost opportunity for earlier development of a lease or field is sure to occur if this limitation is imposed. The intent of this legislation should be to create opportunity with certainty, not further limit the creativity of the industry.

Subsection (j)(7)

This issue was thoroughly discussed in prior hearings with what we thought was an equitable compromise and consensus opinion of the parties testifying. We see no advantage to changing this Subsection and would prefer to see Subsection (6) of the House Finance version reinstated.

Subsection (j)(8)

Thirty (30) days rather than sixty (60) says is an appropriate time period for public comment. The whole review process needs to be streamlined wherever possible.

Subsection (j)(9)

Reviewing and addressing all the requirements under this Subsection will be very expensive, time consuming and may not be applicable in all circumstances. We believe the Commissioner should have the discretion to provide for the contents of the best interests finding and determination. The Department of Natural Resources is well equipped for this process. We feel it is unecessary for this Subsection to be in the Bill, and in fact, the degree to which each of these conditions are to be investigated will be the subject of much debate. If the committee and legislature feel the need to include the details of the finding and determination in this Bill, then paragraphs (A) through (G) should only be suggestions of issues the Commissioner may consider in a royalty adjustment application.

Subsection (j)(12)

We have a similar comment in this Subsection as in Subsection (j)(4) in that legislative approval is unnecessary and administratively burdensome. We contend that Subsection (j)(10) of the House Finance Bill is more appropriate and should replace this Subsection.

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

Thank You

★ 1975 *Serving Alaska for 20 years* 1995 ★

Resource Development Council for Alaska, Inc.

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

Testimony of Resource Development Council
on CS HB 207
An Act relating to the reduction of royalties reserved to the state to encourage production of oil and gas from marginal fields
Senate Resources Committee
April 28, 1995

Good afternoon. My name is Becky Gay, Executive Director of the Resource Development Council for Alaska, Inc. On behalf of RDC, thank you for the opportunity to testify on CS for HB 207.

RDC strongly supports HB 207, as passed by the House in an overwhelming 35-2 margin. The House version of this legislation provides the flexibility needed for the State and industry to work together to change the economic equation for marginal fields. It provides flexibility for working with investors on a case-by-case basis to overcome Alaska's unique challenges and make new development and production a reality. Alaskans will benefit from new jobs, long-term revenues and increased economic activity associated with the development of new fields.

HB 207 is a tool the State can use to enhance the competitiveness of projects whose funding might otherwise go abroad. It sends a clear signal that Alaska aims to be competitive in the world market to attract the investments necessary to develop its oil and gas potential.

This clear signal, however, could become blurred due to recent amendments to the bill. RDC does not support the two sunset provisions nor the requirement of legislative approval on royalty reductions exceeding five million dollars or 50% of the royalty originally specified in the lease. RDC believes these new amendments to the bill are counterproductive and undermine the original purpose of changing state law on royalties. Alaska could be left with a bill of good intentions, but one that, in reality, falls short of what's needed. The amendments unfortunately will give way to **more** needless delays and **more** uncertainty. The 1998 deadline for royalty adjustments puts us back to square one as far as future discoveries are concerned. Ending the royalty adjustment itself in 2002 could hit some fields just when they need royalty relief the most.

HB 207, as passed by the House, is a good piece of legislation which should **not** be changed significantly. It **will** help to open up

marginal fields to development. And it does protect the State's best interests if a marginal field turns out to be more profitable than anticipated.

Please do not compromise the effectiveness of this bill and its ability to change the economic equation for marginal fields. Lets send a CLEAR, CLEAR message that Alaska will take the necessary steps to attract new investments, revenues and jobs.

RDC looks forward to working with the Senate toward final passage of a **strong** and **effective** royalty adjustment bill -- one that will serve as a powerful strategy to overcome roadblocks and make Alaska more competitive in the world market so that more dollars are invested here.

Thank you.

DRAFT

Testimony

by

Eric M. Luttrell

on behalf of

BP Exploration (Alaska) Inc.

to the Senate Resources Committee

on

HB207

April 28, 1995

DRAFT

Mr. Chairman, Members of the Committee, good afternoon. My name is Eric Luttrell, and I am Vice President of Exploration and New Developments for BP Exploration (Alaska) Inc. Thank you for this opportunity to testify to the Committee today on behalf of BP.

I have come here today to testify in support of legislation that would encourage the development of marginal fields, fields like Badami and Northstar, fields of moderate size away from existing infrastructure. Many of these prospects would not have been considered for development only a few years ago. Because the development of these fields within BP is directly under my control, I have taken a special interest in this legislation.

In particular, I would like to talk to you about the version of this bill that passed the House and the differences between that version and the draft Senate Resources Committee Substitute that we received two days ago. We have a number of concerns with the proposed language of the Senate bill, but I only want to address a few of the main ones here today.

Let me begin by briefly reviewing the context for this legislation. In looking at our business in Alaska and our opportunities to develop the business and make it grow, we in BPX Alaska see a number of situations in which the State's present royalty terms may impair our ability to compete within the BP Group for the capital funds to make the investments needed to keep our business sound and healthy for the future. Although BP is a large corporation, it still has only a limited amount of money available each year for capital investments worldwide. Naturally, in allocating these capital funds, priority is given to those investments that are most attractive. So if BP's capital funds are all allocated to more attractive investment opportunities elsewhere before we get down to our Alaskan projects, then the Alaskan projects simply don't get funded even though they may still be quite attractive and feasible economically on their own terms.

This is a fact of life for us, and in this, BP is no different from any of the other oil companies still active in Alaska. The state and those of us who work for BP in Alaska are engaged in a global competition for investment dollars. It is, of course, of great personal concern to those of us working here, because in large part our jobs here are on the line if we don't compete successfully. It is also of concern to us as Alaskans, because the continued oil and gas development of this state is essential for its future economic well-being. So it is extremely important that whatever

"economic feasibility" test that is applied to an application for royalty adjustment recognize this global competition.

The House-passed version of HB 207 would give the Commissioner of Natural Resources clear authority to modify the terms of the State's oil and gas royalties in a variety of ways in order to facilitate and encourage the new investments that need to be made in order to bring marginal new fields into production and to sustain production from existing fields that are in decline. At the same time, it contains safeguards to protect the State's best interests. By protecting those interests while allowing our Alaskan opportunities to be made more competitive against the opportunities elsewhere, the House version embodies a win-win approach for the State and its oil industry. It is a good bill, and BP fully supports it.

Unfortunately, the same cannot be said of the draft Senate Resources Committee Substitute for the bill. It is badly flawed, and seriously out of touch with the realities of a mature oil industry in Alaska.

Problem number one is the requirement that any royalty adjustment be approved by the legislature. This, combined with the extensive findings that the Commissioner must make, is an invitation for long delays in final approval and most probably, litigation. It is entirely possible that it would be two years before an applicant would know whether a project would have a revised royalty arrangement. This process will also compromise any ability to keep sensitive proprietary information confidential. All of this adds up to additional uncertainty and, in our view, makes this proposal unworkable. We recognize the importance of appropriate oversight, but we need to devise something that would not unduly burden the State's and industry's ability to get these marginal projects developed. We think the oversight provisions in the existing HB 207 would be effective.

There is another point that is relevant to the whole question of oversight of the Commissioner's decisions, and that comes in the form of a question: What incentive does BP have to make a deal that is not in the best interest of the State? We will be doing business in Alaska for a long time. Since the nature of the deal will be examined many times after it is made, any undue advantage that we may have gained will become readily apparent. We would fully expect the State to try to recover that advantage in some other way, e.g. increased taxation. In short, it is not in BP's, or any other company's long term interest to make a deal that is bad for the State.

My second major concern is that of encouraging development of new pools within existing fields. Here again, the Senate version could have the effect of discouraging investment and development by carefully removing the words "pool, or portion of a field or pool" everywhere they occur in the House version, leaving only references to "field."

This reflects a fundamental misunderstanding about how investment decisions are made. Fields are not economic monoliths, nor do we view them that way. Each new investment in a field has to be justified at the margin, on its own merits. The profitability (or economic failure, for that matter) of prior investments in a field has no bearing on the decision to make the new investment or not. The plain truth is that there are investment opportunities that are truly marginal in all fields. In terms of competing for limited capital funds, it is just as important to recognize this fact for opportunities in large fields as it is to recognize it in the context of little fields.

A third problem with the draft Committee Substitute is that any royalty adjustment for a new, marginal field automatically terminates on December 31, 2002. How does this benefit the State? Limiting the time when a royalty modification can be in effect, whether it applies to some fields or to all, makes little sense — especially if the modification is a restructuring instead of an outright reduction. Our concept is to share risk with the State, a concept that makes an arbitrary cut-off of the deal potentially contrary to the State's best interest.

For similar reasons we do not understand what the State gains by providing that all of the provisions of this bill terminate at the end of 1998. As a practical matter, if future legislatures and administrations believe that this bill is not in the best interest of the State, it will be repealed. In this sense, the bill and all of the royalty adjustments that are made under its authority will be constantly under review. Nevertheless, if the Committee would be more comfortable with a sunset provision, it should allow a reasonable period for this set of proposals to work. We believe this is a minimum of five years.

The fourth problem with the Committee Substitute is that it requires the Commissioner to include as a condition of a royalty modification the power to "restore or increase the state's royalty share if the assumptions upon which the agreement is based ... are subsequently determined to be in error..." This assumes that all errors are made against the state's interest, which is simply not the way things happen. Our intent is to deal with unknown factors during the course of negotiations with the

Commissioner. This unilateral authority to change the agreement inserts another element of uncertainty into the development decision. The negotiation will cover the relationship of royalty rate to price. We would also expect the negotiation to deal with anticipated recoverable reserves, [well productivity?], and the like. The nature of the negotiation process, combined with an appropriate level of oversight, renders such drastic unilateral powers unnecessary.

What is at stake in the near term? We believe that effective legislation can have a big impact on our decision to develop Badami, and on our decision to develop Northstar. We expect that both of these decisions could be made in the next year and lead to significant production and revenue by 1998.

Badami: I will tell you candidly, I don't know whether we would request royalty adjustment for Badami. That request awaits complete review of our drilling results and the engineering cost estimates. I can tell you that we have a group of experts working diligently on both issues to get us answers to these questions by mid-summer. Then we will run the economic analyses and take a decision to make a request to DNR if we believe the field is developable but marginally economic under low price conditions. And if enabling legislation passes this year.

That is a lot of ifs in a row, but that is the nature of our decision at this time. If we defer the decision to develop out of 1995, we, and the State will lose the opportunity to start production and revenues in 1997. We both loose; Production and Revenue... I fail to see how deferral is in the best interest of either of us.

Northstar: Simply stated, development of Northstar in the foreseeable future requires passage of legislation including net profit share adjustments as a part of the negotiation with the State. We had hoped that we would be talking with the Senate about extending the terms of the House bill to net profit share leases. Now, we are in doubt as to whether there will be a royalty adjustment bill that has any practical effect. This means that we are two steps away from any plan to develop this significant prospect. Pretty strong words, but I could not recommend to BPX proceeding with Northstar development without a change in the NPSL terms.

We have been very open with the DNR on Northstar and have even proposed some possible agreements that would protect the interests of both the State and BP. But they require legislation. With legislation, we

believe we would be negotiating with the State before year end. Delay of legislation or failure to include NPSI would defer the development of Northstar by 1-2 years and, because of that , delay production and revenue from Northstar by 1-2 years. I fail to see how that is in the best interest of the State.

Are there other marginal accumulations on the North Slope that could be developed in the near term? Absolutely. Will their development be encouraged by this legislation? I don't know, they are not mature enough for us to have a clear view of their economic value. I certainly do not expect that all will.

What is in it for the State of Alaska? The State of Alaska stands to benefit greatly from these developments, and from their timely development. At Badami, we project State revenues (using current State price forecasts) of upwards of $350 mm (royalty, severance, ad valorem, income taxes), plus jobs and the infusion of several hundreds of millions of dollars of additional investment during development. Investment in and revenues from Northstar are similar.

When we look beyond the specifics for Badami and Northstar, the proposed legislation has the potential of sending a strong message to the Industry, to Houston, to Los Angeles and to London, a message that Alaska wants to work cooperatively with Industry to encourage investment and new development; that Alaska wants to compete. Not passing legislation this year or passing the wrong legislation will send the opposite message. We believe that this bill is both necessary and beneficial to the state and to industry, but it must be in a useful format. The House version was carefully considered and would work. The Senate version would not work.

I have tried to be open, direct and candid with you here today, just as we would be with the State in a negotiation. Those of you who know me, know that is my style and it is BP's style. Like it or not, the State and the industry have much to gain by improved openness and cooperation and we look forward to a long and mutually beneficial relationship.

Thank you for the opportunity to testify.

DRAFT

PROBLEMS WITH
THE DRAFT SENATE RESOURCES CS
FOR HOUSE BILL NO. 207

Supplement to Testimony by
Eric M. Luttrell on behalf of
BP Exploration (Alaska) Inc.
to the Senate Resources Committee

April 28, 1995

Page 2, lines 1-2: We don't believe there is any good reason to have a sunset date for the Commissioner's authority to enter into agreements to modify royalties for new fields that aren't yet in production. As new fields continue to be discovered (hopefully), some of them may well be suitable for modification of their royalty terms. There is no guarantee these new fields will all be discovered by any given sunset date, and particularly by January 31, 1998. At the very least, the sunset should be far enough in the future to give the new program a reasonable time to work — at least five years. But BP believes the best way to deal with this royalty-modification program if there are problems with it in the future, is to amend the law or even repeal it if necessary, instead of using a sunset clause.

Page 2, line 2 (and everywhere else where the phrase "pool, or portion of a field or pool" appears in the House version and is deleted in the draft Senate CS): the Senate version could have the effect of discouraging investment and development by carefully removing the words "pool, or portion of a field or pool" everywhere they occur in the House version, leaving only references to "field."

This reflects a fundamental misunderstanding about how investment decisions are made. Fields are not economic monoliths, nor do we view them that way. Each new investment in a field has to be justified at the margin, on its own merits. The profitability (or economic failure, for that matter) of prior investments in a field has no bearing on the decision to make the new investment or not. The plain truth is that there are investment opportunities that are truly marginal in all fields. In terms of competing for limited capital funds, it is just as important to recognize this fact for opportunities in large fields as it is to recognize it in the context of little fields. Deletion of the words "pool, or portion of a field or pool" reflects a naïve but fundamental misunderstanding of the real world and how our investment decisions are made. They should be restored.

Page 2, lines 10-12: In the draft CS royalty modification for a field in decline will be forbidden until the field is actually losing money. Well before that time, investments to slow down the decline would have to be made, but nothing could be done then to modify the royalty. In other words, any help for declining fields would be too little and too late to help the investment decisions that would slow the decline. The House version does not make this mistake.

Page 2, lines 27-32: These provisions do not reflect enough attention to the restructuring of royalty obligations. Restructuring does not necessarily mean reduction. For example, a fixed royalty could be converted into a sliding-scale royalty rate based on price levels. Such a sliding scale could be designed so that the State's royalty is the same overall if prices follow the State's mid-case price scenario in its revenue forecast. That's not a reduction, it's a sharing of price risk. But it is one that greatly helps the competitive attractiveness of a prospect in Alaska, where high transportation costs give us a unique degree of vulnerability to low prices. A price-based sliding-scale royalty would afford relief just when we need it most, and thus improves the attractiveness of an Alaskan investment by reducing its economic risk.

Moreover, since the application to modify a royalty is filed before the investments are made and before anyone knows how well the investments will actually perform, errors in the assumptions about how they will work can run both ways — not just against the State as the draft CS seems to fear. The House version is more even-handed in its treatment of changes from what either side expected. Thus, the language in lines 27-32 on page 2 of the draft CS should be replaced

with the language in the House version, starting with "provide for" in line 26 on page 2 of CSHB 207(FIN)am and running through the end of line 32 on that page.

Page 3, lines 1-21: BP recognizes the need for appropriate oversight of the royalty restructuring program. The House passed version of HB207 has three types of oversight. First, there is a thirty day public comment period. Secondly, the legislators are given formal notice of the preliminary findings on the first day of public comment period allowing them time to become involved if they decide it necessary. Third, the commissioner of Natural Resources must offer to make a presentation to LB&A regarding the preliminary findings and determination and the administrative process.

The legislators will clearly be aware of any royalty modification agreement and will be able to receive input from their constituencies and apply pressure to the commissioner as they see appropriate. The risk of an unacceptable deal going forward would be minimal. Provisions elsewhere in the draft CS provide for timely review by the Legislative Budget and Audit Committee before the Commissioner makes a final decision on a royalty modification request. That is the right time and the right way for the Legislature to make known to the Commissioner any reservations it may have about the deal. The requirement of obtaining legislative approval will cause excessive and needless delay and uncertainty in concluding royalty agreements. If such an agreement were reached in principle just after the Legislature adjourned, it could not be finalized until it is approved in the next Session, which would be at least eight months later and perhaps almost twelve. For these reasons BP believes lines 1-21 on page 3 of the draft CS should simply be deleted.

Page 3, lines 12-17: The draft committee substitute automatically terminates any royalty adjustment for new marginal fields on December 31, 2002. How does this benefit the State? Why should royalty agreements for new fields expire after 2002 while identical agreements that might be made for fields in decline or for shut-in fields would have no expiration date? Limiting the time when a royalty modification can be in effect, whether it applies to some fields or to all, makes little sense — especially if the modification is a restructuring instead of an outright reduction.

Page 3, lines 22-23: This is a new provision, forbidding any assignment of a royalty agreement from one lessee to a potential new lessee. The Sectional Analysis for the draft CS does not explain

why the State should be concerned about this, nor can BP figure out what the state interest is that needs to be protected this way. Rather, we see a good reason not to ban such assignments: Banning them would make it more difficult to take in new partners to share the risk in a new development, and that could keep new developments from happening. In any event, BP sees no reason why the State's interest — whatever it may be — would not be fully protected by requiring any assignment to be reviewed and approved by the Commissioner before it can be made, instead of banning them altogether. So, either these lines should be deleted, or the words "without the commissioner's prior approval" should be inserted after the word "assignable" and before the semicolon at the end of line 23.

Page 3, lines 27-31: This subparagraph (A) conflicts with subparagraph (B) that immediately follows. (A) says financial and technical data must be disclosed to the extent the Commissioner determines them to be relevant to the decision to enter a royalty modification agreement. But (B) says that information must be kept confidential under AS 38.05.035(a)(9) upon the lessee's request. It can't be both. Either the information will be kept confidential, or it won't. Given that the Legislative Budget and Audit Committee can review a deal before it is consummated — including the confidential information in an executive session — BP believes there will be adequate oversight of the process in a timely fashion, without forcing lessees to choose between seeking a royalty modification and giving up proprietary and confidential information in order to do so. Thus, we recommend deletion of lines 27-31 in their entirety and of the "(B)" in line 32 on page 3 of the draft CS.

Page 4, lines 4-8: This material relates to the independent contractor who is to advise the Commissioner at the lessee's expense in reviewing the lessee's application for a royalty modification. The draft CS deletes a provision in the House version allowing the lessee to choose the contractor from a list of three offered by the Commissioner. That provision strikes a reasonable balance to keep either party from trying to get an undue advantage over the other through the selection of this independent advisor. The draft CS also deletes a provision in the House version making clear that the Commissioner, not the lessee, controls the scope of work of the advisor. This provision, too, is needed to keep balance as the advisor works for the Commissioner. Accordingly, BP believes this material in the draft CS should be replaced with the material appearing in lines 16-22 on page 3 of CSHB 207(FIN)am.

Page 4, line 12: The 60-day period for public comment adds an element of delay in the process. Thirty days is sufficient — after all, the required public comment period for the very regulations to implement this legislation is only 30 days.

Page 4, line 14 to p. 5, line 1: These highly detailed "best interest" findings are a laundry list of litigation issues to challenge a Commissioner's decision to modify a royalty. Some of them — such as "the projected social effects of the proposed royalty adjustment" or "the projected effects of the proposed royalty adjustment upon existing or potential new commercial enterprise, competition, and patterns of investments within the state" — would require extensive speculation and conjecture by the Commissioner in order to address them. The Commissioner's decision should be made on the basis of facts as they are known at the time, not on wild conjecture or speculation of only marginal relevance. Moreover, to the extent any of these factors would be material to the Commissioner's decision, they would be addressed anyway by the Commissioner in the course of explaining the basis for that decision. These provisions should therefore be deleted as unnecessary and potentially harmful to the program.

Page 5, line 4: The words "to protect confidential information" should be inserted immediately after the word "appropriate" at the beginning of the line.

Page 5, lines 27-28: The "(A)" at the beginning of line 27 and the phrase "that does not, under (4)(A)(i) of this subsection, require legislative approval," should all be deleted at the same time as the rest of the provisions relating to legislative veto are deleted.

Page 6, lines 2-3: By making the Commissioner's decision final only as to the applicant, the draft CS creates a strong presumption that everybody else may sue to challenge that decision. The whole purpose in making the decision final is to cut down on litigation. This, instead, would invite it. Therefore, the phrase ", as to the royalty adjustment applicant," should be deleted.

Page 6, lines 4-24: All of subparagraph (B) should be deleted as part of the general deletion of provisions relating to legislative veto, and the remaining subparagraphs should be redesignated accordingly. In addition, the phrase "or (B)" on line 18 should be deleted because it refers to the subparagraph to be deleted .

Official Business

COMMITTEE: S. Resources

DATE: 4/22/95

SIGN-IN

Subject of meeting: HB 207 Adjustments to Oil & Gas Royalties

PLEASE PRINT!

NAME	ADDRESS (MAILING) & (ZIP)	PHONE	REPRESENTING	DO YOU WANT TO TESTIFY?
Paul Wessells	P.O. Box 196612 Anchorage 995	564-4039	BP Exploration	Yes
John Shively	400 W. Willoughby Juneau	465 2400	DNR	Yes

1. Procedures for Royalty Relief Should Be Clearly Framed and the Need for Royalty Relief Should Be Clear to the Owners of the Resource. *(CSHB 207[Fin]Am page 1, line 10)* Particularly in view of the production trends discussed above and the fact that industry statements about profitability fly in the face of every published report of which I am aware,[6] the process, the criteria and the case for royalty relief should be clearly defined and the case should be part of the public record. This bill does the opposite. For example, where the existing statute requires regulations to make procedures clear, this bill removes that requirement.

2. Economic Considerations Should Include Analysis of Pipeline Profits. *(CSHB 207[FIN]Am page 2, line 31 - Page 3, line 1)* This bill mandates consideration of factors such as capital investment but may be read to exclude investment in pipelines. As mentioned above, pipeline costs can be a major factor affecting the development of new fields and the continued production in existing fields. Moreover, guaranteed profits to the pipeline owners are a significant factor influencing production decisions that this language arguably requires the Commissioner to ignore. You may choose to ignore this important aspect of North Slope production economics; prospective producers will not. And you can bet needless litigation fees that the state will have to spend a bunch to counter industry lawyers who are certain to argue that the Legislature, by its exclusion of pipeline profits from its list, intended to exclude this factor.

3. Blanket Confidentiality. *(CSHB 207[[FIN]Am page 3, lines 15-16.)* The requirement that the Commissioner shall hold application material confidential at industry request contravenes the state's sunshine laws, common sense and jurisprudence. The Alaska judge who has probably reviewed more oil industry documents than any other has thrice ruled against blanket grants of confidentiality

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[6] See: Deakin (1989), Oil Industry Profitability in Alaska, 1969 through 1987, p.2 (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, 1985 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 per barrel [excludes estimated TAPS industry profits of $1.00 per barrel v. state taxes of approximately $0.30 per barrel]).

END

FAX TO: ANNETTE KREITZER
c/o SEN. LOREN LEMAN

FAX #: 465-3810

DATE: 4/23/95

PAGES: 2 (including this sheet)

From: R.A. Fineberg
907 / 479-7778

Re: HB 207

If my testimony has not yet gone to all members and time permits, please substitute the corrected page 4, enclosed (correcting last sentence of the paragraph preceding "3. Blanket Confidentiality. . . ."

If testimony is already distributed, kindly add make this correcting note to your committee file for the record.

TNX!

END

Testimony to the Senate Resources Committee on CSHB 207(FIN)Am

Richard A. Fineberg
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April 21, 1995

A. Data in the State's New Revenue Forecast Demonstrate the North Slope Has Generated and Is Generating the Equivalent of Current TAPS Throughput in Increased Production Every Day.

A substantive case for royalty relief has not been made. To the contrary, new evidence seems to point in the opposite direction. Data in the Department of Revenue's spring revenue forecast released last week greatly strengthen the argument that royalty relief may not be necessary.

1. Over the past decade, the state's North Slope production forecast for 1995-2010 has more than tripled. When forecast production is combined with increases in actual production between 1985 and 1995, by 2010 the North Slope is now expected to generate 6.2 **billion** more barrels of oil than the Department of Revenue forecasted for the 1986-2010 period in 1985. That's more than ten years of additional North Slope production at current levels. Put otherwise: Each and every day over the last ten years, the current tax and royalty regime has generated one day more of production at 1.6 million barrels of oil per day than was forecasted in 1985. This trend of increasing production (i.e., slowed decline in production) was established in the face of declining prices, contradicting the dire warnings of industry and government studies in the late 1980's that said Alaska had seen the end of such increases.[1] This trend was established without royalty relief. This trend continues today: The new state forecast increases production for the 1995-2010 period by 750 million barrels over the previous semi-annual state forecast, issued last fall. That's more than 2.0 million barrels per day for an entire year. On this basis, it seems reasonable to demand that a strong, substantive case for easing the state's existing royalty relief provisions, as proposed in HB 207, must be made before this bill is enacted.

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[1] See attached tables 1 through 4 (see also and graphs V-1 through V-4 summarizing Dept. of Natural Resources forecasts in 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. Marginal Fields. In the new forecast, production from undeveloped fields between 1995 and 2010 increased by 18%, despite a reduction in production from the North Star prospect. Two factors here are worth noting. It is my understanding that in the new Department of Revenue forecast, North Star was delayed in part to higher TAPS tariffs. Could more effective management of pipeline tariffs be an important factor in encouraging or stifling future production? Second, undeveloped fields account for approximately three percent of total forecast production; even with a tripling from the current levels, non-producing fields would comprise less than ten percent of total forecasted production.

3. 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] This dialogue is weirdly bereft of facts. Alaska's interaction with its meal-ticket and 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 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 big, front-page presentation in the Anchorage Daily News last spring, one of many on the hard times theme. That one had a color graph 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 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, North Slope profitability is apparently sufficient to induce the consistent production increases (i.e., slowed decline) identified above. But the public dialogue in

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

[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.)

this area is blunted because North Slope producers steadfastly refuse to disclose information that would justify its position.[4]

B. HB 207 contains serious structural defects

I believe it is unwise to grant royalty reduction without providing for clear and unambiguous clarification on the public record of the necessity for that assistance. Instead, CSHB 207 (FIN)Am deliberately shields the actions of the Commissioner of Natural Resources from the public review that normally safeguards the public interest provisions giving the Commissioner of Natural Resources new powers to grant royalty relief that are ill-conceived and unprecedented. It has been clearly and convincingly documented in other North Slope revenue disputes that public policy evils flourish where confidentiality erodes the checks and balances and balances that normally protect the public interest and keep the public process on a steady course.[5]

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[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 has 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 correspondence; in 1992 and again in 1993, the importance of BP's refusal to provide clear public data on its North Slope operations were clearly delineated for the Legislature in my 1992 report, North Slope Profits and Production Prospects [prepared under contract to the Senate Finance Committee], Nov. 12, 1992, and by the Legislative Research Agency, Distribution of Income from Alaska Oil and Gas Operations . . . [Report No. 93.001], Sept. 15, 1993.)

[5] 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 games that take 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.

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on industry request. In view of the clearly established right of the public to know what its officials are doing, he said, the industry should make a showing that it is necessary to hold documents confidential.[7] As recently as 1990, after careful review in three committees and despite strong industry opposition, the Alaska State House voted unanimously to prohibit oil and gas settlements from extending confidentiality beyond that already required by law.[8] This bill reverses both precedents.

4. Contractor Analysis. *(CSHB 207[[FIN]Am page 3, lines 17-21)*
Apparently throwing in the towel on a 20-year endeavor to establish and maintain expertise within the state system to protect the public interest in the inevitable dialogue with industry, this bill sets up an unprecedented system in which the Commissioner will rely instead on a contractor to the industry.

5. Review. *(CSHB 207[FIN]Am page 3, line 24 through page 5, line 2)*
The public review contemplated by the latest version of HB 207, although much improved, is seriously flawed in two respects — first, by the unprecedented grant of blanket confidentiality, discussed above, and secondly, by excessive reliance on Legislative review. With all respect, that route is notoriously ineffective. Let me tell you about one confidential oil and gas briefing in which I participated in this very committee room (or the one next door) several years back. Two legislators — the most senior member of the Legislature and a member of this present body — refused to participate because they could not accept the confidentiality requirements imposed by the administration. The briefing continued behind closed doors; I watched as the Legislature was misinformed on issues I considered important. I was ordered silent by my bosses. When a clever response to a misdirected question pulled the legislators off track, I could have spoken out; to do so would have meant

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[7] The court specifically refused to hold material confidential merely at the request of the industry, without a showing for the need for confidentiality, 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. "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 judge reaffirmed that order last month. "Order [Denying Motions to File Documents Under Seal]", ANS Royalty Litigation, 1JU-77-847 Civil, March 20, 1995.

[8] HB 541, 1990. Several members of this body, then in the House, voted for the provision limiting settlement confidentiality.

giving up my job — and with it, the ability to directly influence other important executive decisions then pending.[9]

6. Judicial Review. *(CSHB 207[FIN], Page 4, line s 24-25)* It's easy to see why the industry would like to remove judicial review; in view of the long history of increased revenues the state has obtained through the courts, one wonders why the stewards of public resources would recommend this course of action.

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. 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 startling 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.[10]

To summarize: Even if the defects discussed above were corrected, the case for the proposed incentives would have yet to be made. This concludes my testimony; I would be happy to answer any questions you may have, and I thank you for the opportunity to testify.

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[9] While I customarily provide footnotes and documentation, I must ask you to accept this general description because I am constrained by confidentiality requirements from identifying the event. Were the briefing identified, you would find no committee tape or substantive record of the meeting — again due to confidentiality requirements.

[10] 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 the Governor's well-intentioned desire to reduce litigation, the Legislature might consider introducing legislation that puts more information on the public record — not less.

Table 1 Richard A. Fineberg (4/13/95)

1985, 1990 and 1995 ADOR Production Forecasts thru 2010

Forecast:	(1) DOR 1985 (Spring)	(2) DOR 1990 (Spring)	(3) U.S. DOE* (Fall 1990)	(4) DOR 1994 (Fall)	(5) 1995 DOR (Spring)	(6) CERA 1995 (March)
Years	/= = = = = = = = = 000 Barrels Per Day = = = = = = = = = = = = /					
	Forecast:				*Actual:*	
1986	1,730				*1,800*	
1987	1,760				*1,850*	
1988	1,640				*2,010*	
1989	1,560	*Forecast:*	*Forecast:*		*1,960*	
1990	1,450	1,830	1,806		*1,850*	
1991	1,340	1,710	1,770		*1,800*	
1992	1,240	1,570	1,640		*1,790*	
1993	1,160	1,480	1,628		*1,700*	
1994	1,030	1,420	1,625		*1,610*	*Calendar Yr.*
				Forecast:	*Forecast:*	*Forecast:*
1995	910	1,310	1,590	1,641	1,573	1,710
1996	800	1,200	1,503	1,595	1,503	
1997	710	1,080	1,440	1,489	1,457	1,530
1998	630	1,000	1,323	1,408	1,418	
1999	540	920	1,238	1,366	1,375	
2000	470	900	1,113	1,291	1,342	1,350
2001	380	830	1,022	1,213	1,30[illegible]	
2002	310	760	928	1,146	1,246	
2003	250	690	839	1,036	1,195	
2004	200	650	757	934	1,145	
2005	160	590	652	842	1,103	1,730
2006	130	580	582	784	1,037	
2007	110	520	523	729	974	
2008	90	470	455	677	965	
2009	70	430	405	624	904	
2010	60	380	375	583	843	1,640

	/= = = = = 000 Barrels Total Production (000 BPD x 365) = = = = = /					
1995-2010 ==>	2,124,300	4,493,150	5,381,483	6,335,670	7,075,525	*Forecast*
1986-94 ==>	*4,712,150*	*n.a.*	*n.a.*	*n.a.*	*5,975,050*	*Actual*

* U.S. Dept. of Energy 1990 forecast (Col. [3]) was more optimistic than the contemporary state forecast; five years later, the DOE forecast appears to have been rather conservative.

Table 2

Spring 1990 Production Forecast for 1995-2010 (Alaska Dept. of Revenue)
(000 bbls)

000 Barrels per day:

Year	*Field =>*	Prudhoe*	Kuparuk	Lisburne	Pt. McIntyre	Endicott	Milne Pt.	Niakuk	W. Sak	Other**	Total	
1995		920	160	30	60	70	20	30	20		1,300	*000 bpd*
1996		840	140	30	60	70	20	20	20		1,200	"
1997		750	120	30	60	70	20	20	20		1,090	"
1998		690	100	30	60	70	10	20	40		1,020	"
1999		640	90	20	50	60	10	20	40	0	930	"
2000		570	70	20	50	50	10	20	60	50	900	"
2001		530	60	20	40	50	0	20	60	60	840	"
2002		460	50	20	40	40		20	80	60	770	"
2003		410	40	10	30	40		10	80	60	680	"
2004		370	40	10	30	30		10	110	50	650	"
2005		340	30	10	30	30		10	100	40	590	"
2006		300	30	10	30	30		10	150	30	590	"
2007		250	20	10	20	20		10	150	30	510	"
2008		210	20	10	20	20		10	150	30	470	"
2009		190	20	10	20	20		10	150	20	440	"
2010		160	10	10	20	10		0	140	20	370	"
Total Barrels:		2,784,950	365,000	102,200	226,300	248,200	32,850	80,950	500,050	164,250	4,507,750	(000 bbls)

* Includes all NGL's

** North Star

Source: Alaska Dept. of Revenue, "Revenue Sources Book: Forecast & Historical Data," Spring 1990, p. 47 ("Simulated Oil Production [Mid Case]")

Table 3 (Fall 1994)

Research Associates 4/95

Fall 1994 Production Forecast for 1995-2010 (Alaska Dept. of Revenue)

(000 bbls)

000 Barrels per day:

Year	*Field =>*	Prudhoe *	Kuparuk	Lisburne	Pt McIntyre	Endicott	Milne Pt.**	Nikaitchuq	W.Sak	Other***	Total	
1995		1,084	304	17	106	91	21	16			1,639	*000 bpd*
1996		1,057	292	15	101	80	27	24			1,596	"
1997		969	279	12	93	74	38	24			1,489	"
1998		926	251	11	86	67	39	21		6	1,407	"
1999		874	226	9	79	62	36	19		59	1,364	"
2000		827	204	8	73	58	36	18		68	1,292	"
2001		785	181	6	67	53	35	16		70	1,213	"
2002		753	161	5	62	48	32	14		71	1,146	"
2003		684	143	5	57	42	29	12		65	1,037	"
2004		622	128	4	52	38	25	10		56	935	"
2005		565	113	3	48	34	22	8		50	843	"
2006		536	101	3	44	30	19	7		45	785	"
2007		506	90	2	41	27	16	6		40	728	"
2008		479	80	2	37	24	14	5		35	676	"
2009		453	71	2	34	16	12	4		31	623	"
2010		431	63	1	31	15	11	4	0	28	584	"
Total Barrels:		4,216,115	980,755	38,325	369,015	277,035	150,380	75,920	0	227,760	6,335,305	*(000 bbls.)*

* Includes all NGLs, N Prudhoe, W Beach

** Includes Schrader Bluffs

*** North Star, Cascade

Source: Alaska Dept of Revenue, "Revenue Source Book: Forecast & Historical Data," Fall 1994, p. 43 ("Base Case Simulated Oil Production")