

ALASKA LEGISLATURE COMMITTEE FILES, 2003-2004 0072

10977 HOUSE RESOURCES

1 interest in land for oil and gas or for gas only under (5) of this subsection, the director
2 shall make available to the public a written finding that, in accordance with (1) of this
3 subsection, sets out the material facts and applicable statutes and regulations and any
4 other information required by statute or regulation to be considered upon which the
5 determination that the sale, lease, or other disposal will best serve the interests of the
6 state was based; however, a written finding is not required before the approval of

7 (A) a contract for a negotiated sale authorized under
8 AS 38.05.115;

9 (B) a lease of land for a shore fishery site under AS 38.05.082;

10 (C) a permit or other authorization revocable by the
11 commissioner;

12 (D) a mineral claim located under AS 38.05.195;

13 (E) a mineral lease issued under AS 38.05.205;

14 (F) an exempt oil and gas lease sale or gas only lease sale
15 under AS 38.05.180(d) of acreage subject to a best interest finding issued
16 within the previous 10 years or a reoffer oil and gas lease sale or gas only
17 lease sale under AS 38.05.180(w) of acreage subject to a best interest finding
18 issued within the previous 10 years, unless the commissioner determines that
19 substantial new information has become available that justifies a supplement to
20 the most recent best interest finding for the exempt oil and gas lease sale or
21 gas only lease sale acreage and for the reoffer oil and gas lease sale or gas
22 only lease sale acreage; however, for each oil and gas lease sale or gas only
23 lease sale described in this subparagraph, the director shall call for comments
24 from the public; the director's call for public comments must provide
25 opportunity for public comment for a period of not less than 30 days; if the
26 director determines that a supplement to the most recent best interest finding
27 for the acreage is required under this subparagraph,

28 (i) the director shall issue the supplement to the best
29 interest finding not later than 90 days before the sale;

30 (ii) not later than 45 days before the sale, the director
31 shall issue a notice describing the interests to be offered, the location

1 and time of the sale, and the terms and conditions of the sale; and

2 (iii) the supplement has the status of a final written best
3 interest finding for purposes of (i) and (l) of this section;

4 (G) [A SHALLOW GAS LEASE AUTHORIZED UNDER
5 AS 38.05.177 IN AN AREA FOR WHICH LEASING IS AUTHORIZED
6 UNDER AS 38.05.177;

7 (H)] a surface use lease under AS 38.05.255;

8 (H) [(I)] a permit, right-of-way, or easement under
9 AS 38.05.850;

10 (7) the director shall include in

11 (A) a preliminary written finding, if required, a summary of
12 agency and public comments, if any, obtained as a result of contacts with other
13 agencies concerning a proposed disposal or as a result of informal efforts
14 undertaken by the department to solicit public response to a proposed disposal,
15 and the department's preliminary responses to those comments; and

16 (B) the final written finding a summary of agency and public
17 comments received and the department's responses to those comments.

18 * Sec. 11. AS 38.05.035(g) is amended to read:

19 (g) Notwithstanding (e)(1)(A) and (B) of this section, when the director
20 prepares a written finding required under (e) of this section for an oil and gas lease
21 sale or a gas only lease sale scheduled under AS 38.05.180, the director shall consider
22 and discuss

23 (1) in a preliminary or final written finding facts that are known to the
24 director at the time of preparation of the finding and that are

25 (A) material to issues that were raised during the period
26 allowed for receipt of public comment, whether or not material to a matter set
27 out in (B) of this paragraph, and within the scope of the administrative review
28 established by the director under (e)(1) of this section; or

29 (B) material to the following matters:

30 (i) property descriptions and locations;

31 (ii) the petroleum potential of the sale area, in general

- 1 terms;
- 2 (iii) fish and wildlife species and their habitats in the
- 3 area;
- 4 (iv) the current and projected uses in the area, including
- 5 uses and value of fish and wildlife;
- 6 (v) the governmental powers to regulate the [OIL AND
- 7 GAS] exploration, development, production, and transportation of oil
- 8 and gas or of gas only;
- 9 (vi) the reasonably foreseeable cumulative effects of
- 10 [OIL AND GAS] exploration, development, production, and
- 11 transportation for oil and gas or for gas only on the sale area,
- 12 including effects on subsistence uses, fish and wildlife habitat and
- 13 populations and their uses, and historic and cultural resources;
- 14 (vii) lease stipulations and mitigation measures,
- 15 including any measures to prevent and mitigate releases of oil and
- 16 hazardous substances, to be included in the leases, and a discussion of
- 17 the protections offered by these measures;
- 18 (viii) the method or methods most likely to be used to
- 19 transport oil or gas from the lease sale area, and the advantages,
- 20 disadvantages, and relative risks of each;
- 21 (ix) the reasonably foreseeable fiscal effects of the lease
- 22 sale and the subsequent activity on the state and affected municipalities
- 23 and communities, including the explicit and implicit subsidies
- 24 associated with the lease sale, if any;
- 25 (x) the reasonably foreseeable effects of [OIL AND
- 26 GAS] exploration, development, production, and transportation
- 27 involving oil and gas or gas only on municipalities and communities
- 28 within or adjacent to the lease sale area; and
- 29 (xi) the bidding method or methods adopted by the
- 30 commissioner under AS 38.05.180; and
- 31 (2) the basis for the director's preliminary or final finding, as

1 applicable, that, on balance, leasing the area would be in the state's best interest.

2 * Sec. 12. AS 38.05.036(a) is amended to read:

3 (a) The department may conduct audits regarding royalty and net profits under
4 oil and gas contracts, agreements, or leases under this chapter and regarding costs
5 related to [OIL AND GAS] exploration licenses entered into under AS 38.05.131 -
6 38.05.134 and exploration incentive credits under this chapter or under AS 41.09. For
7 purposes of audit under this section,

8 (1) the department may examine the books, papers, records, or
9 memoranda of a person regarding matters related to the audit; and

10 (2) the records and premises where a business is conducted shall be
11 open at all reasonable times for inspection by the department.

12 * Sec. 13. AS 38.05.127(e) is amended to read:

13 (e) The establishment of easements or rights-of-way for oil and gas, gas only,
14 and mineral leases under (a) of this section need not be made until the leases are ready
15 to be developed.

16 * Sec. 14. AS 38.05.131(a) is amended to read:

17 (a) Unless specifically provided otherwise in AS 38.05.132 - 38.05.134, the
18 provisions of AS 38.05.005 - 38.05.037, 38.05.140(f), 38.05.180, 38.05.182 -
19 38.05.184, and 38.05.920 - 38.05.990 apply to the issuance of [OIL AND GAS]
20 exploration licenses and leases for oil and gas, or for gas only, as appropriate,
21 under AS 38.05.132 - 38.05.134.

22 * Sec. 15. AS 38.05.132(a) is amended to read:

23 (a) To encourage exploration for oil and gas on state land, the commissioner
24 may issue [OIL AND GAS] exploration licenses. The commissioner may limit the
25 exploration licenses under AS 38.05.132 - 38.05.134 to exploration for and
26 recovery of gas only.

27 * Sec. 16. AS 38.05.132(b) is amended to read:

28 (b) An [OIL AND GAS] exploration license issued under this section gives
29 the licensee

30 (1) the exclusive right to explore, for a term not to exceed 10 years,
31 [FOR DEPOSITS OF OIL AND GAS] on unleased state land described in the

1 exploration license for deposits of oil and gas, or for deposits of gas only, as
2 appropriate, unless the exploration license is terminated under (d)(1) of this section
3 or the land is earlier relinquished, removed, or deleted under (d)(2) of this section; and

4 (2) unless the exploration license is terminated under (d)(1) of this
5 section, the option to convert the exploration license for all or part of the state land,
6 except the land that is deleted or removed from the land described in the exploration
7 license under (d)(2) of this section, into an oil and gas lease, or a gas lease only, as
8 appropriate, upon fulfillment of the work commitments contained in the exploration
9 license.

10 * Sec. 17. AS 38.05.132(c) is amended to read:

11 (c) An exploration license awarded under this section

12 (1) is not subject to the acreage limitations imposed by
13 AS 38.05.140(c) or 38.05.180(m);

14 (2) may cover, subject to the maximum acreage limitation on
15 exploration licenses by one licensee under AS 38.05.131(e), an area of not less than
16 10,000 acres and not more than 500,000 acres, that must be reasonably compact and
17 contiguous;

18 (3) must be conditioned upon an obligation to perform a specified
19 work commitment, in total for the term of the license, expressed in dollars of direct
20 exploration expenditures; the specified work commitment

21 (A) may include a provision that adjusts the total amount of
22 work commitment, expressed in dollars of direct exploration expenditures, to
23 account for inflation;

24 (B) must include a requirement that the licensee complete at
25 least 25 percent of the licensee's total specified work commitment by the fourth
26 anniversary of the effective date of the issuance of the [OIL AND GAS]
27 exploration license;

28 (4) must be conditioned upon the posting of a bond or other security
29 acceptable to the commissioner, in favor of the state and subject to the following
30 requirements:

31 (A) the bond or other security must be renewed annually;

1 (B) the annual bond or other security shall be calculated as the
2 entire work commitment expressed in dollars, less the cumulative direct
3 exploration expenditures of the licensee as of the last day of the most recent
4 project year, divided by the number of years remaining in the term of the
5 exploration license;

6 (5) is subject to an annual review and revocation if the commissioner
7 determines that the licensee has failed to provide or maintain in effect the bond or
8 other security required by (4) of this subsection;

9 (6) must be conditioned upon the licensee's payment to the state of a
10 nonrefundable [OIL AND GAS] exploration license fee of \$1 for each acre of land or
11 fraction of each acre that is subject to the exploration license; and

12 (7) must be conditioned upon an agreement that exploration
13 expenditures are subject to audit by the commissioner.

14 * Sec. 18. AS 38.05.132(f) is amended to read:

15 (f) In this section,

16 (1) "direct exploration expenditure" means cash expenses undertaken
17 in performance of a specified work commitment under the provisions of AS 38.05.131
18 - 38.05.134 and necessarily incurred by the licensee in the permitting, mobilization,
19 conducting, demobilization, and evaluation of geophysical and geological surveys, or
20 the drilling, logging, coring, testing, and evaluation of oil and gas or gas only wells;
21 the term

22 (A) includes direct labor costs, including the cost of benefits,
23 for employees directly associated with the work commitment programs, the
24 cost of renting or leasing equipment from parties not affiliated with the
25 licensee, the reasonable costs of maintaining and operating equipment,
26 payments to consultants and independent contractors not affiliated with the
27 licensee, and costs of materials and supplies;

28 (B) does not include noncash expenses such as depreciation
29 and reserves, interest or other costs of borrowed funds, return on investment,
30 overhead, insurance or bond premiums, or any other expense that is
31 unreasonable or that the licensee has not incurred to satisfy the licensee's work

1 commitment;

2 (2) "work commitment" includes the drilling of one or more
3 exploration wells or the gathering of data from activities described in (1) of this
4 subsection, or both.

5 * **Sec. 19.** AS 38.05.133(a) is amended to read:

6 (a) The procedures in this section apply to the issuance of an [OIL AND GAS]
7 exploration license under AS 38.05.132.

8 * **Sec. 20.** AS 38.05.133(f) is amended to read:

9 (f) After considering proposals not rejected under (d) of this section and public
10 comment on those proposals, the commissioner shall issue a written finding
11 addressing all matters set out in AS 38.05.035(e) and (g), except for
12 AS 38.05.035(g)(1)(B)(xi). If the finding concludes that the state's best interests
13 would be served by issuing an [OIL AND GAS] exploration license, the finding must
14 (1) describe the limitations, stipulations, conditions, or changes from the initiating
15 proposal or competing proposals that are required to make the issuance of the
16 exploration license conform to the best interests of the state, and (2) if only one
17 proposal was submitted, identify the prospective licensee whom the commissioner
18 finds should be issued the exploration license. The commissioner shall attach to the
19 finding a copy of the exploration license to be issued and the form of lease that will be
20 used for any portion of the exploration license area subsequently converted to a [AN
21 OIL AND GAS] lease under AS 38.05.134.

22 * **Sec. 21.** AS 38.05.133(h) is amended to read:

23 (h) If competing proposals are submitted, and the commissioner's finding
24 under (f) of this section concludes that an [OIL AND GAS] exploration license should
25 be issued, the commissioner shall issue a request for competitive sealed bids, under
26 procedures adopted by the commissioner by regulation, to determine which
27 prospective licensee should be issued the exploration license. The finding provided to
28 the prospective licensees and the public under (f) of this section must contain notice
29 that (1) the commissioner intends to request competitive sealed bids, (2) a prospective
30 licensee who intends to participate in the bidding must notify the commissioner in
31 writing by the date specified in the notice, and (3) a prospective licensee's notice of

1 intent to participate in the bidding constitutes acceptance of issuance of the
2 exploration license, as limited or conditioned by the terms contained in the finding and
3 by the exploration license to be issued and the form of lease to be used that have been
4 attached to that finding, if the prospective licensee is the successful bidder. The
5 successful bidder is the prospective licensee who submits the highest bid in terms of
6 the minimum work commitment dollar amount.

7 * Sec. 22. AS 38.05.134 is amended to read:

8 **Sec. 38.05.134. Conversion to lease.** If the licensee requests and the
9 commissioner determines that the work commitment obligation set out in an [OIL
10 AND GAS] exploration license issued under AS 38.05.132 has been met, the
11 commissioner shall convert to one or more [OIL AND GAS] leases all or part, as the
12 licensee may indicate, of the area described in the exploration license that remains
13 after the relinquishments, removals, or deletions required by AS 38.05.132(d)(2). A
14 lease issued under this section

15 (1) is subject to the acreage limitations imposed by AS 38.05.140(c);

16 (2) is subject to AS 38.05.180(j) - (m), (o) - (u), and (x) - (z);

17 (3) must be conditioned upon a royalty in amount or value of not less
18 than 12.5 percent of production, except that

19 (A) the lessee who, proceeding under AS 38.05.131 -
20 38.05.134, under a lease issued in the Cook Inlet sedimentary basin who is the
21 first to file with the commissioner a nonconfidential sworn statement claiming
22 to be the first to have drilled a well discovering oil or gas in a previously
23 undiscovered oil or gas pool and who is certified by the commissioner within
24 one year of completion of that discovery well to have drilled a well in that pool
25 that is capable of producing in paying quantities shall pay a royalty of five
26 percent on all production of oil or gas from that pool attributable to that lease
27 for a period of 10 years following the date of discovery of that pool, and
28 thereafter the royalty payable on all production of oil or gas from the pool
29 attributable to that lease shall be determined and payable as specified in the
30 lease; the payment of the five percent royalty under this paragraph is
31 authorized only to a holder of a lease who meets the requirements of

1 AS 38.05.180(f)(4); and

2 (B) for nonconventional gas that is not produced in direct
 3 competition with gas on which a royalty at a rate of at least 12.5 percent is
 4 payable, if the licensee requests, the commissioner may negotiate with the
 5 licensee and set a royalty rate for the gas of at least 6.25 percent; for
 6 purposes of this subparagraph, "nonconventional gas" has the meaning
 7 given in AS 38.05.965;

8 (4) must include an annual rent of \$3 per acre or fraction of an acre
 9 initially paid to the state at inception of the lease and payable annually after that until
 10 the income to the state from royalty under that lease exceeds the rental income to the
 11 state under that lease for that year; and

12 (5) is subject to other conditions and obligations that are specified in
 13 the lease.

14 * Sec. 23. AS 38.05.140(a) is amended to read:

15 (a) A person may not take or hold coal leases or permits during the life of coal
 16 leases on state land exceeding an aggregate of 92,160 acres, except that a person may
 17 apply for coal leases or permits for acreage in addition to 92,160 acres, not exceeding
 18 a total of 5,120 additional acres of state land. The additional area applied for shall be
 19 in multiples of 40 acres, and the application shall contain a statement that the granting
 20 of a lease for additional land is necessary for the person to carry on business
 21 economically and is in the public interest. On the filing of the application, [EXCEPT
 22 AS PROVIDED BY AS 38.05.177(a)(2)(C),] the coal deposits in the land covered by
 23 the application shall be temporarily set aside and withdrawn from all other forms of
 24 disposal provided under AS 38.05.135 - 38.05.181.

25 * Sec. 24. AS 38.05.140(f) is amended to read:

26 (f) The submerged and shoreland lying north of 57 degrees, 30 minutes, North
 27 [NORTH] latitude and east of 159 degrees, 49 minutes, West [WEST] longitude
 28 within the Bristol Bay drainage are designated as the Bristol Bay Fisheries Reserve.
 29 Within the Bristol Bay Fisheries Reserve, a [NO] surface entry permit to develop an
 30 oil or gas lease or an [OIL AND GAS] exploration license under AS 38.05.131 -
 31 38.05.134 may not be issued on state owned or controlled land until the legislature by

1 appropriate resolution specifically finds that the entry will not constitute danger to the
2 fishery.

3 * Sec. 25. AS 38.05.150(f) is amended to read:

4 (f) A [NOTWITHSTANDING AS 38.05.177, A] lease entered into under this
5 section gives the lessee the right to vent or remove methane and other gas held in
6 association with the coal in the land covered by the lease to ensure safe coal mining
7 operations.

8 * Sec. 26. AS 38.05.177(a) is amended to read:

9 (a) The provisions of this section

10 [(1)] apply to nonconventional gas [, WHETHER METHANE
11 ASSOCIATED WITH AND DERIVED FROM COAL DEPOSITS OR
12 OTHERWISE, FROM A FIELD IF A PART OF THE FIELD IS WITHIN 3,000
13 FEET OF THE SURFACE; AND

14 (2) DO NOT APPLY TO AUTHORIZE LEASE OF

15 (A) LAND

16 (i) THAT IS SUBJECT TO AN OIL AND GAS
17 EXPLORATION LICENSE OR LEASE ISSUED UNDER
18 AS 38.05.131 - 38.05.134; OR

19 (ii) THAT IS LEASED UNDER AS 38.05.180;

20 (B) THE LAND (i) THAT IS PROPOSED TO BE SUBJECT
21 TO AN OIL AND GAS EXPLORATION LICENSE OR LEASE ISSUED
22 UNDER AS 38.05.131 - 38.05.134; OR (ii) THAT IS DESCRIBED IN AND
23 PART OF A PROPOSED OIL AND GAS LEASING PROGRAM
24 PREPARED UNDER AS 38.05.180(b); HOWEVER, THE COMMISSIONER
25 MAY WAIVE THE LIMITATIONS OF THIS SUBPARAGRAPH;

26 (C) THE LAND THAT IS HELD UNDER A COAL LEASE
27 ENTERED INTO UNDER AS 38.05.150, UNLESS THE APPLICANT FOR
28 A SHALLOW NATURAL GAS LEASE IS ALSO THE LESSEE UNDER
29 AS 38.05.150 OF THAT LAND; OR

30 (D) THE VALID EXISTING SELECTIONS OF THE
31 ALASKA MENTAL HEALTH TRUST AUTHORITY MADE FOR THE

1 PURPOSE OF RECONSTITUTING THE MENTAL HEALTH TRUST
2 ESTABLISHED UNDER THE ALASKA MENTAL HEALTH ENABLING
3 ACT, P.L. 84-830, 70 STAT. 709 (1956), THAT BECOME SUBJECT TO
4 MANAGEMENT UNDER AS 38.05.801, OR OF LAND THAT HAS BEEN
5 DESIGNATED BY LAW FOR OR IS SUBJECT TO DESIGNATION FOR
6 CONVEYANCE TO THE ALASKA MENTAL HEALTH TRUST
7 AUTHORITY; HOWEVER, AFTER CONSULTATION WITH THE
8 ALASKA MENTAL HEALTH TRUST AUTHORITY, THE
9 COMMISSIONER MAY WAIVE THE LIMITATIONS OF THIS
10 SUBPARAGRAPH].

11 * Sec. 27. AS 38.05.177(d) is amended to read:

12 (d) A lease

13 (1) shall be automatically extended if and for so long thereafter as gas
14 is produced in paying quantities from the lease and the lessee continues to meet all
15 requirements of the lease; a [. A] lease issued under this section covering land on
16 which there is a well capable of producing gas in paying quantities does not expire
17 because the lessee fails to produce gas unless the lessee is allowed reasonable time to
18 place the well on a producing status; if [. IF] drilling has commenced on the
19 expiration date of the primary term of the lease and is continued with reasonable
20 diligence, including such operations as redrilling, sidetracking, or other means
21 necessary to reach the originally proposed bottom hole location, the lease is extended
22 for one year and for so long thereafter as gas is produced in paying quantities; a [. A]
23 gas lease issued under this section that is subject to termination by reason of cessation
24 of production does not terminate if, within 90 days after production ceases or a longer
25 period determined at the discretion of the director, reworking or drilling operations are
26 commenced on the land under lease and are thereafter conducted with reasonable
27 diligence during the period of nonproduction;

28 (2) issued under former (c) of this section before January 1, 2004,
29 may be extended at the discretion of the director; a lease may be extended under
30 this paragraph [. IN ADDITION,] upon application by the lessee; [,] the director
31 may once extend the [A] lease [ISSUED UNDER (c) OF THIS SECTION] for a

1 period of not more than three years: in exercising discretion to extend a lease under
2 this paragraph, the director may not extend the lease unless the director
3 considers

4 (A) the extent of the shallow natural gas exploration
5 activity already conducted on the lease and on adjacent areas;

6 (B) the probability that further shallow natural gas
7 exploration activity will occur on the lease and will lead to shallow natural
8 gas development and production; and

9 (C) whether extension of the lease's primary term will
10 accelerate the eventual production of shallow natural gas from the lease.

11 * Sec. 28. AS 38.05.177(I) is amended to read:

12 (I) A lessee holding [OBTAINING] a lease modified under
13 AS 38.05.180(n)(2) [THIS SECTION] may exercise the rights authorized by this
14 section and the lease. The rights granted by the lease must be exercised in a manner
15 that does not unreasonably interfere with eventual development of other mineral
16 deposits on the land leased. However, in a lease entered into under AS 38.05.150 for
17 land that is already subject to a lease covered [LEASED] under this section, coal may
18 not be mined or extracted by the coal lessee from the coal lease without prior
19 agreement with the lessee holding the lease covered [ISSUED] under this section.

20 * Sec. 29. AS 38.05.180(a) is amended to read:

21 (a) The legislature finds that

22 (1) the people of Alaska have an interest in the development of the
23 state's oil and gas resources to

24 (A) maximize the economic and physical recovery of the
25 resources;

26 (B) maximize competition among parties seeking to explore
27 and develop the resources;

28 (C) maximize use of Alaska's human resources in the
29 development of the resources;

30 (2) it is in the best interests of the state

31 (A) to encourage an assessment of its oil and gas resources and

1 to allow the maximum flexibility in the methods of issuing leases to

2 (i) recognize the many varied geographical regions of
3 the state and the different costs of exploring for oil and gas in these
4 regions;

5 (ii) minimize the adverse impact of exploration,
6 development, production, and transportation activity; and

7 (B) to offer acreage for oil and gas leases or for gas only
8 leases, specifically including

9 (i) state acreage that has been the subject of a best
10 interest finding at annual areawide lease sales; and

11 (ii) land in areas that, under (d) of this section, may be
12 leased without having been included in the leasing program prepared
13 and submitted under (b) of this section.

14 * **Sec. 30.** AS 38.05.180(b) is amended to read:

15 (b) The commissioner shall biennially prepare and, between the first and the
16 15th day of the first regular session of each legislature, notify the legislature of the
17 availability of, a five-year proposed oil and gas leasing program consisting of a
18 schedule of proposed lease sales and specifying as precisely as practicable the location
19 of tracts proposed to be offered for oil and gas leasing or for leasing of gas only
20 during the calendar year in which the proposed program is made available to the
21 legislature and the following four calendar years.

22 * **Sec. 31.** AS 38.05.180(c) is amended to read:

23 (c) Except as provided in (d) and (w) of this section, an oil and gas lease sale
24 or gas only lease sale may not be held unless it was included in the proposed leasing
25 programs submitted to the legislature during the two calendar years preceding the year
26 in which the sale is held. A lease sale, whether for oil and gas or for gas only, may
27 not be held before the date it is scheduled in the proposed oil and gas leasing program.

28 * **Sec. 32.** AS 38.05.180(d) is amended to read:

29 (d) The commissioner

30 (1) may annually offer leases for oil and gas or leases for gas only
31 [LEASES] of the acreage described in AS 38.05.035(e)(6)(F);

1 (2) may issue [OIL AND GAS] leases in an area that has not been
2 included in a leasing program prepared, in accordance with (b) of this section, if the
3 land to be leased

4 (A) was previously subject to a valid state oil and gas lease, a
5 valid state gas lease, or a valid federal oil and gas lease;

6 (B) is contiguous to land already under state, federal, or private
7 lease and the commissioner makes a written finding, after hearing, that leasing
8 of the land would result in a substantial probability of early evaluation and
9 development of the land to be leased;

10 (C) is adjacent to land owned or controlled by another party on
11 which a discovery of commercial quantities of oil or gas has been made, and
12 the commissioner finds, after hearing, that there is a reasonable probability that
13 the land to be leased contains oil or gas in communication with the oil or gas
14 discovered on the land of the other party;

15 (D) is adjacent to land included in the federal five-year Outer
16 Continental Shelf leasing program under 43 U.S.C. 1344, and the
17 commissioner makes a written finding, after hearing, that coordinated or
18 simultaneous leasing with the federal government is in the public interest; or

19 (E) is the subject of an [OIL AND GAS] exploration license
20 issued under AS 38.05.131 - 38.05.134; however, if the license issued was
21 for exploration for and recovery of gas only, then the lease issued under
22 this subsection shall be limited to exploration for and recovery of gas only.

23 * Sec. 33. AS 38.05.180(f) is amended to read:

24 (f) Except as provided by AS 38.05.131 - 38.05.134 [AND 38.05.177], the
25 commissioner may issue oil and gas leases or leases for gas only on state land to the
26 highest responsible qualified bidder as follows:

27 (1) the commissioner shall issue an oil and gas lease or a gas only
28 lease, as appropriate, to the successful bidder determined by competitive bidding
29 under regulations adopted by the commissioner; bidding may be by sealed bid or
30 according to any other bidding procedure the commissioner determines is in the best
31 interests of the state;

1 (2) whenever, under any of the leasing methods listed in this
2 subsection, a royalty share is reserved to the state, it shall be delivered in pipeline
3 quality and free of all lease or unit expenses, including but not limited to separation,
4 cleaning, dehydration, gathering, salt water disposal, and preparation for transportation
5 off the lease or unit area;

6 (3) following a pre-sale analysis, the commissioner may choose at least
7 one of the following leasing methods:

8 (A) a cash bonus bid with a fixed royalty share reserved to the
9 state of not less than 12.5 percent in amount or value of the production
10 removed or sold from the lease;

11 (B) a cash bonus bid with a fixed royalty share reserved to the
12 state of not less than 12.5 percent in amount or value of the production
13 removed or sold from the lease and a fixed share of the net profit derived from
14 the lease of not less than 30 percent reserved to the state;

15 (C) a fixed cash bonus with a royalty share reserved to the state
16 as the bid variable but no less than 12.5 percent in amount or value of the
17 production removed or sold from the lease;

18 (D) a fixed cash bonus with the share of the net profit derived
19 from the lease reserved to the state as the bid variable;

20 (E) a fixed cash bonus with a fixed royalty share reserved to the
21 state of not less than 12.5 percent in amount or value of the production
22 removed or sold from the lease with the share of the net profit derived from the
23 lease reserved to the state as the bid variable;

24 (F) a cash bonus bid with a fixed royalty share reserved to the
25 state based on a sliding scale according to the volume of production or other
26 factor but in no event less than 12.5 percent in amount or value of the
27 production removed or sold from the lease;

28 (G) a fixed cash bonus with a royalty share reserved to the state
29 based on a sliding scale according to the volume of production or other factor
30 as the bid variable but not less than 12.5 percent in amount or value of the
31 production removed or sold from the lease;

1 (H) for nonconventional gas that will not be produced in
2 direct competition with gas on which a royalty at a rate of at least 12.5
3 percent is payable, a royalty share reserved to the state of at least 6.25
4 percent in amount or value of the production removed or sold from the
5 lease;

6 (4) notwithstanding a requirement in the leasing method chosen of a
7 minimum fixed royalty share, on and after March 3, 1997, the lessee under a lease
8 issued in the Cook Inlet sedimentary basin who is the first to file with the
9 commissioner a nonconfidential sworn statement claiming to be the first to have
10 drilled a well discovering oil or gas in a previously undiscovered oil or gas pool and
11 who is certified by the commissioner within one year of completion of that discovery
12 well to have drilled a well in that pool that is capable of producing in paying quantities
13 shall pay a royalty of five percent on all production of oil or gas from that pool
14 attributable to that lease for a period of 10 years following the date of discovery of that
15 pool, and thereafter the royalty payable on all production of oil or gas from the pool
16 attributable to that lease shall be determined and payable as specified in the lease; for
17 purposes of this paragraph, the reduced royalty authorized by this paragraph is subject
18 to the following:

19 (A) only one reduction of royalty authorized by this paragraph
20 may be allowed on each lease that qualifies for reduction of royalty under this
21 paragraph;

22 (B) if, under this paragraph, application is made for a royalty
23 reduction for a lease that was entered into before March 3, 1997, the
24 commissioner may approve the application only if, on that date, the lease was a
25 nonproducing lease that was not committed to a unit approved by the
26 commissioner under (m) of this section, that is not part of a unit under (p) or
27 (q) of this section, and that has not been made part of a unit under AS 31.05;

28 (C) if application for a royalty reduction is made under this
29 paragraph for a lease on which a discovery royalty was claimed or may be
30 claimed under the discovery royalty provisions of former AS 38.05.180(a) in
31 effect before May 6, 1969, the commissioner shall disallow the application

1 under this paragraph unless the applicant waives the right to claim the right to
2 a reduced royalty under the discovery royalty provisions of former
3 AS 38.05.180(a) in effect before May 6, 1969; and

4 (D) the commissioner shall adopt regulations setting out the
5 standards, criteria, and definitions of terms that apply to implement the filing
6 of applications for, and the review and certification of, discovery [OIL AND
7 GAS ROYALTY] certifications under this paragraph;

8 (5) notwithstanding and in lieu of a requirement in the leasing method
9 chosen of a minimum fixed royalty share, or the royalty provision of a lease, for leases
10 unitized as described in (p) of this section, leases subject to an agreement described in
11 (s) or (t) of this section, or interests unitized under AS 31.05, the lessee of all or part of
12 an oil or gas field identified in this section that has been granted approval of a written
13 plan submitted to the Alaska Oil and Gas Conservation Commission under
14 AS 31.05.030(i) shall, subject to (dd) of this section, pay a royalty of five percent on
15 the first 25,000,000 barrels of oil and the first 35,000,000,000 cubic feet of gas
16 produced for sale from that field that occurs in the 10 years following the date on
17 which the production for sale commences; the fields eligible for royalty reduction
18 under this paragraph, all of which are located within the Cook Inlet sedimentary basin,
19 were discovered before January 1, 1988, and have been undeveloped or shut in from at
20 least January 1, 1988, through December 31, 1997, are

21 (A) Falls Creek;

22 (B) Nicolai Creek;

23 (C) North Fork;

24 (D) Point Starichkof;

25 (E) Redoubt Shoal; and

26 (F) West Foreland;

27 (6) notwithstanding and in lieu of a requirement in the leasing method
28 chosen of a minimum fixed royalty share, or the royalty provision of a lease, for leases
29 unitized as described in (p) of this section, leases subject to an agreement described in
30 (s) or (t) of this section, or interests unitized under AS 31.05, the lessee of all or part of
31 an oil field located offshore in Cook Inlet on which an oil production platform

1 specified in (A), (C), or (E) of this paragraph operates, or the lessee of all or part of the
2 field located offshore in Cook Inlet and described in (G) of this paragraph,

3 (A) shall pay a royalty of five percent on oil produced from the
4 platform if oil production that equaled or exceeded a volume of 1,200 barrels a
5 day declines to less than that amount for a period of at least one calendar
6 quarter, as certified by the Alaska Oil and Gas Conservation Commission, for
7 as long as the volume of oil produced from the platform remains less than
8 1,200 barrels a day; the provisions of this subparagraph apply to

- 9 (i) Dolly;
10 (ii) Grayling;
11 (iii) King Salmon;
12 (iv) Steelhead; and
13 (v) Monopod;

14 (B) shall pay a royalty calculated under this subparagraph if the
15 volume of oil produced from the platform that was certified by the Alaska Oil
16 and Gas Conservation Commission under (A) of this paragraph later increases
17 to 1,200 or more barrels a day and remains at 1,200 or more barrels a day for a
18 period of at least one calendar quarter; until the royalty rate determined under
19 this subparagraph applies, the royalty continues to be calculated under (A) of
20 this paragraph; on and after the first day of the month following the month the
21 increased production exceeds the period specified in this subparagraph, the
22 royalty payable under this subparagraph is

- 23 (i) for production of at least 1,200 barrels a day but not
24 more than 1,300 barrels a day - seven percent;
25 (ii) for production of more than 1,300 barrels a day but
26 not more than 1,400 barrels a day - 8.5 percent;
27 (iii) for production of more than 1,400 barrels a day but
28 not more than 1,500 barrels a day - 10 percent; and
29 (iv) for production of more than 1,500 barrels a day -
30 12.5 percent;

31 (C) shall pay a royalty of five percent on oil produced from the

1 platform if oil production that equaled or exceeded a volume of 975 barrels a
2 day declines to less than that amount for a period of at least one calendar
3 quarter, as certified by the Alaska Oil and Gas Conservation Commission, for
4 as long as the volume of oil produced from the platform remains less than 975
5 barrels a day; the provisions of this subparagraph apply to

- 6 (i) Baker;
7 (ii) Dillon;
8 (iii) XTO.A; and
9 (iv) XTO.C;

10 (D) shall pay a royalty calculated under this subparagraph if the
11 volume of oil produced from the platform that was certified by the Alaska Oil
12 and Gas Conservation Commission under (C) of this paragraph later increases
13 to 975 or more barrels a day and remains at 975 or more barrels a day for a
14 period of at least one calendar quarter; until the royalty rate determined under
15 this subparagraph applies, the royalty continues to be calculated under (C) of
16 this paragraph; on and after the first day of the month following the month the
17 increased production exceeds the period specified in this subparagraph, the
18 royalty payable under this subparagraph is

- 19 (i) for production of at least 975 barrels a day but not
20 more than 1,100 barrels a day - seven percent;
21 (ii) for production of more than 1,100 barrels a day but
22 not more than 1,200 barrels a day - 8.5 percent;
23 (iii) for production of more than 1,200 barrels a day but
24 not more than 1,350 barrels a day - 10 percent; and
25 (iv) for production of more than 1,350 barrels a day -
26 12.5 percent;

27 (E) shall pay a royalty of five percent on oil produced from the
28 platform if oil production that equaled or exceeded a volume of 750 barrels a
29 day declines to less than that amount for a period of at least one calendar
30 quarter, as certified by the Alaska Oil and Gas Conservation Commission, for
31 as long as the volume of oil produced from the platform remains less than 750

1 barrels a day; the provisions of this subparagraph apply to

2 (i) Granite Point;

3 (ii) Anna; and

4 (iii) Bruce;

5 (F) shall pay a royalty calculated under this subparagraph if the
6 volume of oil produced from the platform that was certified by the Alaska Oil
7 and Gas Conservation Commission under (E) of this paragraph later increases
8 to 750 or more barrels a day and remains at 750 or more barrels a day for a
9 period of at least one calendar quarter; until the royalty rate determined under
10 this subparagraph applies, the royalty continues to be calculated under (E) of
11 this paragraph; on and after the first day of the month following the month the
12 increased production exceeds the period specified in this subparagraph, the
13 royalty payable under this subparagraph is

14 (i) for production of at least 750 barrels a day but not
15 more than 850 barrels a day - seven percent;

16 (ii) for production of more than 850 barrels a day but
17 not more than 1,000 barrels a day - 8.5 percent;

18 (iii) for production of more than 1,000 barrels a day but
19 not more than 1,200 barrels a day - 10 percent; and

20 (iv) for production of more than 1,200 barrels a day -
21 12.5 percent;

22 (G) shall pay a royalty of five percent on oil produced from the
23 field if oil production that equaled or exceeded a volume of 750 barrels a day
24 declines to less than that amount for a period of at least one calendar quarter,
25 as certified by the Alaska Oil and Gas Conservation Commission, for as long
26 as the volume of oil produced from the field remains less than 750 barrels a
27 day; the provisions of this subparagraph apply to the West McArthur River
28 field;

29 (H) shall pay a royalty calculated under this subparagraph if the
30 volume of oil produced from the field that was certified by the Alaska Oil and
31 Gas Conservation Commission under (G) of this paragraph later increases to

1 750 or more barrels a day and remains at 750 or more barrels a day for a period
2 of at least one calendar quarter; until the royalty rate determined under this
3 subparagraph applies, the royalty continues to be calculated under (G) of this
4 paragraph; on and after the first day of the month following the month the
5 increased production exceeds the period specified in this subparagraph, the
6 royalty payable under this subparagraph is

7 (i) for production of at least 750 barrels a day but not
8 more than 850 barrels a day - seven percent;

9 (ii) for production of more than 850 barrels a day but
10 not more than 1,000 barrels a day - 8.5 percent;

11 (iii) for production of more than 1,000 barrels a day but
12 not more than 1,200 barrels a day - 10 percent; and

13 (iv) for production of more than 1,200 barrels a day -
14 12.5 percent; and

15 (I) may obtain the benefits of the royalty adjustments set out in
16 (A) - (H) of this paragraph only if the commissioner determines that the
17 reduction in production from the platform or the field is

18 (i) based on the average daily production during the
19 calendar quarter based on reservoir conditions; and

20 (ii) not the result of short-term production declines due
21 to mechanical or other choke-back factors, temporary shutdowns or
22 decreased production due to environmental or facility constraints, or
23 market conditions.

24 * Sec. 34. AS 38.05.180(h) is amended to read:

25 (h) The commissioner may include terms in any [OIL AND GAS] lease
26 imposing a minimum work commitment on the lessee. These terms shall be made
27 public before the sale, and may include appropriate penalty provisions to take effect in
28 the event the lessee does not fulfill the minimum work commitment. If it is
29 demonstrated that a lease has been proven unproductive by actions of adjacent lease
30 holders, the commissioner may set aside a work commitment. The commissioner may
31 waive for a period not to exceed one two-year period any term of a minimum work

1 commitment if the commissioner makes a written finding either that conditions
2 preventing drilling or exploration were beyond the lessee's reasonable ability to
3 foresee or control or that the lessee has demonstrated through good faith efforts an
4 intent and ability to drill or develop the lease during the term of the waiver.

5 * Sec. 35. AS 38.05.180(i) is amended to read:

6 (i) The commissioner may provide for the establishment of an exploration
7 incentive credit system under which a lessee of state land drilling an exploratory well
8 on that land may earn credits based upon the footage drilled and the region in which
9 the well is situated. The commissioner may also provide for credits to be earned by
10 persons performing geophysical work on state land, if that work is performed during
11 the two seasons immediately preceding an announced lease sale and on land included
12 within the sale area and the geophysical information is made public following the sale.
13 Credits may not exceed 50 percent of the cost of the drilling or geophysical work.
14 Credits may be used during a limited period established by the commissioner and may
15 be assigned during that period. Credits may be applied against (1) [OIL AND GAS]
16 royalty and rental payments for oil and gas or for gas only payable to the state or (2)
17 taxes payable under AS 43.55. A credit may not exceed 50 percent of the payment
18 toward which it is being applied. Amounts due the Alaska permanent fund
19 (AS 37.13.010) shall be calculated before the application of credits under this
20 subsection.

21 * Sec. 36. AS 38.05.180(j) is amended to read:

22 (j) The commissioner

23 (1) may provide for modification of royalty on individual leases, leases
24 unitized as described in (p) of this section, leases subject to an agreement described in
25 (s) or (t) of this section, or interests unitized under AS 31.05

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

27 (i) the oil or gas field or pool has been sufficiently
28 delineated to the satisfaction of the commissioner;

29 (ii) the field or pool has not previously produced oil or
30 gas for sale; and

31 (iii) oil or gas production from the field or pool would

1 not otherwise be economically feasible;

2 (B) to prolong the economic life of an oil or gas field or pool as
3 per barrel or barrel equivalent costs increase or as the price of oil or gas
4 decreases, and the increase or decrease is sufficient to make future production
5 no longer economically feasible; or

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

8 (2) may not grant a royalty modification unless the lessee or lessees
9 requesting the change make a clear and convincing showing that a modification of
10 royalty meets the requirements of this subsection and is in the best interests of the
11 state;

12 (3) shall provide for an increase or decrease or other modification of
13 the state's royalty share by a sliding scale royalty or other mechanism that shall be
14 based on a change in the price of oil or gas and may also be based on other relevant
15 factors such as a change in production rate, projected ultimate recovery, development
16 costs, and operating costs

17 (4) may not grant a royalty reduction for a field or pool

18 (A) under (1)(A) of this subsection if the royalty modification
19 for the field or pool would establish a royalty rate of less than five percent in
20 amount or value of the production removed or sold from a lease or leases
21 covering the field or pool;

22 (B) under (1)(B) or (1)(C) of this subsection if the royalty
23 modification for the field or pool would establish a royalty rate of less than
24 three percent in amount or value of the production removed or sold from a
25 lease or leases covering the field or pool;

26 (5) may not grant a royalty reduction under this subsection without
27 including an explicit condition that the royalty reduction is not assignable without the
28 prior written approval, which may not be unreasonably withheld, by the
29 commissioner; the commissioner shall, in the preliminary and final findings and
30 determinations, set out the conditions under which the royalty reduction may be
31 assigned;

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

4 (A) may require disclosure of only the financial and technical
5 data related to development, production, and transportation of oil and gas or
6 gas only from the field or pool that are reasonably available to the applicant;
7 and

8 (B) shall keep the data confidential under AS 38.05.035(a)(9)
9 at the request of the lessee or lessees making application for the royalty
10 reduction; the confidential data may be disclosed by the commissioner to
11 legislators and to the legislative auditor and as directed by the chair or vice-
12 chair of the Legislative Budget and Audit Committee to the director of the
13 division of legislative finance, the permanent employees of their respective
14 divisions who are responsible for evaluating a royalty reduction, and to agents
15 or contractors of the legislative auditor or the legislative finance director who
16 are engaged under contract to evaluate the royalty reduction, if they sign an
17 appropriate confidentiality agreement;

18 (7) may

19 (A) require the lessee or lessees making application for the
20 royalty reduction under (1)(A) of this subsection to pay for the services of an
21 independent contractor, selected by the lessee or lessees from a list of qualified
22 consultants compiled by the commissioner, to evaluate hydrocarbon
23 development, production, transportation, and economics and to assist the
24 commissioner in evaluating the application and financial and technical data; if,
25 under this subparagraph, the commissioner requires payment for the services of
26 an independent contractor, the total cost of the services to be paid for by the
27 lessee or lessees may not exceed \$150,000 for each application, and the
28 commissioner shall determine the relevant scope of the work to be performed
29 by the contractor; selection of an independent contractor under this
30 subparagraph is not subject to AS 36.30;

31 (B) with the mutual consent of the lessee or lessees making

1 application for the royalty reduction under (1)(B) or (1)(C) of this subsection,
2 request payment for the services of an independent contractor, selected from a
3 list of qualified consultants to evaluate hydrocarbon development, production,
4 transportation, and economics by the commissioner to assist the commissioner
5 in evaluating the application and financial and technical data; if, under this
6 subparagraph, the commissioner requires payment for the services of an
7 independent contractor, the total cost of the services that may be paid for by
8 the lessee or lessees may not exceed \$150,000 for each application, and the
9 commissioner shall determine the relevant scope of the work to be performed
10 by the contractor; selection of an independent contractor under this
11 subparagraph is not subject to AS 36.30;

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

16 (9) shall offer to appear before the Legislative Budget and Audit
17 Committee, on a day that is not earlier than 10 days and not later than 20 days after
18 giving public notice under (8) of this subsection, to provide the committee a review of
19 the commissioner's preliminary findings and determination on the royalty reduction
20 application and administrative process; if the Legislative Budget and Audit Committee
21 accepts the commissioner's offer, the committee shall give notice of the committee's
22 meeting to all members of the legislature;

23 (10) shall make copies of the preliminary findings and determination
24 available to

25 (A) the presiding officer of each house of the legislature;

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

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

30 (11) shall, within 30 days after the close of the public comment period
31 under (8) of this subsection,

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

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

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

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

11 (E) make copies of the final findings and determination
12 available to each person who submitted comment under (8) of this subsection
13 and who has filed a request for the copies;

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

16 * Sec. 37. AS 38.05.180(l) is amended to read:

17 (l) Subject to the provisions of AS 31.05, the commissioner has discretion to
18 enter into an agreement whereby, with the consent of the lessee, the state's royalty
19 share of [OIL AND GAS] production of oil and gas or gas only may be stored or
20 retained in storage by the lessee, or the commissioner may enter into an agreement
21 with one or more of the affected field lease holders to trade current royalty production
22 from a field for a like amount, kind, and quality of future production, on the condition
23 that the state receives back its stored or traded royalty share during the first half of the
24 estimated field life or no later than 15 years after start of production, whichever is
25 sooner.

26 * Sec. 38. AS 38.05.180(m) is amended to read:

27 (m) An oil and gas lease or a gas only lease must cover a reasonably compact
28 area not exceeding 5,760 acres, and may be for a maximum period of 10 years, except
29 that the commissioner may issue a lease for a period not less than five years upon a
30 finding that it is in the best interests of the state. An oil and gas lease shall be
31 automatically extended if and for so long thereafter as oil or gas is produced in paying

1 quantities from the lease or if the lease is committed to a unit approved by the
 2 commissioner, and a gas only lease shall be automatically extended if and for so
 3 long thereafter as gas is produced in paying quantities from the lease or if the
 4 lease is committed to a unit approved by the commissioner. A lease issued under
 5 this section covering land on which there is a well capable of producing oil or gas in
 6 paying quantities does not expire because the lessee fails to produce oil or gas unless
 7 the lessee is allowed reasonable time to place the well on a producing status. Upon
 8 extension, the commissioner may increase lease rentals so long as the increased rental
 9 rate does not exceed 150 percent of the rate for the preceding year. If drilling has
 10 commenced on the expiration date of the primary term of the lease and is continued
 11 with reasonable diligence, including such operations as redrilling, sidetracking, or
 12 other means necessary to reach the originally proposed bottom hole location, the lease
 13 continues in effect until 90 days after drilling has ceased and for so long thereafter as
 14 oil or gas is produced in paying quantities. An oil and gas lease or a gas only lease
 15 issued under this section which is subject to termination by reason of cessation of
 16 production does not terminate if, within 60 days after production ceases, reworking or
 17 drilling operations are commenced on the land under lease and are thereafter
 18 conducted with reasonable diligence during the period of nonproduction.

19 * Sec. 39. AS 38.05.180(n) is amended to read:

20 (n) The commissioner may establish by regulation that after a well has been
 21 plugged and abandoned, the rental rate which was in effect during the year of
 22 abandonment is maintained for the remainder of the term. Rental is payable in
 23 advance and continues until income to the state from royalty or net profit share
 24 exceeds rental income to the state for that year. Under this subsection,

25 (1) [OIL AND GAS] leases for oil and gas or for gas only shall
 26 provide for payment to the state of rental on the following basis:

27 (A) [(1)] for the first year, \$1.00 per acre;

28 (B) [(2)] for the second year, \$1.50 per acre;

29 (C) [(3)] for the third year, \$2.00 per acre;

30 (D) [(4)] for the fourth year, \$2.50 per acre;

31 (E) [(5)] for the fifth and following years, \$3.00 per acre;

1 (2) if the lessee under a gas only lease demonstrates to the
2 commissioner that the potential resources underlying the lease are reasonably
3 estimated to be only nonconventional gas, the rental payment is \$1.00 per acre
4 until the lease expires or paying quantities of conventional oil or gas are
5 discovered underlying the lease.

6 * Sec. 40. AS 38.05.180(p) is amended to read:

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

24 * Sec. 41. AS 38.05.180 is amended by adding a new subsection to read:

25 (ff) The provisions of this section that authorize oil and gas leases also apply
26 to authorize the commissioner to issue leases for the production of gas only. In
27 authorizing and managing leases under this subsection, the terms "oil and gas" or "oil
28 or gas" as they are used in this chapter may be read and applied as appropriate as
29 referring to gas only. When a lease is authorized as a gas only lease, the lease does
30 not give the lessee the right to produce oil. If a well drilling for gas under a gas only
31 lease authorized by this subsection penetrates a formation capable of producing oil, the

1 owner or operator

2 (1) shall notify the department and the Alaska Oil and Gas
3 Conservation Commission; and

4 (2) may not conduct further operations in the drilled well until the
5 facility complies with all applicable laws and regulations relating to oil and gas
6 exploration and production; however, this paragraph does not prevent the owner or
7 operator from conducting activities that may be required by the Alaska Oil and Gas
8 Conservation Commission to plug, plug-back, or abandon a well.

9 * Sec. 42. AS 38.05.860(a) is amended to read:

10 (a) The commissioner may require an applicant seeking the sale, lease, or
11 other disposal of land or an interest in land, other than under an oil and gas lease, gas
12 only lease, or mineral lease, to deposit an amount covering the estimated cost of an
13 appraisal, survey, and other costs necessary to offer the land or interest in land,
14 including advertising. All deposited funds not expended shall be refunded to the
15 applicant. If the land or interest in land is awarded to a person other than the applicant
16 making the deposit, the person awarded the land shall pay the total actual cost incurred
17 by the department in making the disposal, and the deposit shall be returned to the
18 original applicant. In lieu of requiring the deposit under this subsection, the
19 commissioner may enter into an agreement with an applicant seeking land or an
20 interest in land requiring the applicant to reimburse the department for costs incurred
21 in the disposal if the applicant is awarded the land or interest in land.

22 * Sec. 43. AS 38.05.860(c) is amended to read:

23 (c) The commissioner shall require each bidder for the competitive leasing of
24 [OIL AND GAS] land for oil and gas, or for gas only, to submit with each bid a
25 deposit of money equal to 20 percent of the bonus.

26 * Sec. 44. AS 38.05.945(a) is amended to read:

27 (a) This section establishes the requirements for notice given by the
28 department for the following actions:

29 (1) classification or reclassification of state land under AS 38.05.300
30 and the closing of land to mineral leasing or entry under AS 38.05.185;

31 (2) zoning of land under applicable law;

1 (3) issuance of a

2 (A) preliminary written finding under AS 38.05.035(e)(5)(A)
3 regarding the sale, lease, or disposal of an interest in state land or resources for
4 oil and gas, or for gas only, subject to AS 38.05.180(b);

5 (B) [REPEALED

6 (C)] written finding for the sale, lease, or disposal of an interest
7 in state land or resources under AS 38.05.035(e)(6), except a [AN OIL OR
8 GAS] lease sale described in AS 38.05.035(e)(6)(F) for which the director
9 must provide opportunity for public comment under the provisions of that
10 subparagraph;

11 (4) a competitive disposal of an interest in state land or resources after
12 final decision under AS 38.05.035(e);

13 (5) a preliminary finding under AS 38.05.035(e) concerning sites for
14 aquatic farms and related hatcheries;

15 (6) a decision under AS 38.05.132 - 38.05.134 regarding the sale,
16 lease, or disposal of an interest in state land or resources.

17 * Sec. 45. AS 38.05.965 is amended by adding a new paragraph to read:

18 (25) "nonconventional gas" means coal bed methane, shales containing
19 gas, or gas hydrates.

20 * Sec. 46. AS 38.06.080(2) is amended to read:

21 (2) "state lease" means an oil and gas lease or gas only lease on state
22 land.

23 * Sec. 47. AS 38.35.020(a) is amended to read:

24 (a) Rights-of-way on state land including rights-of-way over, under, along,
25 across, or upon the right-of-way of a public road or highway or the right-of-way of a
26 railroad or other public utility, or across, upon, over, or under a river or other body of
27 water or land belonging to or administered by the state may be granted by
28 noncompetitive lease by the commissioner for pipeline purposes for the transportation
29 of oil, products, or natural gas under those conditions prescribed by law or by
30 administrative regulation. Except to the extent authorized by an oil and gas lease, a
31 gas only lease, or an oil and gas or gas only unit agreement approved by the state, no

1 person may engage in any construction or operation of any part of an oil, products, or
2 natural gas pipeline, which in whole or in part is or is proposed to be on state land
3 unless that person has obtained from the commissioner a right-of-way lease of the land
4 under this chapter.

5 * Sec. 48. AS 43.20.072(c) is amended to read:

6 (c) A taxpayer's business income shall be apportioned to this state by
7 multiplying the taxpayer's income determined under (b) of this section by the
8 apportionment factor applicable to the taxpayer among the following factors:

9 (1) the apportionment factor of a taxpayer subject to this section but
10 not engaged in the production of oil and gas, or of gas only, as appropriate, from a
11 lease or property in this state during the tax period is a fraction, the numerator of
12 which is the sum of the property factor under AS 43.19 (Multistate Tax Compact) and
13 the sales factor under (d) of this section for the taxpayer for that tax period, and the
14 denominator of which is two;

15 (2) the apportionment factor of a taxpayer subject to this section but
16 not engaged in the pipeline transportation of oil or gas in this state during the tax
17 period is a fraction, the numerator of which is the sum of the property factor under (e)
18 of this section and the extraction factor under (f) of this section for the taxpayer for the
19 tax period, and the denominator of which is two;

20 (3) the apportionment factor of a taxpayer engaged both in the
21 production of oil or gas from a lease or property in this state and in the pipeline
22 transportation of oil or gas in this state during the tax period is a fraction, the
23 numerator of which is the sum of the sales factor under (d) of this section, the property
24 factor under (e) of this section, and the extraction factor under (f) of this section for
25 the taxpayer for the tax period, and the denominator of which is three.

26 * Sec. 49. AS 43.55.025(a) is amended to read:

27 (a) Subject to the terms and conditions of this section, on oil and gas produced
28 from an oil and gas lease, or on gas produced from a gas only lease, on or after
29 July 1, 2004, a credit against the tax due under this chapter is allowed in an amount
30 equal to

31 (1) 20 percent of the total exploration expenditures that qualify under

1 (b) and (c) of this section, 20 percent of the total exploration expenditures that qualify
2 under (b) and (d) of this section, or both, for a total credit that does not exceed 40
3 percent of the total exploration expenditures; or

4 (2) 40 percent of the total exploration expenditures that qualify under
5 (b) and (e) of this section, for a total production tax credit that does not exceed 40
6 percent of the total qualified exploration expenditures.

7 * **Sec. 50.** AS 43.55.900(9) is amended to read:

8 (9) "lease or property" means any right, title, or interest in or the right
9 to produce or recover oil or gas including:

10 (A) a mineral interest,

11 (B) a leasehold interest,

12 (C) a working interest, royalty interest, overriding royalty
13 interest, production payment, net profit interest or any other interest in a lease,
14 concession, joint venture, or other agreement for [OIL AND GAS] exploration,
15 development, or production of oil and gas or of gas only,

16 (D) a working interest, royalty interest, overriding royalty
17 interest, production payment, net profit interest or any other interest in an
18 agreement for unitization or pooling under the provisions of 26 U.S.C.
19 614(b)(3) (Internal Revenue Code) as defined on January 1, 1974;

20 * **Sec. 51.** AS 46.03.100(f) is amended to read:

21 (f) This section does not apply to discharges of solid or liquid waste material
22 or water discharges from the following activities if the discharge is incidental to the
23 activity and the activity does not produce a discharge from a point source, as that term
24 is defined in regulations adopted under this chapter, directly into any surface water of
25 the state:

26 (1) mineral drilling, trenching, ditching, and similar activities;

27 (2) landscaping;

28 (3) water well drilling, geophysical drilling, or nonconventional
29 [COAL BED METHANE DRILLING OR OTHER NATURAL] gas drilling; for
30 purposes of this paragraph, "nonconventional gas" has the meaning given in
31 AS 38.05.965 [TO RECOVER GAS FROM A FIELD IF A PART OF THE FIELD IS

1 WITHIN 3,000 FEET OF THE SURFACE]; or

2 (4) drilling, ditching, trenching, and similar activities associated with
3 facility construction and maintenance or with road or other transportation facility
4 construction and maintenance; however, the exemption provided by this paragraph
5 does not relieve a person from obtaining a permit under this section if

6 (A) the drilling, ditching, trenching, or similar activity will
7 involve the removal of the groundwater, stormwater, or wastewater runoff that
8 has accumulated and is present at an excavation site for facility, road, or other
9 transportation construction or maintenance; and

10 (B) a permit is otherwise required by this section.

11 * **Sec. 52.** AS 46.04.030(b) is amended to read:

12 (b) A person may not cause or permit the operation of a pipeline or an
13 exploration or production facility in the state unless an oil discharge prevention and
14 contingency plan for the pipeline or facility has been approved by the department and
15 the person is in compliance with the plan. This subsection does not apply to an
16 exploration or production facility used solely to explore for or to develop or produce
17 nonconventional [SHALLOW NATURAL] gas resources, except that this exemption
18 does not apply if the Alaska Oil and Gas Conservation Commission determines under
19 AS 31.05.030(j) that

20 (1) a well drilled for nonconventional [SHALLOW NATURAL] gas
21 may penetrate a formation capable of flowing oil; and

22 (2) the volume of oil encountered will be of such quantities that a
23 contingency plan will be required.

24 * **Sec. 53.** AS 46.04.040(b) is amended to read:

25 (b) A person may not cause or permit the operation of a pipeline or an
26 exploration or production facility in the state unless the person has furnished to the
27 department, and the department has approved, proof of financial ability to respond in
28 damages. Proof of financial responsibility required for

29 (1) a pipeline or an offshore exploration or production facility is
30 \$50,000,000 per incident;

31 (2) an onshore production facility is

1 (A) \$20,000,000 per incident if the facility produces over
2 10,000 barrels per day of oil;

3 (B) \$10,000,000 per incident if the facility produces over 5,000
4 barrels per day but not more than 10,000 barrels per day of oil;

5 (C) \$5,000,000 per incident if the facility produces over 2,500
6 barrels per day but not more than 5,000 barrels per day of oil;

7 (D) \$1,000,000 per incident if the facility produces 2,500
8 barrels per day or less of oil;

9 (3) an onshore exploration facility is

10 (A) \$25,000 per incident for a facility used solely to explore for
11 nonconventional [SHALLOW NATURAL] gas by means of drilling a well to
12 explore for the gas [, WHETHER METHANE ASSOCIATED WITH AND
13 DERIVED FROM COAL DEPOSITS OR OTHERWISE, FROM A FIELD IF
14 A PART OF THE FIELD IS WITHIN 3,000 FEET OF THE SURFACE]; and

15 (B) except as provided by (A) of this paragraph, \$1,000,000 per
16 incident.

17 * Sec. 54. AS 46.04.900 is amended by adding a new paragraph to read:

18 (31) "nonconventional gas" has the meaning given in AS 38.05.965.

19 * Sec. 55. AS 46.40.205 is amended to read:

20 **Sec. 46.40.205. Consistency determinations for certain activities involving**
21 **nonconventional [SHALLOW NATURAL] gas.** (a) When conducted under
22 oversight and regulation of the Alaska Oil and Gas Conservation Commission and the
23 state's resource agencies, projects for the exploration and development of
24 nonconventional [SHALLOW NATURAL] gas are consistent with the program
25 described in this chapter. Persons responsible for activities subject to this section shall
26 obtain all required permits and approvals from municipal, state, and federal agencies
27 as otherwise required by law.

28 (b) In this section, "nonconventional [SHALLOW NATURAL] gas" has the
29 meaning given in AS 38.05.965 [AS 46.04.900].

30 * Sec. 56. AS 46.40.210(12) is amended to read:

31 (12) "uses of state concern" means those land and water uses that

1 would significantly affect the long-term public interest; "uses of state concern" include

2 (A) uses of national interest, including the use of resources for
3 the siting of ports and major facilities that contribute to meeting national
4 energy needs, construction and maintenance of navigational facilities and
5 systems, resource development of federal land, and national defense and
6 related security facilities that are dependent upon coastal locations;

7 (B) uses of more than local concern, including those land and
8 water uses that confer significant environmental, social, cultural, or economic
9 benefits or burdens beyond a single coastal resource district;

10 (C) the siting of major energy facilities, activities pursuant to a
11 state oil and gas lease, a state gas only lease, or a federal oil and gas lease, or
12 large-scale industrial or commercial development activities that are dependent
13 on a coastal location and that, because of their magnitude or the magnitude of
14 their effect on the economy of the state or the surrounding area, are reasonably
15 likely to present issues of more than local significance;

16 (D) facilities serving statewide or interregional transportation
17 and communication needs; and

18 (E) uses in areas established as state parks or recreational areas
19 under AS 41.21 or as state game refuges, game sanctuaries, or critical habitat
20 areas under AS 16.20.

21 * **Sec. 57.** AS 31.05.170(14); AS 38.05.177(b), 38.05.177(c), 38.05.177(e), 38.05.177(f),
22 38.05.177(g), 38.05.177(h), 38.05.177(j), 38.05.177(k), 38.05.177(m), 38.05.177(o); and
23 AS 46.04.900(25) are repealed.

24 * **Sec. 58.** The uncodified law of the State of Alaska is amended by adding a new section to
25 read:

26 CERTAIN SHALLOW NATURAL GAS LEASES AND LEASE APPLICATIONS
27 TO BE ADMINISTERED UNDER FORMER LAW. The provisions of AS 38.05.177(a),
28 (d)(1), and (l), amended by secs. 26 - 28 of this Act, as those provisions read on the day
29 before the effective date of amendment of those subsections, and the provisions of
30 AS 38.05.177(b), (c), (e) - (h), (j), (k), (m), and (o), repealed by sec. 57 of this Act, as those
31 provisions read on the day before the effective date of the repeal of those subsections, apply to

1 shallow natural gas

2 (1) leases issued under AS 38.05.177 and in effect on December 31, 2003; and

3 (2) lease applications under AS 38.05.177 that were received by the

4 Department of Natural Resources before January 1, 2004.

5 * Sec. 59. This Act takes effect immediately under AS 01.10.070(c).

23-LS1818U
Chenoweth
4/12/04

CS FOR HOUSE BILL NO. 531(RES)

IN THE LEGISLATURE OF THE STATE OF ALASKA
TWENTY-THIRD LEGISLATURE - SECOND SESSION

BY THE HOUSE RESOURCES COMMITTEE

**Offered:
Referred:**

Sponsor(s): HOUSE RESOURCES COMMITTEE

A BILL

FOR AN ACT ENTITLED

1 **"An Act relating to natural gas exploration and development and to nonconventional**
2 **gas, and amending the section under which shallow natural gas leases may be issued;**
3 **and providing for an effective date."**

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

5 *** Section 1.** AS 14.40.365(a) is amended to read:

6 (a) The University of Alaska may select and is entitled to receive the
7 conveyance of not less than 250,000 and not more than 260,000 acres of land
8 conveyed to the state under sec. 6(b) of the Alaska Statehood Act (P.L. 85-508, 72
9 Stat. 339). The Board of Regents of the University of Alaska shall periodically submit
10 a list of selections to the commissioner of natural resources and, if the list of selections
11 contains land within the boundaries of a municipality, the Board of Regents of the
12 University of Alaska shall submit the list to the municipality. The Board of Regents
13 and the commissioner of natural resources shall periodically and jointly submit to the
14 legislature, within 30 days of the beginning of a regular legislative session, a list of the

1 selections of land proposed to be conveyed by the state to the University of Alaska
2 under this section. If the list submitted to the legislature contains land within the
3 boundaries of a municipality, the Board of Regents and the commissioner of natural
4 resources shall provide a copy of the list to the municipality. Each list must contain
5 not more than 25 percent of the total acres of land to which the university is entitled
6 after subtracting previous conveyances under this section, but not less than 25,000
7 acres or the remaining entitlement under this section, whichever is less. A list of
8 selections submitted shall be considered approved for conveyance to the University of
9 Alaska unless the legislature acts to disapprove the list during the legislative session
10 during which the list was submitted. If the amount of land to be conveyed exceeds the
11 balance due the university under this section, the university shall set out the land to be
12 conveyed in priority order. Land may not be selected if, on the date of its selection by
13 the university, it

14 (1) is identified in AS 16.20, AS 41.15.300 - 41.15.330, or AS 41.21 or
15 has been reserved by law from the public domain;

16 (2) is located within a municipality unless the land is vacant,
17 unappropriated, unreserved land; if land included on the list of selections is selected
18 by the municipality with remaining selection rights under AS 29.65 within 120 days of
19 receiving the Board of Regents' list of selections under this subsection, the university
20 may not select the land unless a binding agreement between the university and the
21 municipality is negotiated to allow the selection; if the municipal selection is
22 disapproved, in whole or in part, the university may select the land, or any available
23 portion of the land, and that selection will relate back to the date of the Board of
24 Regents' list of selections under this subsection and shall have priority over all other
25 selections or claims made subsequent to that notice; in this paragraph, "vacant,
26 unappropriated, unreserved land" has the meaning given in AS 29.65.130;

27 (3) is land

28 (A) included in a five-year proposed [OIL AND GAS] leasing
29 program under AS 38.05.180(b); or

30 (B) leased under, or for which a lease application is pending
31 under, AS 38.05.180(d) or 38.05.150;

- 1 (4) is subject to
2 (A) an oil, gas, or coal lease, or coal prospecting permit;
3 (B) a mining claim, offshore prospecting permit, a prospecting
4 site, an upland mining lease, or a mining leasehold location;
5 (5) is necessary to carry out the purpose of an interagency land
6 management agreement; or
7 (6) is subject to conveyance under a land exchange or land settlement
8 agreement.

9 * **Sec. 2.** AS 14.40.365(e) is amended to read:

10 (e) The list of selections of land submitted to the legislature may not include a
11 land selection made by the University of Alaska under this section if the commissioner
12 of natural resources determines in writing that the proposed selection

13 (1) includes land that the commissioner, in consultation with the
14 commissioner of fish and game, determines has demonstrated value to the public as a
15 habitat area that is especially critical to the perpetuation of fish or wildlife;

16 (2) includes land for which, at the time of its selection under this
17 section, a municipality has made a selection under AS 29.65 unless the land selection
18 is, at a later date, rejected by the commissioner of natural resources or relinquished by
19 the municipality;

20 (3) includes land that the commissioner reasonably believes may be
21 selected by a newly formed municipality under AS 29.65.030, but the commissioner
22 may not withhold selection under this paragraph for more than three years after the
23 municipality's incorporation;

24 (4) includes land within the boundaries of a municipality, the
25 municipality has a remaining entitlement under AS 29.65, and the municipality selects
26 the land under AS 29.65 within 120 days after receipt by the municipality of the Board
27 of Regents' list of selections under (a) of this section;

28 (5) includes land that, at the time of its selection under this section,

29 (A) is subject to an [OIL AND GAS] exploration license
30 issued under AS 38.05.131 - 38.05.134; or

31 (B) the commissioner reasonably believes will be made part of

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an [OIL AND GAS] exploration license issued under AS 38.05.131 - 38.05.134; the commissioner may not refuse to convey title to land to the University of Alaska under this subparagraph for more than two years after its first selection by the University of Alaska; or

(6) includes land the commissioner of natural resources reasonably believes would not be in the best interests of the state to convey outside of state ownership.

* Sec. 3. AS 19.40.200(b) is amended to read:

(b) The prohibition on disposal of state land under (a) of this section does not apply to a disposal

(1) to a licensed public utility or a licensed common carrier under AS 38.05.810(e);

(2) for the reauthorization of leases that were in effect on January 1, 1994, for nonresidential purposes within the following development nodes:

(A) Coldfoot:

Township 28 North, Range 12 West, Fairbanks Meridian

Sections 3 - 4

Sections 9 - 10

Sections 15 - 16

Sections 20 - 22

(B) Yukon River Crossing:

Township 12 North, Range 10 West, Fairbanks Meridian

Sections 6 - 7

Township 12 North, Range 11 West, Fairbanks Meridian

Sections 1 - 2

Section 12

Township 13 North, Range 10 West, Fairbanks Meridian

Sections 29 - 32

Township 13 North, Range 11 West, Fairbanks Meridian

Section 22

Sections 25 - 27

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Sections 34 - 36

(3) for nonresidential development within the following development

nodes:

(A) Deadhorse:

Township 10 North, Range 14 East, Umiat Meridian

Township 10 North, Range 15 East, Umiat Meridian

Section 8

Sections 17 - 20

Section 30

(B) Coldfoot:

Township 28 North, Range 12 West, Fairbanks Meridian

Sections 3 - 4

Sections 9 - 10

Sections 15 - 16

Sections 20 - 22

Township 29 North, Range 12 West, Fairbanks Meridian

Sections 23 - 27

Sections 34 - 35

(C) Franklin Bluffs:

Township 4 North, Range 14 East, Umiat Meridian

Sections 3 - 4

Sections 9 - 10

Sections 15 - 16

(D) Happy Valley:

Township 3 South, Range 14 East, Umiat Meridian

Sections 19 - 20

Sections 29 - 30

(E) Yukon River Crossing:

Township 12 North, Range 10 West, Fairbanks Meridian

Sections 6 - 7

Township 12 North, Range 11 West, Fairbanks Meridian

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Sections 1 - 2

Section 12

Township 13 North, Range 10 West, Fairbanks Meridian

Sections 29 - 32

Township 13 North, Range 11 West, Fairbanks Meridian

Section 22

Sections 25 - 27

Sections 34 - 36; or

(4) necessary for

(A) an oil and gas lease or gas only lease under AS 38.05.180;

(B) exploration, development, production, or transportation of oil and gas north of 68 degrees north latitude; or

(C) a state lease or materials sale for

(i) exploration, development, production, or transportation of oil or [AND] gas;

(ii) reconstruction or maintenance of state highways; or

(iii) construction or maintenance of airports.

* Sec. 4. AS 31.05.030(j) is amended to read:

(j) For exploration and development operations involving nonconventional gas, the commission

(1) may not

(A) issue a permit to drill under this chapter if the well would be used to produce gas from an aquifer that serves as a source of water for human consumption or agricultural purposes unless the commission finds that the well will not adversely affect the aquifer as a source of water for human consumption or agricultural purposes; or

(B) allow injection of produced water except at depths below known sources of water for human consumption or agricultural purposes;

(2) shall

(A) regulate hydraulic fracturing in nonconventional gas

1 wells to assure protection of drinking water quality;

2 (B) regulate the disposal of wastes produced from the
3 operations unless the disposal is otherwise subject to regulation by the
4 Department of Environmental Conservation or the Environmental
5 Protection Agency; and

6 (C) for the purposes of AS 46.04.030(b), [THE
7 COMMISSION SHALL] determine whether a well drilled for
8 nonconventional [SHALLOW NATURAL] gas may penetrate a formation
9 capable of flowing oil and, if so, whether the volume of oil encountered will be
10 of such quantities that an oil discharge prevention and contingency plan will be
11 required.

12 * Sec. 5. AS 31.05.060(c) is amended to read:

13 (c) Notwithstanding the requirements of (a) and (b) of this section that relate
14 to fixing a date for a hearing and causing notice of the hearing to be given, for an
15 action under this chapter that involves the exploration for or development of
16 nonconventional [SHALLOW NATURAL] gas and that has application to a single
17 well or a single field, upon the request of a lessee or operator, the commission may,
18 where operations might be unduly delayed, approve a variance from the commission's
19 regulations that apply to the well or field without providing notice and opportunity to
20 be heard. In the exercise of its authority to issue the variance,

21 (1) the commission may approve the variance if

22 (A) the approval provides at least an equally effective means of
23 accomplishing the requirement set out in the commission's regulation; or

24 (B) the commission determines that the request is more
25 appropriate to the proposed operation than compliance with the requirement of
26 the regulation; and

27 (2) the terms of the approval of the variance may include exempting
28 the lessee or operator from a requirement of a regulation if the commission determines
29 that the requirement is not necessary or not suited to the well or field taking into
30 consideration

31 (A) the nature of the operation involved;

1 (B) the characteristics of the well or field for which the
2 variance is sought; and

3 (C) the reasonably anticipated risks of the exemption from the
4 requirement to human safety and the environment.

5 * Sec. 6. AS 31.05.125 is amended to read:

6 **Sec. 31.05.125. Regulation of nonconventional [SHALLOW NATURAL]
7 gas; relationship of chapter to other laws.** If the Department of Natural Resources
8 clearly demonstrates an overriding state interest, the commissioner of natural
9 resources may approve a waiver of local planning authority approval and requirements
10 relating to compliance of a nonconventional gas lease with local ordinances and
11 regulations. The commissioner shall issue specific findings giving reasons for
12 granting a waiver under this section.

13 * Sec. 7. AS 31.05.170 is amended by adding a new paragraph to read:

14 (16) "nonconventional gas" has the meaning given in AS 38.05.965.

15 * Sec. 8. AS 36.30.850(b)(25) is amended to read:

16 (25) acquisition of confidential seismic survey data necessary for pre-
17 sale oil and gas lease or gas only lease analyses under AS 38.05.180;

18 * Sec. 9. AS 36.30.850(b)(33) is amended to read:

19 (33) contracts between the Department of Natural Resources and
20 contractors qualified to evaluate hydrocarbon development, production, transportation,
21 and economics, to assist the commissioner of natural resources in evaluating
22 applications for [OIL AND GAS] royalty increases or decreases or other [OIL AND
23 GAS] royalty adjustments, and evaluating the related financial and technical data,
24 entered into under AS 38.05.180(j);

25 * Sec. 10. AS 38.04.065(i) is amended to read:

26 (i) An oil and gas lease sale or gas only lease sale is not subject to this
27 section. Oil and gas lease sales and gas only lease sales are subject to the planning
28 process established under AS 38.05.180.

29 * Sec. 11. AS 38.05.035(e) is amended to read:

30 (e) Upon a written finding that the interests of the state will be best served, the
31 director may, with the consent of the commissioner, approve contracts for the sale,

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lease, or other disposal of available land, resources, property, or interests in them. In approving a contract under this subsection, the director need only prepare a single written finding. In addition to the conditions and limitations imposed by law, the director may impose additional conditions or limitations in the contracts as the director determines, with the consent of the commissioner, will best serve the interests of the state. The preparation and issuance of the written finding by the director are subject to the following:

(1) with the consent of the commissioner and subject to the director's discretion, for a specific proposed disposal of available land, resources, or property, or of an interest in them, the director, in the written finding,

(A) shall establish the scope of the administrative review on which the director's determination is based, and the scope of the written finding supporting that determination; the scope of the administrative review and finding may address only reasonably foreseeable, significant effects of the uses proposed to be authorized by the disposal;

(B) may limit the scope of an administrative review and finding for a proposed disposal to

(i) applicable statutes and regulations;

(ii) the facts pertaining to the land, resources, or property, or interest in them, that the director finds are material to the determination and that are known to the director or knowledge of which is made available to the director during the administrative review; and

(iii) issues that, based on the statutes and regulations referred to in (i) of this subparagraph, on the facts as described in (ii) of this subparagraph, and on the nature of the uses sought to be authorized by the disposal, the director finds are material to the determination of whether the proposed disposal will best serve the interests of the state; and

(C) may, if the project for which the proposed disposal is sought is a multiphased development, limit the scope of an administrative review and finding for the proposed disposal to the applicable statutes and

1 regulations, facts, and issues identified in (B)(i) - (iii) of this paragraph that
2 pertain solely to the disposal phase of the project when

3 (i) the only uses to be authorized by the proposed
4 disposal are part of that phase;

5 (ii) the disposal is a [AN OIL AND GAS] disposal of
6 oil and gas, or of gas only, and, before the next phase of the project
7 may proceed, public notice and the opportunity to comment are
8 provided under regulations adopted by the department unless the
9 project is subject to a consistency review under AS 46.40 and public
10 notice and the opportunity to comment are provided under
11 AS 46.40.096(c);

12 (iii) the department's approval is required before the
13 next phase of the project may proceed; and

14 (iv) the department describes its reasons for a decision
15 to phase;

16 (2) the director shall discuss in the written finding prepared and issued
17 under this subsection the reasons that each of the following was not material to the
18 director's determination that the interests of the state will be best served:

19 (A) facts pertaining to the land, resources, or property, or an
20 interest in them other than those that the director finds material under (1)(B)(ii)
21 of this subsection; and

22 (B) issues based on the statutes and regulations referred to in
23 (1)(B)(i) of this subsection and on the facts described in (1)(B)(ii) of this
24 subsection;

25 (3) a written finding for an oil and gas lease sale or gas only lease sale
26 under AS 38.05.180 is subject to (g) of this section;

27 (4) a contract for the sale, lease, or other disposal of available land or
28 an interest in land is not legally binding on the state until the commissioner approves
29 the contract, but if the appraised value is not greater than \$50,000 in the case of the
30 sale of land or an interest in land, or \$5,000 in the case of the annual rental of land or
31 interest in land, the director may execute the contract without the approval of the

1 commissioner;

2 (5) public notice requirements relating to the sale, lease, or other
3 disposal of available land or an interest in land for oil and gas, or for gas only,
4 proposed to be scheduled in the five-year oil and gas leasing program under
5 AS 38.05.180(b), except for a sale under (6)(F) of this subsection, are as follows:

6 (A) before a public hearing, if held, or in any case not less than
7 180 days before the sale, lease, or other disposal of available land or an interest
8 in land, the director shall make available to the public a preliminary written
9 finding that states the scope of the review established under (1)(A) of this
10 subsection and includes the applicable statutes and regulations, the material
11 facts and issues in accordance with (1)(B) of this subsection, and information
12 required by (g) of this section, upon which the determination that the sale,
13 lease, or other disposal will serve the best interests of the state will be based;
14 the director shall provide opportunity for public comment on the preliminary
15 written finding for a period of not less than 60 days;

16 (B) after the public comment period for the preliminary written
17 finding and not less than 90 days before the sale, lease, or other disposal of
18 available land or an interest in land for oil and gas or for gas only, the director
19 shall make available to the public a final written finding that states the scope of
20 the review established under (1)(A) of this subsection and includes the
21 applicable statutes and regulations, the material facts and issues in accordance
22 with (1) of this subsection, and information required by (g) of this section,
23 upon which the determination that the sale, lease, or other disposal will serve
24 the best interests of the state is based;

25 (6) before a public hearing, if held, or in any case not less than 21 days
26 before the sale, lease, or other disposal of available land, property, resources, or
27 interests in them other than a sale, lease, or other disposal of available land or an
28 interest in land for oil and gas or for gas only under (5) of this subsection, the director
29 shall make available to the public a written finding that, in accordance with (1) of this
30 subsection, sets out the material facts and applicable statutes and regulations and any
31 other information required by statute or regulation to be considered upon which the

1 determination that the sale, lease, or other disposal will best serve the interests of the
2 state was based; however, a written finding is not required before the approval of

3 (A) a contract for a negotiated sale authorized under
4 AS 38.05.115;

5 (B) a lease of land for a shore fishery site under AS 38.05.082;

6 (C) a permit or other authorization revocable by the
7 commissioner;

8 (D) a mineral claim located under AS 38.05.195;

9 (E) a mineral lease issued under AS 38.05.205;

10 (F) an exempt oil and gas lease sale or gas only lease sale
11 under AS 38.05.180(d) of acreage subject to a best interest finding issued
12 within the previous 10 years or a reoffer oil and gas lease sale or gas only
13 lease sale under AS 38.05.180(w) of acreage subject to a best interest finding
14 issued within the previous 10 years, unless the commissioner determines that
15 substantial new information has become available that justifies a supplement to
16 the most recent best interest finding for the exempt oil and gas lease sale or
17 gas only lease sale acreage and for the reoffer oil and gas lease sale or gas
18 only lease sale acreage; however, for each oil and gas lease sale or gas only
19 lease sale described in this subparagraph, the director shall call for comments
20 from the public; the director's call for public comments must provide
21 opportunity for public comment for a period of not less than 30 days; if the
22 director determines that a supplement to the most recent best interest finding
23 for the acreage is required under this subparagraph,

24 (i) the director shall issue the supplement to the best
25 interest finding not later than 90 days before the sale;

26 (ii) not later than 45 days before the sale, the director
27 shall issue a notice describing the interests to be offered, the location
28 and time of the sale, and the terms and conditions of the sale; and

29 (iii) the supplement has the status of a final written best
30 interest finding for purposes of (i) and (j) of this section;

31 (G) [A SHALLOW GAS LEASE AUTHORIZED UNDER

1 AS 38.05.177 IN AN AREA FOR WHICH LEASING IS AUTHORIZED
2 UNDER AS 38.05.177;

3 (H)] a surface use lease under AS 38.05.255;

4 (H) [(I)] a permit, right-of-way, or easement under
5 AS 38.05.850;

6 (7) the director shall include in

7 (A) a preliminary written finding, if required, a summary of
8 agency and public comments, if any, obtained as a result of contacts with other
9 agencies concerning a proposed disposal or as a result of informal efforts
10 undertaken by the department to solicit public response to a proposed disposal,
11 and the department's preliminary responses to those comments; and

12 (B) the final written finding a summary of agency and public
13 comments received and the department's responses to those comments.

14 * S.c. 12. AS 38.05.035(g) is amended to read:

15 (g) Notwithstanding (e)(1)(A) and (B) of this section, when the director
16 prepares a written finding required under (e) of this section for an oil and gas lease
17 sale or a gas only lease sale scheduled under AS 38.05.180, the director shall consider
18 and discuss

19 (1) in a preliminary or final written finding facts that are known to the
20 director at the time of preparation of the finding and that are

21 (A) material to issues that were raised during the period
22 allowed for receipt of public comment, whether or not material to a matter set
23 out in (B) of this paragraph, and within the scope of the administrative review
24 established by the director under (e)(1) of this section; or

25 (B) material to the following matters:

26 (i) property descriptions and locations;

27 (ii) the petroleum potential of the sale area, in general
28 terms;

29 (iii) fish and wildlife species and their habitats in the
30 area;

31 (iv) the current and projected uses in the area, including

1 uses and value of fish and wildlife;

2 (v) the governmental powers to regulate the [OIL AND
3 GAS] exploration, development, production, and transportation of oil
4 and gas or of gas only;

5 (vi) the reasonably foreseeable cumulative effects of
6 [OIL AND GAS] exploration, development, production, and
7 transportation for oil and gas or for gas only on the sale area,
8 including effects on subsistence uses, fish and wildlife habitat and
9 populations and their uses, and historic and cultural resources;

10 (vii) lease stipulations and mitigation measures,
11 including any measures to prevent and mitigate releases of oil and
12 hazardous substances, to be included in the leases, and a discussion of
13 the protections offered by these measures;

14 (viii) the method or methods most likely to be used to
15 transport oil or gas from the lease sale area, and the advantages,
16 disadvantages, and relative risks of each;

17 (ix) the reasonably foreseeable fiscal effects of the lease
18 sale and the subsequent activity on the state and affected municipalities
19 and communities, including the explicit and implicit subsidies
20 associated with the lease sale, if any;

21 (x) the reasonably foreseeable effects of [OIL AND
22 GAS] exploration, development, production, and transportation
23 involving oil and gas or gas only on municipalities and communities
24 within or adjacent to the lease sale area; and

25 (xi) the bidding method or methods adopted by the
26 commissioner under AS 38.05.180; and

27 (2) the basis for the director's preliminary or final finding, as
28 applicable, that, on balance, leasing the area would be in the state's best interest.

29 * Sec. 13. AS 38.05.036(a) is amended to read:

30 (a) The department may conduct audits regarding royalty and net profits under
31 oil and gas contracts, agreements, or leases under this chapter and regarding costs

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related to [OIL AND GAS] exploration licenses entered into under AS 38.05.131 - 38.05.134 and exploration incentive credits under this chapter or under AS 41.09. For purposes of audit under this section,

(1) the department may examine the books, papers, records, or memoranda of a person regarding matters related to the audit; and

(2) the records and premises where a business is conducted shall be open at all reasonable times for inspection by the department.

* Sec. 14. AS 38.05.127(e) is amended to read:

(e) The establishment of easements or rights-of-way for oil and gas, gas only, and mineral leases under (a) of this section need not be made until the leases are ready to be developed.

* Sec. 15. AS 38.05.131(a) is amended to read:

(a) Unless specifically provided otherwise in AS 38.05.132 - 38.05.134, the provisions of AS 38.05.005 - 38.05.037, 38.05.140(f), 38.05.180, 38.05.182 - 38.05.184, and 38.05.920 - 38.05.990 apply to the issuance of [OIL AND GAS] exploration licenses and leases for oil and gas, or for gas only, as appropriate, under AS 38.05.132 - 38.05.134.

* Sec. 16. AS 38.05.132(a) is amended to read:

(a) To encourage exploration for oil and gas on state land, the commissioner may issue [OIL AND GAS] exploration licenses. The commissioner may limit the exploration licenses under AS 38.05.132 - 38.05.134 to exploration for and recovery of gas only.

* Sec. 17. AS 38.05.132(b) is amended to read:

(b) An [OIL AND GAS] exploration license issued under this section gives the licensee

(1) the exclusive right to explore, for a term not to exceed 10 years, [FOR DEPOSITS OF OIL AND GAS] on unleased state land described in the exploration license for deposits of oil and gas, or for deposits of gas only, as appropriate, unless the exploration license is terminated under (d)(1) of this section or the land is earlier relinquished, removed, or deleted under (d)(2) of this section; and

(2) unless the exploration license is terminated under (d)(1) of this

1 section, the option to convert the exploration license for all or part of the state land,
2 except the land that is deleted or removed from the land described in the exploration
3 license under (d)(2) of this section, into an oil and gas lease, or a gas lease only, as
4 appropriate, upon fulfillment of the work commitments contained in the exploration
5 license.

6 * Sec. 18. AS 38.05.132(c) is amended to read:

7 (c) An exploration license awarded under this section

8 (1) is not subject to the acreage limitations imposed by
9 AS 38.05.140(c) or 38.05.180(m);

10 (2) may cover, subject to the maximum acreage limitation on
11 exploration licenses by one licensee under AS 38.05.131(e), an area of not less than
12 10,000 acres and not more than 500,000 acres, that must be reasonably compact and
13 contiguous;

14 (3) must be conditioned upon an obligation to perform a specified
15 work commitment, in total for the term of the license, expressed in dollars of direct
16 exploration expenditures; the specified work commitment

17 (A) may include a provision that adjusts the total amount of
18 work commitment, expressed in dollars of direct exploration expenditures, to
19 account for inflation;

20 (B) must include a requirement that the licensee complete at
21 least 25 percent of the licensee's total specified work commitment by the fourth
22 anniversary of the effective date of the issuance of the [OIL AND GAS]
23 exploration license;

24 (4) must be conditioned upon the posting of a bond or other security
25 acceptable to the commissioner, in favor of the state and subject to the following
26 requirements:

27 (A) the bond or other security must be renewed annually;

28 (B) the annual bond or other security shall be calculated as the
29 entire work commitment expressed in dollars, less the cumulative direct
30 exploration expenditures of the licensee as of the last day of the most recent
31 project year, divided by the number of years remaining in the term of the

1 exploration license;

2 (5) is subject to an annual review and revocation if the commissioner
3 determines that the licensee has failed to provide or maintain in effect the bond or
4 other security required by (4) of this subsection;

5 (6) must be conditioned upon the licensee's payment to the state of a
6 nonrefundable [OIL AND GAS] exploration license fee of \$1 for each acre of land or
7 fraction of each acre that is subject to the exploration license; and

8 (7) must be conditioned upon an agreement that exploration
9 expenditures are subject to audit by the commissioner.

10 * Sec. 19. AS 38.05.132(f) is amended to read:

11 (f) In this section,

12 (1) "direct exploration expenditure" means cash expenses undertaken
13 in performance of a specified work commitment under the provisions of AS 38.05.131
14 - 38.05.134 and necessarily incurred by the licensee in the permitting, mobilization,
15 conducting, demobilization, and evaluation of geophysical and geological surveys, or
16 the drilling, logging, coring, testing, and evaluation of oil and gas or gas only wells;
17 the term

18 (A) includes direct labor costs, including the cost of benefits,
19 for employees directly associated with the work commitment programs, the
20 cost of renting or leasing equipment from parties not affiliated with the
21 licensee, the reasonable costs of maintaining and operating equipment,
22 payments to consultants and independent contractors not affiliated with the
23 licensee, and costs of materials and supplies;

24 (B) does not include noncash expenses such as depreciation
25 and reserves, interest or other costs of borrowed funds, return on investment,
26 overhead, insurance or bond premiums, or any other expense that is
27 unreasonable or that the licensee has not incurred to satisfy the licensee's work
28 commitment;

29 (2) "work commitment" includes the drilling of one or more
30 exploration wells or the gathering of data from activities described in (1) of this
31 subsection, or both.

1 * **Sec. 20.** AS 38.05.133(a) is amended to read:

2 (a) The procedures in this section apply to the issuance of an [OIL AND GAS]
3 exploration license under AS 38.05.132.

4 * **Sec. 21.** AS 38.05.133(f) is amended to read:

5 (f) After considering proposals not rejected under (d) of this section and public
6 comment on those proposals, the commissioner shall issue a written finding
7 addressing all matters set out in AS 38.05.035(e) and (g), except for
8 AS 38.05.035(g)(1)(B)(xi). If the finding concludes that the state's best interests
9 would be served by issuing an [OIL AND GAS] exploration license, the finding must
10 (1) describe the limitations, stipulations, conditions, or changes from the initiating
11 proposal or competing proposals that are required to make the issuance of the
12 exploration license conform to the best interests of the state, and (2) if only one
13 proposal was submitted, identify the prospective licensee whom the commissioner
14 finds should be issued the exploration license. The commissioner shall attach to the
15 finding a copy of the exploration license to be issued and the form of lease that will be
16 used for any portion of the exploration license area subsequently converted to a [AN
17 OIL AND GAS] lease under AS 38.05.134.

18 * **Sec. 22.** AS 38.05.133(h) is amended to read:

19 (h) If competing proposals are submitted, and the commissioner's finding
20 under (f) of this section concludes that an [OIL AND GAS] exploration license should
21 be issued, the commissioner shall issue a request for competitive sealed bids, under
22 procedures adopted by the commissioner by regulation, to determine which
23 prospective licensee should be issued the exploration license. The finding provided to
24 the prospective licensees and the public under (f) of this section must contain notice
25 that (1) the commissioner intends to request competitive sealed bids, (2) a prospective
26 licensee who intends to participate in the bidding must notify the commissioner in
27 writing by the date specified in the notice, and (3) a prospective licensee's notice of
28 intent to participate in the bidding constitutes acceptance of issuance of the
29 exploration license, as limited or conditioned by the terms contained in the finding and
30 by the exploration license to be issued and the form of lease to be used that have been
31 attached to that finding, if the prospective licensee is the successful bidder. The

1 successful bidder is the prospective licensee who submits the highest bid in terms of
2 the minimum work commitment dollar amount.

3 * **Sec. 23.** AS 38.05.134 is amended to read:

4 **Sec. 38.05.134. Conversion to lease.** If the licensee requests and the
5 commissioner determines that the work commitment obligation set out in an [OIL
6 AND GAS] exploration license issued under AS 38.05.132 has been met, the
7 commissioner shall convert to one or more [OIL AND GAS] leases all or part, as the
8 licensee may indicate, of the area described in the exploration license that remains
9 after the relinquishments, removals, or deletions required by AS 38.05.132(d)(2). A
10 lease issued under this section

11 (1) is subject to the acreage limitations imposed by AS 38.05.140(c);

12 (2) is subject to AS 38.05.180(j) - (m), (o) - (u), and (x) - (z);

13 (3) must be conditioned upon a royalty in amount or value of not less
14 than 12.5 percent of production, except that

15 (A) the lessee who, proceeding under AS 38.05.131 -
16 38.05.134, under a lease issued in the Cook Inlet sedimentary basin who is the
17 first to file with the commissioner a nonconfidential sworn statement claiming
18 to be the first to have drilled a well discovering oil or gas in a previously
19 undiscovered oil or gas pool and who is certified by the commissioner within
20 one year of completion of that discovery well to have drilled a well in that pool
21 that is capable of producing in paying quantities shall pay a royalty of five
22 percent on all production of oil or gas from that pool attributable to that lease
23 for a period of 10 years following the date of discovery of that pool, and
24 thereafter the royalty payable on all production of oil or gas from the pool
25 attributable to that lease shall be determined and payable as specified in the
26 lease; t' ayment of the five percent royalty under this paragraph is
27 authorized only to a holder of a lease who meets the requirements of
28 AS 38.05.180(f)(4); and

29 (B) for nonconventional gas that is not produced in direct
30 competition with gas on which a royalty at a rate of at least 12.5 percent is
31 payable, if the licensee requests, the commissioner may negotiate with the

1 licensee and set a royalty rate for the gas of at least 6.25 percent; for
2 purposes of this subparagraph, "nonconventional gas" has the meaning
3 given in AS 38.05.965;

4 (4) must include an annual rent of \$3 per acre or fraction of an acre
5 initially paid to the state at inception of the lease and payable annually after that until
6 the income to the state from royalty under that lease exceeds the rental income to the
7 state under that lease for that year; and

8 (5) is subject to other conditions and obligations that are specified in
9 the lease.

10 * Sec. 24. AS 38.05.140(a) is amended to read:

11 (a) A person may not take or hold coal leases or permits during the life of coal
12 leases on state land exceeding an aggregate of 92,160 acres, except that a person may
13 apply for coal leases or permits for acreage in addition to 92,160 acres, not exceeding
14 a total of 5,120 additional acres of state land. The additional area applied for shall be
15 in multiples of 40 acres, and the application shall contain a statement that the granting
16 of a lease for additional land is necessary for the person to carry on business
17 economically and is in the public interest. On the filing of the application, [EXCEPT
18 AS PROVIDED BY AS 38.05.177(a)(2)(C),] the coal deposits in the land covered by
19 the application shall be temporarily set aside and withdrawn from all other forms of
20 disposal provided under AS 38.05.135 - 38.05.181.

21 * Sec. 25. AS 38.05.140(f) is amended to read:

22 (f) The submerged and shoreland lying north of 57 degrees, 30 minutes, North
23 [NORTH] latitude and east of 159 degrees, 49 minutes, West [WEST] longitude
24 within the Bristol Bay drainage are designated as the Bristol Bay Fisheries Reserve.
25 Within the Bristol Bay Fisheries Reserve, a [NO] surface entry permit to develop an
26 oil or gas lease or an [OIL AND GAS] exploration license under AS 38.05.131 -
27 38.05.134 may not be issued on state owned or controlled land until the legislature by
28 appropriate resolution specifically finds that the entry will not constitute danger to the
29 fishery.

30 * Sec. 26. AS 38.05.150(f) is amended to read:

31 (f) A [NOTWITHSTANDING AS 38.05.177, A] lease entered into under this

1 section gives the lessee the right to vent or remove methane and other gas held in
2 association with the coal in the land covered by the lease to ensure safe coal mining
3 operations.

4 * Sec. 27. AS 38.05.177(a) is amended to read:

5 (a) The provisions of this section

6 [(1)] apply to nonconventional gas [, WHETHER METHANE
7 ASSOCIATED WITH AND DERIVED FROM COAL DEPOSITS OR
8 OTHERWISE, FROM A FIELD IF A PART OF THE FIELD IS WITHIN 3,000
9 FEET OF THE SURFACE; AND

10 (2) DO NOT APPLY TO AUTHORIZE LEASE OF

11 (A) LAND

12 (i) THAT IS SUBJECT TO AN OIL AND GAS
13 EXPLORATION LICENSE OR LEASE ISSUED UNDER
14 AS 38.05.131 - 38.05.134; OR

15 (ii) THAT IS LEASED UNDER AS 38.05.180;

16 (B) THE LAND (i) THAT IS PROPOSED TO BE SUBJECT
17 TO AN OIL AND GAS EXPLORATION LICENSE OR LEASE ISSUED
18 UNDER AS 38.05.131 - 38.05.134; OR (ii) THAT IS DESCRIBED IN AND
19 PART OF A PROPOSED OIL AND GAS LEASING PROGRAM
20 PREPARED UNDER AS 38.05.180(b); HOWEVER, THE COMMISSIONER
21 MAY WAIVE THE LIMITATIONS OF THIS SUBPARAGRAPH;

22 (C) THE LAND THAT IS HELD UNDER A COAL LEASE
23 ENTERED INTO UNDER AS 38.05.150, UNLESS THE APPLICANT FOR
24 A SHALLOW NATURAL GAS LEASE IS ALSO THE LESSEE UNDER
25 AS 38.05.150 OF THAT LAND; OR

26 (D) THE VALID EXISTING SELECTIONS OF THE
27 ALASKA MENTAL HEALTH TRUST AUTHORITY MADE FOR THE
28 PURPOSE OF RECONSTITUTING THE MENTAL HEALTH TRUST
29 ESTABLISHED UNDER THE ALASKA MENTAL HEALTH ENABLING
30 ACT, P.L. 84-830, 70 STAT. 709 (1956), THAT BECOME SUBJECT TO
31 MANAGEMENT UNDER AS 38.05.801, OR OF LAND THAT HAS BEEN

1 DESIGNATED BY LAW FOR OR IS SUBJECT TO DESIGNATION FOR
2 CONVEYANCE TO THE ALASKA MENTAL HEALTH TRUST
3 AUTHORITY; HOWEVER, AFTER CONSULTATION WITH THE
4 ALASKA MENTAL HEALTH TRUST AUTHORITY, THE
5 COMMISSIONER MAY WAIVE THE LIMITATIONS OF THIS
6 SUBPARAGRAPH].

7 * Sec. 28. AS 38.05.177(d) is amended to read:

8 (d) A lease

9 (1) shall be automatically extended if and for so long thereafter as gas
10 is produced in paying quantities from the lease and the lessee continues to meet all
11 requirements of the lease; a [. A] lease issued under this section covering land on
12 which there is a well capable of producing gas in paying quantities does not expire
13 because the lessee fails to produce gas unless the lessee is allowed reasonable time to
14 place the well on a producing status; if [. IF] drilling has commenced on the
15 expiration date of the primary term of the lease and is continued with reasonable
16 diligence, including such operations as redrilling, sidetracking, or other means
17 necessary to reach the originally proposed bottom hole location, the lease is extended
18 for one year and for so long thereafter as gas is produced in paying quantities; a [. A]
19 gas lease issued under this section that is subject to termination by reason of cessation
20 of production does not terminate if, within 90 days after production ceases or a longer
21 period determined at the discretion of the director, reworking or drilling operations are
22 commenced on the land under lease and are thereafter conducted with reasonable
23 diligence during the period of nonproduction;

24 (2) issued under former (c) of this section before January 1, 2004,
25 may be extended at the discretion of the director; a lease may be extended under
26 this paragraph [. IN ADDITION,] upon application by the lessee; [,] the director
27 may once extend the [A] lease [ISSUED UNDER (c) OF THIS SECTION] for a
28 period of not more than three years; in exercising discretion to extend a lease under
29 this paragraph, the director may not extend the lease unless the director
30 considers

31 (A) the extent of the shallow natural gas exploration

1 activity already conducted on the lease and on adjacent areas;

2 (B) the probability that further shallow natural gas
3 exploration activity will occur on the lease and will lead to shallow natural
4 gas development and production; and

5 (C) whether extension of the lease's primary term will
6 accelerate the eventual production of shallow natural gas from the lease.

7 * Sec. 29. AS 38.05.177(l) is amended to read:

8 (l) A lessee holding [OBTAINING] a lease modified under
9 AS 38.05.180(n)(2) [THIS SECTION] may exercise the rights authorized by this
10 section and the lease. The rights granted by the lease must be exercised in a manner
11 that does not unreasonably interfere with eventual development of other mineral
12 deposits on the land leased. However, in a lease entered into under AS 38.05.150 for
13 land that is already subject to a lease covered [LEASED] under this section, coal may
14 not be mined or extracted by the coal lessee from the coal lease without prior
15 agreement with the lessee holding the lease covered [ISSUED] under this section.

16 * Sec. 30. AS 38.05.180(a) is amended to read:

17 (a) The legislature finds that

18 (1) the people of Alaska have an interest in the development of the
19 state's oil and gas resources to

20 (A) maximize the economic and physical recovery of the
21 resources;

22 (B) maximize competition among parties seeking to explore
23 and develop the resources;

24 (C) maximize use of Alaska's human resources in the
25 development of the resources;

26 (2) it is in the best interests of the state

27 (A) to encourage an assessment of its oil and gas resources and
28 to allow the maximum flexibility in the methods of issuing leases to

29 (i) recognize the many varied geographical regions of
30 the state and the different costs of exploring for oil and gas in these
31 regions;

1 (ii) minimize the adverse impact of exploration,
2 development, production, and transportation activity; and

3 (B) to offer acreage for oil and gas leases or for gas only
4 leases, specifically including

5 (i) state acreage that has been the subject of a best
6 interest finding at annual areawide lease sales; and

7 (ii) land in areas that, under (d) of this section, may be
8 leased without having been included in the leasing program prepared
9 and submitted under (b) of this section.

10 * Sec. 31. AS 38.05.180(b) is amended to read:

11 (b) The commissioner shall biennially prepare and, between the first and the
12 15th day of the first regular session of each legislature, notify the legislature of the
13 availability of, a five-year proposed oil and gas leasing program consisting of a
14 schedule of proposed lease sales and specifying as precisely as practicable the location
15 of tracts proposed to be offered for oil and gas leasing or for leasing of gas only
16 during the calendar year in which the proposed program is made available to the
17 legislature and the following four calendar years.

18 * Sec. 32. AS 38.05.180(c) is amended to read:

19 (c) Except as provided in (d) and (w) of this section, an oil and gas lease sale
20 or gas only lease sale may not be held unless it was included in the proposed leasing
21 programs submitted to the legislature during the two calendar years preceding the year
22 in which the sale is held. A lease sale, whether for oil and gas or for gas only, may
23 not be held before the date it is scheduled in the proposed oil and gas leasing program.

24 * Sec. 33. AS 38.05.180(d) is amended to read:

25 (d) The commissioner

26 (1) may annually offer leases for oil and gas or leases for gas only
27 [LEASES] of the acreage described in AS 38.05.035(e)(6)(F);

28 (2) may issue [OIL AND GAS] leases in an area that has not been
29 included in a leasing program prepared, in accordance with (b) of this section, if the
30 land to be leased

31 (A) was previously subject to a valid state oil and gas lease, a

1 valid state gas lease, or a valid federal oil and gas lease;

2 (B) is contiguous to land already under state, federal, or private
3 lease and the commissioner makes a written finding, after hearing, that leasing
4 of the land would result in a substantial probability of early evaluation and
5 development of the land to be leased;

6 (C) is adjacent to land owned or controlled by another party on
7 which a discovery of commercial quantities of oil or gas has been made, and
8 the commissioner finds, after hearing, that there is a reasonable probability that
9 the land to be leased contains oil or gas in communication with the oil or gas
10 discovered on the land of the other party;

11 (D) is adjacent to land included in the federal five-year Outer
12 Continental Shelf leasing program under 43 U.S.C. 1344, and the
13 commissioner makes a written finding, after hearing, that coordinated or
14 simultaneous leasing with the federal government is in the public interest; or

15 (E) is the subject of an [OIL AND GAS] exploration license
16 issued under AS 38.05.131 - 38.05.134; however, if the license issued was
17 for exploration for and recovery of gas only, then the lease issued under
18 this subsection shall be limited to exploration for and recovery of gas only.

19 * Sec. 34. AS 38.05.180(f) is amended to read:

20 (f) Except as provided by AS 38.05.131 - 38.05.134 [AND 38.05.177], the
21 commissioner may issue oil and gas leases or leases for gas only on state land to the
22 highest responsible qualified bidder as follows:

23 (1) the commissioner shall issue an oil and gas lease or a gas only
24 lease, as appropriate, to the successful bidder determined by competitive bidding
25 under regulations adopted by the commissioner; bidding may be by sealed bid or
26 according to any other bidding procedure the commissioner determines is in the best
27 interests of the state;

28 (2) whenever, under any of the leasing methods listed in this
29 subsection, a royalty share is reserved to the state, it shall be delivered in pipeline
30 quality and free of all lease or unit expenses, including but not limited to separation,
31 cleaning, dehydration, gathering, salt water disposal, and preparation for transportation

1 off the lease or unit area;

2 (3) following a pre-sale analysis, the commissioner may choose at least
3 one of the following leasing methods:

4 (A) a cash bonus bid with a fixed royalty share reserved to the
5 state of not less than 12.5 percent in amount or value of the production
6 removed or sold from the lease;

7 (B) a cash bonus bid with a fixed royalty share reserved to the
8 state of not less than 12.5 percent in amount or value of the production
9 removed or sold from the lease and a fixed share of the net profit derived from
10 the lease of not less than 30 percent reserved to the state;

11 (C) a fixed cash bonus with a royalty share reserved to the state
12 as the bid variable but no less than 12.5 percent in amount or value of the
13 production removed or sold from the lease;

14 (D) a fixed cash bonus with the share of the net profit derived
15 from the lease reserved to the state as the bid variable;

16 (E) a fixed cash bonus with a fixed royalty share reserved to the
17 state of not less than 12.5 percent in amount or value of the production
18 removed or sold from the lease with the share of the net profit derived from the
19 lease reserved to the state as the bid variable;

20 (F) a cash bonus bid with a fixed royalty share reserved to the
21 state based on a sliding scale according to the volume of production or other
22 factor but in no event less than 12.5 percent in amount or value of the
23 production removed or sold from the lease;

24 (G) a fixed cash bonus with a royalty share reserved to the state
25 based on a sliding scale according to the volume of production or other factor
26 as the bid variable but not less than 12.5 percent in amount or value of the
27 production removed or sold from the lease;

28 (H) for nonconventional gas that will not be produced in
29 direct competition with gas on which a royalty at a rate of at least 12.5
30 percent is payable, a royalty share reserved to the state of at least 6.25
31 percent in amount or value of the production removed or sold from the

1 lease:

2 (4) notwithstanding a requirement in the leasing method chosen of a
3 minimum fixed royalty share, on and after March 3, 1997, the lessee under a lease
4 issued in the Cook Inlet sedimentary basin who is the first to file with the
5 commissioner a nonconfidential sworn statement claiming to be the first to have
6 drilled a well discovering oil or gas in a previously undiscovered oil or gas pool and
7 who is certified by the commissioner within one year of completion of that discovery
8 well to have drilled a well in that pool that is capable of producing in paying quantities
9 shall pay a royalty of five percent on all production of oil or gas from that pool
10 attributable to that lease for a period of 10 years following the date of discovery of that
11 pool, and thereafter the royalty payable on all production of oil or gas from the pool
12 attributable to that lease shall be determined and payable as specified in the lease; for
13 purposes of this paragraph, the reduced royalty authorized by this paragraph is subject
14 to the following:

15 (A) only one reduction of royalty authorized by this paragraph
16 may be allowed on each lease that qualifies for reduction of royalty under this
17 paragraph;

18 (B) if, under this paragraph, application is made for a royalty
19 reduction for a lease that was entered into before March 3, 1997, the
20 commissioner may approve the application only if, on that date, the lease was a
21 nonproducing lease that was not committed to a unit approved by the
22 commissioner under (m) of this section, that is not part of a unit under (p) or
23 (q) of this section, and that has not been made part of a unit under AS 31.05;

24 (C) if application for a royalty reduction is made under this
25 paragraph for a lease on which a discovery royalty was claimed or may be
26 claimed under the discovery royalty provisions of former AS 38.05.180(a) in
27 effect before May 6, 1969, the commissioner shall disallow the application
28 under this paragraph unless the applicant waives the right to claim the right to
29 a reduced royalty under the discovery royalty provisions of former
30 AS 38.05.180(a) in effect before May 6, 1969; and

31 (D) the commissioner shall adopt regulations setting out the

1 standards, criteria, and definitions of terms that apply to implement the filing
2 of applications for, and the review and certification of, discovery [OIL AND
3 GAS ROYALTY] certifications under this paragraph;

4 (5) notwithstanding and in lieu of a requirement in the leasing method
5 chosen of a minimum fixed royalty share, or the royalty provision of a lease, for leases
6 unitized as described in (p) of this section, leases subject to an agreement described in
7 (s) or (t) of this section, or interests unitized under AS 31.05, the lessee of all or part of
8 an oil or gas field identified in this section that has been granted approval of a written
9 plan submitted to the Alaska Oil and Gas Conservation Commission under
10 AS 31.05.030(i) shall, subject to (dd) of this section, pay a royalty of five percent on
11 the first 25,000,000 barrels of oil and the first 35,000,000,000 cubic feet of gas
12 produced for sale from that field that occurs in the 10 years following the date on
13 which the production for sale commences; the fields eligible for royalty reduction
14 under this paragraph, all of which are located within the Cook Inlet sedimentary basin,
15 were discovered before January 1, 1988, and have been undeveloped or shut in from at
16 least January 1, 1988, through December 31, 1997, are

- 17 (A) Falls Creek;
- 18 (B) Nicolai Creek;
- 19 (C) North Fork;
- 20 (D) Point Starichkof;
- 21 (E) Redoubt Shoal; and
- 22 (F) West Foreland;

23 (6) notwithstanding and in lieu of a requirement in the leasing method
24 chosen of a minimum fixed royalty share, or the royalty provision of a lease, for leases
25 unitized as described in (p) of this section, leases subject to an agreement described in
26 (s) or (t) of this section, or interests unitized under AS 31.05, the lessee of all or part of
27 an oil field located offshore in Cook Inlet on which an oil production platform
28 specified in (A), (C), or (E) of this paragraph operates, or the lessee of all or part of the
29 field located offshore in Cook Inlet and described in (G) of this paragraph,

30 (A) shall pay a royalty of five percent on oil produced from the
31 platform if oil production that equaled or exceeded a volume of 1,200 barrels a

1 day declines to less than that amount for a period of at least one calendar
2 quarter, as certified by the Alaska Oil and Gas Conservation Commission, for
3 as long as the volume of oil produced from the platform remains less than
4 1,200 barrels a day; the provisions of this subparagraph apply to

- 5 (i) Dolly;
- 6 (ii) Grayling;
- 7 (iii) King Salmon;
- 8 (iv) Steelhead; and
- 9 (v) Monopod;

10 (B) shall pay a royalty calculated under this subparagraph if the
11 volume of oil produced from the platform that was certified by the Alaska Oil
12 and Gas Conservation Commission under (A) of this paragraph later increases
13 to 1,200 or more barrels a day and remains at 1,200 or more barrels a day for a
14 period of at least one calendar quarter; until the royalty rate determined under
15 this subparagraph applies, the royalty continues to be calculated under (A) of
16 this paragraph; on and after the first day of the month following the month the
17 increased production exceeds the period specified in this subparagraph, the
18 royalty payable under this subparagraph is

- 19 (i) for production of at least 1,200 barrels a day but not
20 more than 1,300 barrels a day - seven percent;
- 21 (ii) for production of more than 1,300 barrels a day but
22 not more than 1,400 barrels a day - 8.5 percent;
- 23 (iii) for production of more than 1,400 barrels a day but
24 not more than 1,500 barrels a day - 10 percent; and
- 25 (iv) for production of more than 1,500 barrels a day -
26 12.5 percent;

27 (C) shall pay a royalty of five percent on oil produced from the
28 platform if oil production that equaled or exceeded a volume of 975 barrels a
29 day declines to less than that amount for a period of at least one calendar
30 quarter, as certified by the Alaska Oil and Gas Conservation Commission, for
31 as long as the volume of oil produced from the platform remains less than 975

1 barrels a day; the provisions of this subparagraph apply to

- 2 (i) Baker;
3 (ii) Dillon;
4 (iii) XTO.A; and
5 (iv) XTO.C;

6 (D) shall pay a royalty calculated under this subparagraph if the
7 volume of oil produced from the platform that was certified by the Alaska Oil
8 and Gas Conservation Commission under (C) of this paragraph later increases
9 to 975 or more barrels a day and remains at 975 or more barrels a day for a
10 period of at least one calendar quarter; until the royalty rate determined under
11 this subparagraph applies, the royalty continues to be calculated under (C) of
12 this paragraph; on and after the first day of the month following the month the
13 increased production exceeds the period specified in this subparagraph, the
14 royalty payable under this subparagraph is

- 15 (i) for production of at least 975 barrels a day but not
16 more than 1,100 barrels a day - seven percent;
17 (ii) for production of more than 1,100 barrels a day but
18 not more than 1,200 barrels a day - 8.5 percent;
19 (iii) for production of more than 1,200 barrels a day but
20 not more than 1,350 barrels a day - 10 percent; and
21 (iv) for production of more than 1,350 barrels a day -
22 12.5 percent;

23 (E) shall pay a royalty of five percent on oil produced from the
24 platform if oil production that equaled or exceeded a volume of 750 barrels a
25 day declines to less than that amount for a period of at least one calendar
26 quarter, as certified by the Alaska Oil and Gas Conservation Commission, for
27 as long as the volume of oil produced from the platform remains less than 750
28 barrels a day; the provisions of this subparagraph apply to

- 29 (i) Granite Point;
30 (ii) Anna; and
31 (iii) Bruce;

1 (F) shall pay a royalty calculated under this subparagraph if the
2 volume of oil produced from the platform that was certified by the Alaska Oil
3 and Gas Conservation Commission under (E) of this paragraph later increases
4 to 750 or more barrels a day and remains at 750 or more barrels a day for a
5 period of at least one calendar quarter; until the royalty rate determined under
6 this subparagraph applies, the royalty continues to be calculated under (E) of
7 this paragraph; on and after the first day of the month following the month the
8 increased production exceeds the period specified in this subparagraph, the
9 royalty payable under this subparagraph is

10 (i) for production of at least 750 barrels a day but not
11 more than 850 barrels a day - seven percent;

12 (ii) for production of more than 850 barrels a day but
13 not more than 1,000 barrels a day - 8.5 percent;

14 (iii) for production of more than 1,000 barrels a day but
15 not more than 1,200 barrels a day - 10 percent; and

16 (iv) for production of more than 1,200 barrels a day -
17 12.5 percent;

18 (G) shall pay a royalty of five percent on oil produced from the
19 field if oil production that equaled or exceeded a volume of 750 barrels a day
20 declines to less than that amount for a period of at least one calendar quarter,
21 as certified by the Alaska Oil and Gas Conservation Commission, for as long
22 as the volume of oil produced from the field remains less than 750 barrels a
23 day; the provisions of this subparagraph apply to the West McArthur River
24 field;

25 (H) shall pay a royalty calculated under this subparagraph if the
26 volume of oil produced from the field that was certified by the Alaska Oil and
27 Gas Conservation Commission under (G) of this paragraph later increases to
28 750 or more barrels a day and remains at 750 or more barrels a day for a period
29 of at least one calendar quarter; until the royalty rate determined under this
30 subparagraph applies, the royalty continues to be calculated under (G) of this
31 paragraph; on and after the first day of the month following the month the

1 increased production exceeds the period specified in this subparagraph, the
2 royalty payable under this subparagraph is

3 (i) for production of at least 750 barrels a day but not
4 more than 850 barrels a day - seven percent;

5 (ii) for production of more than 850 barrels a day but
6 not more than 1,000 barrels a day - 8.5 percent;

7 (iii) for production of more than 1,000 barrels a day but
8 not more than 1,200 barrels a day - 10 percent; and

9 (iv) for production of more than 1,200 barrels a day -
10 12.5 percent; and

11 (I) may obtain the benefits of the royalty adjustments set out in
12 (A) - (H) of this paragraph only if the commissioner determines that the
13 reduction in production from the platform or the field is

14 (i) based on the average daily production during the
15 calendar quarter based on reservoir conditions; and

16 (ii) not the result of short-term production declines due
17 to mechanical or other choke-back factors, temporary shutdowns or
18 decreased production due to environmental or facility constraints, or
19 market conditions.

20 * Sec. 35. AS 38.05.180(h) is amended to read:

21 (h) The commissioner may include terms in any [OIL AND GAS] lease
22 imposing a minimum work commitment on the lessee. These terms shall be made
23 public before the sale, and may include appropriate penalty provisions to take effect in
24 the event the lessee does not fulfill the minimum work commitment. If it is
25 demonstrated that a lease has been proven unproductive by actions of adjacent lease
26 holders, the commissioner may set aside a work commitment. The commissioner may
27 waive for a period not to exceed one two-year period any term of a minimum work
28 commitment if the commissioner makes a written finding either that conditions
29 preventing drilling or exploration were beyond the lessee's reasonable ability to
30 foresee or control or that the lessee has demonstrated through good faith efforts an
31 intent and ability to drill or develop the lease during the term of the waiver.

1 * **Sec. 36.** AS 38.05.180(i) is amended to read:

2 (i) The commissioner may provide for the establishment of an exploration
3 incentive credit system under which a lessee of state land drilling an exploratory well
4 on that land may earn credits based upon the footage drilled and the region in which
5 the well is situated. The commissioner may also provide for credits to be earned by
6 persons performing geophysical work on state land, if that work is performed during
7 the two seasons immediately preceding an announced lease sale and on land included
8 within the sale area and the geophysical information is made public following the sale.
9 Credits may not exceed 50 percent of the cost of the drilling or geophysical work.
10 Credits may be used during a limited period established by the commissioner and may
11 be assigned during that period. Credits may be applied against (1) [OIL AND GAS]
12 royalty and rental payments for oil and gas or for gas only payable to the state or (2)
13 taxes payable under AS 43.55. A credit may not exceed 50 percent of the payment
14 toward which it is being applied. Amounts due the Alaska permanent fund
15 (AS 37.13.010) shall be calculated before the application of credits under this
16 subsection.

17 * **Sec. 37.** AS 38.05.180(j) is amended to read:

18 (j) The commissioner

19 (1) may provide for modification of royalty on individual leases, leases
20 unitized as described in (p) of this section, leases subject to an agreement described in
21 (s) or (t) of this section, or interests unitized under AS 31.05

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

23 (i) the oil or gas field or pool has been sufficiently
24 delineated to the satisfaction of the commissioner;

25 (ii) the field or pool has not previously produced oil or
26 gas for sale; and

27 (iii) oil or gas production from the field or pool would
28 not otherwise be economically feasible;

29 (B) to prolong the economic life of an oil or gas field or pool as
30 per barrel or barrel equivalent costs increase or as the price of oil or gas
31 decreases, and the increase or decrease is sufficient to make future production

1 no longer economically feasible; or

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

4 (2) may not grant a royalty modification unless the lessee or lessees
5 requesting the change make a clear and convincing showing that a modification of
6 royalty meets the requirements of this subsection and is in the best interests of the
7 state;

8 (3) shall provide for an increase or decrease or other modification of
9 the state's royalty share by a sliding scale royalty or other mechanism that shall be
10 based on a change in the price of oil or gas and may also be based on other relevant
11 factors such as a change in production rate, projected ultimate recovery, development
12 costs, and operating costs

13 (4) may not grant a royalty reduction for a field or pool

14 (A) under (1)(A) of this subsection if the royalty modification
15 for the field or pool would establish a royalty rate of less than five percent in
16 amount or value of the production removed or sold from a lease or leases
17 covering the field or pool;

18 (B) under (1)(B) or (1)(C) of this subsection if the royalty
19 modification for the field or pool would establish a royalty rate of less than
20 three percent in amount or value of the production removed or sold from a
21 lease or leases covering the field or pool;

22 (5) may not grant a royalty reduction under this subsection without
23 including an explicit condition that the royalty reduction is not assignable without the
24 prior written approval, which may not be unreasonably withheld, by the
25 commissioner; the commissioner shall, in the preliminary and final findings and
26 determinations, set out the conditions under which the royalty reduction may be
27 assigned;

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

31 (A) may require disclosure of only the financial and technical

1 data related to development, production, and transportation of oil and gas or
2 gas only from the field or pool that are reasonably available to the applicant;
3 and

4 (B) shall keep the data confidential under AS 38.05.035(a)(9)
5 at the request of the lessee or lessees making application for the royalty
6 reduction; the confidential data may be disclosed by the commissioner to
7 legislators and to the legislative auditor and as directed by the chair or vice-
8 chair of the Legislative Budget and Audit Committee to the director of the
9 division of legislative finance, the permanent employees of their respective
10 divisions who are responsible for evaluating a royalty reduction, and to agents
11 or contractors of the legislative auditor or the legislative finance director who
12 are engaged under contract to evaluate the royalty reduction, if they sign an
13 appropriate confidentiality agreement;

14 (7) may

15 (A) require the lessee or lessees making application for the
16 royalty reduction under (1)(A) of this subsection to pay for the services of an
17 independent contractor, selected by the lessee or lessees from a list of qualified
18 consultants compiled by the commissioner, to evaluate hydrocarbon
19 development, production, transportation, and economics and to assist the
20 commissioner in evaluating the application and financial and technical data: if
21 under this subparagraph, the commissioner requires payment for the services of
22 an independent contractor, the total cost of the services to be paid for by the
23 lessee or lessees may not exceed \$150,000 for each application, and the
24 commissioner shall determine the relevant scope of the work to be performed
25 by the contractor; selection of an independent contractor under this
26 subparagraph is not subject to AS 36.30;

27 (B) with the mutual consent of the lessee or lessees making
28 application for the royalty reduction under (1)(B) or (1)(C) of this subsection,
29 request payment for the services of an independent contractor, selected from a
30 list of qualified consultants to evaluate hydrocarbon development, production,
31 transportation, and economics by the commissioner to assist the commissioner

1 in evaluating the application and financial and technical data; if, under this
2 subparagraph, the commissioner requires payment for the services of an
3 independent contractor, the total cost of the services that may be paid for by
4 the lessee or lessees may not exceed \$150,000 for each application, and the
5 commissioner shall determine the relevant scope of the work to be performed
6 by the contractor; selection of an independent contractor under this
7 subparagraph is not subject to AS 36.30;

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

12 (9) shall offer to appear before the Legislative Budget and Audit
13 Committee, on a day that is not earlier than 10 days and not later than 20 days after
14 giving public notice under (8) of this subsection, to provide the committee a review of
15 the commissioner's preliminary findings and determination on the royalty reduction
16 application and administrative process; if the Legislative Budget and Audit Committee
17 accepts the commissioner's offer, the committee shall give notice of the committee's
18 meeting to all members of the legislature;

19 (10) shall make copies of the preliminary findings and determination
20 available to

21 (A) the presiding officer of each house of the legislature;

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

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

26 (11) shall, within 30 days after the close of the public comment period
27 under (8) of this subsection,

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

30 (B) make a final findings and determination; the
31 commissioner's final findings and determination prepared under this

1 subparagraph regarding a royalty reduction is final and not appealable to the
2 court;

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

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

7 (E) make copies of the final findings and determination
8 available to each person who submitted comment under (8) of this subsection
9 and who has filed a request for the copies;

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

12 * **Sec. 38.** AS 38.05.180(l) is amended to read:

13 (l) Subject to the provisions of AS 31.05, the commissioner has discretion to
14 enter into an agreement whereby, with the consent of the lessee, the state's royalty
15 share of [OIL AND GAS] production of oil and gas or gas only may be stored or
16 retained in storage by the lessee, or the commissioner may enter into an agreement
17 with one or more of the affected field lease holders to trade current royalty production
18 from a field for a like amount, kind, and quality of future production, on the condition
19 that the state receives back its stored or traded royalty share during the first half of the
20 estimated field life or no later than 15 years after start of production, whichever is
21 sooner.

22 * **Sec. 39.** AS 38.05.180(m) is amended to read:

23 (m) An oil and gas lease or a gas only lease must cover a reasonably compact
24 area not exceeding 5,760 acres, and may be for a maximum period of 10 years, except
25 that the commissioner may issue a lease for a period not less than five years upon a
26 finding that it is in the best interests of the state. An oil and gas lease shall be
27 automatically extended if and for so long thereafter as oil or gas is produced in paying
28 quantities from the lease or if the lease is committed to a unit approved by the
29 commissioner, and a gas only lease shall be automatically extended if and for so
30 long thereafter as gas is produced in paying quantities from the lease or if the
31 lease is committed to a unit approved by the commissioner. A lease issued under

1 this section covering land on which there is a well capable of producing oil or gas in
2 paying quantities does not expire because the lessee fails to produce oil or gas unless
3 the lessee is allowed reasonable time to place the well on a producing status. Upon
4 extension, the commissioner may increase lease rentals so long as the increased rental
5 rate does not exceed 150 percent of the rate for the preceding year. If drilling has
6 commenced on the expiration date of the primary term of the lease and is continued
7 with reasonable diligence, including such operations as redrilling, sidetracking, or
8 other means necessary to reach the originally proposed bottom hole location, the lease
9 continues in effect until 90 days after drilling has ceased and for so long thereafter as
10 oil or gas is produced in paying quantities. An oil and gas lease or a gas only lease
11 issued under this section which is subject to termination by reason of cessation of
12 production does not terminate if, within 60 days after production ceases, reworking or
13 drilling operations are commenced on the land under lease and are thereafter
14 conducted with reasonable diligence during the period of nonproduction.

15 * Sec. 40. AS 38.05.180(n) is amended to read:

16 (n) The commissioner may establish by regulation that after a well has been
17 plugged and abandoned, the rental rate which was in effect during the year of
18 abandonment is maintained for the remainder of the term. Rental is payable in
19 advance and continues until income to the state from royalty or net profit share
20 exceeds rental income to the state for that year. Under this subsection,

21 (1) [OIL AND GAS] leases for oil and gas or for gas only shall
22 provide for payment to the state of rental on the following basis:

23 (A) [(1)] for the first year, \$1.00 per acre;

24 (B) [(2)] for the second year, \$1.50 per acre;

25 (C) [(3)] for the third year, \$2.00 per acre;

26 (D) [(4)] for the fourth year, \$2.50 per acre;

27 (E) [(5)] for the fifth and following years, \$3.00 per acre;

28 (2) if the lessee under a gas only lease demonstrates to the
29 commissioner that the potential resources underlying the lease are reasonably
30 estimated to be only nonconventional gas, the rental payment is \$1.00 per acre
31 until the lease expires or paying quantities of conventional oil or gas are

1 discover:d underlying the lease.

2 * Sec. 41. AS 38.05.180(p) is amended to read:

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

20 * Sec. 42. AS 38.05.180 is amended by adding a new subsection to read:

21 (ff) The provisions of this section that authorize oil and gas leases also apply
22 to authorize the commissioner to issue leases for the production of gas only, subject to
23 the following:

24 (1) in authorizing and managing leases under this subsection, the terms
25 "oil and gas" or "oil or gas" as they are used in this chapter may be read and applied as
26 appropriate as referring to gas only;

27 (2) when a lease is authorized as a gas only lease, the lease does not
28 give the lessee the right to produce oil; if a well drilling for gas under a gas only lease
29 authorized by this subsection penetrates a formation capable of producing oil, the
30 owner or operator

31 (A) shall notify the department and the Alaska Oil and Gas

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Conservation Commission; and

(B) may not conduct further operations in the drilled well until the facility complies with all applicable laws and regulations relating to oil and gas exploration and production; however, this subparagraph does not prevent the owner or operator from conducting activities that may be required by the Alaska Oil and Gas Conservation Commission to plug, plug-back, or abandon a well;

(3) for a nonconventional gas lease, if a bond is sought under AS 38.05.130,

(A) before the amount of the surety bond to be posted is determined by the director, require, as a condition for issuing the lease, that the director, after notice and an opportunity to be heard, determine that, to exercise rights under the reservation as set out in AS 38.05.125 and the lease, the lessee has no other reasonable means of entry than access and entry upon the land of the owner; the lessee has the burden of demonstrating compliance with the requirement of this subparagraph; and

(B) in addition to the coverage for actual damages required by that section, provide for payment of reasonable compensation to the owner for any loss by the owner of the owner's use and enjoyment of the property.

* Sec. 43. AS 38.05.860(a) is amended to read:

(a) The commissioner may require an applicant seeking the sale, lease, or other disposal of land or an interest in land, other than under an oil and gas lease, gas only lease, or mineral lease, to deposit an amount covering the estimated cost of an appraisal, survey, and other costs necessary to offer the land or interest in land, including advertising. All deposited funds not expended shall be refunded to the applicant. If the land or interest in land is awarded to a person other than the applicant making the deposit, the person awarded the land shall pay the total actual cost incurred by the department in making the disposal, and the deposit shall be returned to the original applicant. In lieu of requiring the deposit under this subsection, the commissioner may enter into an agreement with an applicant seeking land or an interest in land requiring the applicant to reimburse the department for costs incurred

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1 in the disposal if the applicant is awarded the land or interest in land.

2 * Sec. 44. AS 38.05.860(c) is amended to read:

3 (c) The commissioner shall require each bidder for the competitive leasing of
4 [OIL AND GAS] land for oil and gas, or for gas only, to submit with each bid a
5 deposit of money equal to 20 percent of the bonus.

6 * Sec. 45. AS 38.05.945(a) is amended to read:

7 (a) This section establishes the requirements for notice given by the
8 department for the following actions:

9 (1) classification or reclassification of state land under AS 38.05.300
10 and the closing of land to mineral leasing or entry under AS 38.05.185;

11 (2) zoning of land under applicable law;

12 (3) issuance of a

13 (A) preliminary written finding under AS 38.05.035(e)(5)(A)
14 regarding the sale, lease, or disposal of an interest in state land or resources for
15 oil and gas, or for gas only, subject to AS 38.05.180(b);

16 (B) [REPEALED

17 (C)] written finding for the sale, lease, or disposal of an interest
18 in state land or resources under AS 38.05.035(e)(6), except a [AN OIL OR
19 GAS] lease sale described in AS 38.05.035(e)(6)(F) for which the director
20 must provide opportunity for public comment under the provisions of that
21 subparagraph;

22 (4) a competitive disposal of an interest in state land or resources after
23 final decision under AS 38.05.035(e);

24 (5) a preliminary finding under AS 38.05.035(e) concerning sites for
25 aquatic farms and related hatcheries;

26 (6) a decision under AS 38.05.132 - 38.05.134 regarding the sale,
27 lease, or disposal of an interest in state land or resources.

28 * Sec. 46. AS 38.05.965 is amended by adding a new paragraph to read:

29 (25) "nonconventional gas" means coal bed methane, shales containing
30 gas, or gas hydrates.

31 * Sec. 47. AS 38.06.080(2) is amended to read:

1 (2) "state lease" means an oil and gas lease or gas only lease on state
2 land.

3 * **Sec. 48.** AS 38.35.020(a) is amended to read:

4 (a) Rights-of-way on state land including rights-of-way over, under, along,
5 across, or upon the right-of-way of a public road or highway or the right-of-way of a
6 railroad or other public utility, or across, upon, over, or under a river or other body of
7 water or land belonging to or administered by the state may be granted by
8 noncompetitive lease by the commissioner for pipeline purposes for the transportation
9 of oil, products, or natural gas under those conditions prescribed by law or by
10 administrative regulation. Except to the extent authorized by an oil and gas lease, a
11 gas only lease, or an oil and gas or gas only unit agreement approved by the state, no
12 person may engage in any construction or operation of any part of an oil, products, or
13 natural gas pipeline, which in whole or in part is or is proposed to be on state land
14 unless that person has obtained from the commissioner a right-of-way lease of the land
15 under this chapter.

16 * **Sec. 49.** AS 43.20.072(c) is amended to read:

17 (c) A taxpayer's business income shall be apportioned to this state by
18 multiplying the taxpayer's income determined under (b) of this section by the
19 apportionment factor applicable to the taxpayer among the following factors:

20 (1) the apportionment factor of a taxpayer subject to this section but
21 not engaged in the production of oil and gas, or of gas only, as appropriate, from a
22 lease or property in this state during the tax period is a fraction, the numerator of
23 which is the sum of the property factor under AS 43.19 (Multistate Tax Compact) and
24 the sales factor under (d) of this section for the taxpayer for that tax period, and the
25 denominator of which is two;

26 (2) the apportionment factor of a taxpayer subject to this section but
27 not engaged in the pipeline transportation of oil or gas in this state during the tax
28 period is a fraction, the numerator of which is the sum of the property factor under (e)
29 of this section and the extraction factor under (f) of this section for the taxpayer for the
30 tax period, and the denominator of which is two;

31 (3) the apportionment factor of a taxpayer engaged both in the

1 production of oil or gas from a lease or property in this state and in the pipeline
2 transportation of oil or gas in this state during the tax period is a fraction, the
3 numerator of which is the sum of the sales factor under (d) of this section, the property
4 factor under (e) of this section, and the extraction factor under (f) of this section for
5 the taxpayer for the tax period, and the denominator of which is three.

6 * Sec. 50. AS 43.55.025(a) is amended to read:

7 (a) Subject to the terms and conditions of this section, on oil and gas produced
8 from an oil and gas lease, or on gas produced from a gas only lease, on or after
9 July 1, 2004, a credit against the tax due under this chapter is allowed in an amount
10 equal to

11 (1) 20 percent of the total exploration expenditures that qualify under
12 (b) and (c) of this section, 20 percent of the total exploration expenditures that qualify
13 under (b) and (d) of this section, or both, for a total credit that does not exceed 40
14 percent of the total exploration expenditures; or

15 (2) 40 percent of the total exploration expenditures that qualify under
16 (b) and (e) of this section, for a total production tax credit that does not exceed 40
17 percent of the total qualified exploration expenditures.

18 * Sec. 51. AS 43.55.900(9) is amended to read:

19 (9) "lease or property" means any right, title, or interest in or the right
20 to produce or recover oil or gas including:

21 (A) a mineral interest,

22 (B) a leasehold interest,

23 (C) a working interest, royalty interest, overriding royalty
24 interest, production payment, net profit interest or any other interest in a lease,
25 concession, joint venture, or other agreement for [OIL AND GAS] exploration
26 development, or production of oil and gas or of gas only,

27 (D) a working interest, royalty interest, overriding royalty
28 interest, production payment, net profit interest or any other interest in an
29 agreement for unitization or pooling under the provisions of 26 U.S.C.
30 614(b)(3) (Internal Revenue Code) as defined on January 1, 1974;

31 * Sec. 52. AS 46.03.100(f) is amended to read:

1 (f) This section does not apply to discharges of solid or liquid waste material
2 or water discharges from the following activities if the discharge is incidental to the
3 activity and the activity does not produce a discharge from a point source, as that term
4 is defined in regulations adopted under this chapter, directly into any surface water of
5 the state:

6 (1) mineral drilling, trenching, ditching, and similar activities;

7 (2) landscaping;

8 (3) water well drilling, geophysical drilling, or nonconventional
9 [COAL BED METHANE DRILLING OR OTHER NATURAL] gas drilling; for
10 purposes of this paragraph, "nonconventional gas" has the meaning given in
11 AS 38.05.965 [TO RECOVER GAS FROM A FIELD IF A PART OF THE FIELD IS
12 WITHIN 3,000 FEET OF THE SURFACE]; or

13 (4) drilling, ditching, trenching, and similar activities associated with
14 facility construction and maintenance or with road or other transportation facility
15 construction and maintenance; however, the exemption provided by this paragraph
16 does not relieve a person from obtaining a permit under this section if

17 (A) the drilling, ditching, trenching, or similar activity will
18 involve the removal of the groundwater, stormwater, or wastewater runoff that
19 has accumulated and is present at an excavation site for facility, road, or other
20 transportation construction or maintenance; and

21 (B) a permit is otherwise required by this section.

22 * Sec. 53. AS 46.04.030(b) is amended to read:

23 (b) A person may not cause or permit the operation of a pipeline or an
24 exploration or production facility in the state unless an oil discharge prevention and
25 contingency plan for the pipeline or facility has been approved by the department and
26 the person is in compliance with the plan. This subsection does not apply to an
27 exploration or production facility used solely to explore for or to develop or produce
28 nonconventional [SHALLOW NATURAL] gas resources, except that this exemption
29 does not apply if the Alaska Oil and Gas Conservation Commission determines under
30 AS 31.05.030(j) that

31 (1) a well drilled for nonconventional [SHALLOW NATURAL] gas

1 may penetrate a formation capable of flowing oil; and

2 (2) the volume of oil encountered will be of such quantities that a
3 contingency plan will be required.

4 * **Sec. 54.** AS 46.04.040(b) is amended to read:

5 (b) A person may not cause or permit the operation of a pipeline or an
6 exploration or production facility in the state unless the person has furnished to the
7 department, and the department has approved, proof of financial ability to respond in
8 damages. Proof of financial responsibility required for

9 (1) a pipeline or an offshore exploration or production facility is
10 \$50,000,000 per incident;

11 (2) an onshore production facility is

12 (A) \$20,000,000 per incident if the facility produces over
13 10,000 barrels per day of oil;

14 (B) \$10,000,000 per incident if the facility produces over 5,000
15 barrels per day but not more than 10,000 barrels per day of oil;

16 (C) \$5,000,000 per incident if the facility produces over 2,500
17 barrels per day but not more than 5,000 barrels per day of oil;

18 (D) \$1,000,000 per incident if the facility produces 2,500
19 barrels per day or less of oil;

20 (3) an onshore exploration facility is

21 (A) \$25,000 per incident for a facility used solely to explore for
22 nonconventional [SHALLOW NATURAL] gas by means of drilling a well to
23 explore for the gas [, WHETHER METHANE ASSOCIATED WITH AND
24 DERIVED FROM COAL DEPOSITS OR OTHERWISE, FROM A FIELD IF
25 A PART OF THE FIELD IS WITHIN 3,000 FEET OF THE SURFACE]; and

26 (B) except as provided by (A) of this paragraph, \$1,000,000 per
27 incident.

28 * **Sec. 55.** AS 46.04.900 is amended by adding a new paragraph to read:

29 (31) "nonconventional gas" has the meaning given in AS 38.05.965.

30 * **Sec. 56.** AS 46.40.205 is amended to read:

31 **Sec. 46.40.205. Consistency determinations for certain activities involving**

1 nonconventional [SHALLOW NATURAL] gas. (a) When conducted under
2 oversight and regulation of the Alaska Oil and Gas Conservation Commission and the
3 state's resource agencies, projects for the exploration and development of
4 nonconventional [SHALLOW NATURAL] gas are consistent with the program
5 described in this chapter. Persons responsible for activities subject to this section shall
6 obtain all required permits and approvals from municipal, state, and federal agencies
7 as otherwise required by law.

8 (b) In this section, "nonconventional [SHALLOW NATURAL] gas" has the
9 meaning given in AS 38.05.965 [AS 46.04.900].

10 * Sec. 57. AS 46.40.210(12) is amended to read:

11 (12) "uses of state concern" means those land and water uses that
12 would significantly affect the long-term public interest; "uses of state concern" include

13 (A) uses of national interest, including the use of resources for
14 the siting of ports and major facilities that contribute to meeting national
15 energy needs, construction and maintenance of navigational facilities and
16 systems, resource development of federal land, and national defense and
17 related security facilities that are dependent upon coastal locations;

18 (B) uses of more than local concern, including those land and
19 water uses that confer significant environmental, social, cultural, or economic
20 benefits or burdens beyond a single coastal resource district;

21 (C) the siting of major energy facilities, activities pursuant to a
22 state oil and gas lease, a state gas only lease, or a federal oil and gas lease, or
23 large-scale industrial or commercial development activities that are dependent
24 on a coastal location and that, because of their magnitude or the magnitude of
25 their effect on the economy of the state or the surrounding area, are reasonably
26 likely to present issues of more than local significance;

27 (D) facilities serving statewide or interregional transportation
28 and communication needs; and

29 (E) uses in areas established as state parks or recreational areas
30 under AS 41.21 or as state game refuges, game sanctuaries, or critical habitat
31 areas under AS 16.20.

1 * **Sec. 58.** AS 31.05.170(14); AS 38.05.177(b), 38.05.177(c), 38.05.177(e), 38.05.177(f),
2 38.05.177(g), 38.05.177(h), 38.05.177(j), 38.05.177(k), 38.05.177(m), 38.05.177(o); and
3 AS 46.04.900(25) are repealed.

4 * **Sec. 59.** The uncodified law of the State of Alaska is amended by adding a new section to
5 read:

6 CERTAIN SHALLOW NATURAL GAS LEASES AND LEASE APPLICATIONS
7 TO BE ADMINISTERED UNDER FORMER LAW. The provisions of AS 38.05.177(a),
8 (d)(1), and (l), amended by secs. 27 - 29 of this Act, as those provisions read on the day
9 before the effective date of amendment of those subsections, and the provisions of
10 AS 38.05.177(b), (c), (e) - (h), (j), (k), (m), and (o), repealed by sec. 58 of this Act, as those
11 provisions read on the day before the effective date of the repeal of those subsections, apply to
12 shallow natural gas

13 (1) leases issued under AS 38.05.177 and in effect on December 31, 2003; and

14 (2) lease applications under AS 38.05.177 that were received by the
15 Department of Natural Resources before January 1, 2004.

16 * **Sec. 60.** This Act takes effect immediately under AS 01.10.070(c).