

ALASKA LEGISLATURE COMMITTEE FILES, 2003-2004 8672

11308 SENATE RESOURCES

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. 33. 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. 34. 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. 35. 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. 36. 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. 37. 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 re-drilling, 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. 38. 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 advance
 23 and continues until income to the state from royalty or net profit share exceeds rental
 24 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. 39. 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. 40. 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. 41. 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. 42. 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. 43. 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. 44. 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. 45. 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. 46. 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. 47. 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. 48. 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. 49. 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. 50. 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. 51.** 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. 52.** 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. 53. 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. 54. 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. 55. 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. 56. AS 31.05.170(14); AS 38.05.177(b), 38.05.177(c), 38.05.177(d), 38.05.177(e),
22 38.05.177(f), 38.05.177(g), 38.05.177(h), 38.05.177(j), 38.05.177(k), 38.05.177(m),
23 38.05.177(o); and AS 46.04.900(25) are repealed.

24 * Sec. 57. 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) and
28 (I), amended by secs. 26 and 27 of this Act, as those provisions read on the day before the
29 effective date of amendment of those sections, and the provisions of AS 38.05.177(b) - (h),
30 (j), (k), (m), and (o), repealed by sec. 56 of this Act, as those provisions read on the day
31 before the effective date of the repeal of that section, apply to shallow natural gas

- 1 (1) leases issued under AS 38.05.177 and in effect on December 31, 2003; and
- 2 (2) lease applications under AS 38.05.177 that were received by the
- 3 Department of Natural Resources before January 1, 2004.

4 * Sec. 58. This Act takes effect immediately under AS 01.10.070(c).

LEGAL SERVICES

DIVISION OF LEGAL AND RESEARCH SERVICES
LEGISLATIVE AFFAIRS AGENCY
STATE OF ALASKA

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Juneau, Alaska 99801-1182
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MEMORANDUM

February 17, 2004

SUBJECT: Draft CSSB 312(), relating to natural gas exploration and development and to nonconventional gas, and amending the section under which shallow natural gas leases may be issued -- sectional analysis (Work Order No. 23-LS1552\Q)

TO: Senator Scott Ogan, Chair
Senate Resources Committee

FROM: Jack Chenoweth
Assistant Revisor of Statutes

The draft committee substitute treats comprehensively with the exploration and development of natural gas. It contains changes that

-- convert references and substantive provisions covering shallow natural gas leasing into a leasing policy covering "nonconventional gas" and provide a definition of that term;

-- authorize the Department of Natural Resources to lease for "gas only" under the conventional oil and gas leasing procedures, with limited reservations governing activity involving nonconventional gas leases;

-- expand the use of exploration licensing and leasing under AS 38.05.131 - 38.05.134 to cover "gas only" licenses and leases; and

-- amend or repeal specific parts of AS 38.05.177, the section of the Alaska Land Act (AS 38.05) that currently authorizes and guides shallow natural gas leasing.

PROVISIONS ESTABLISHING A "NONCONVENTIONAL GAS" LEASING POLICY, SUPPLYING A DEFINITION FOR THAT TERM, AND MAKING CONFORMING CHANGES:

Bill section 44 supplies a definition of "nonconventional gas." The definition is added to the body of definitions that are generally applicable to the Alaska Land Act, AS 38.05. This definition replaces a pair of definitions for "shallow natural gas" and a working reference to shallow natural gas in the language of AS 38.05.177(a)(1), appearing at page 20, lines 10 - 13. Note that the definition of "nonconventional gas" proposed in the measure covers "coalbed methane, shales containing gas, or gas hydrates."

With the substitution of the new term and a definition for it, each of the following makes conforming changes:

-- bill sections 4 - 6, amending or adding to provisions in AS 31.05 (Alaska Oil and Gas Conservation Commission);

-- a reference in bill section 26, amending AS 38.05.177(a); and

-- bill sections 50 - 54, substituting "nonconventional gas" for "shallow natural gas" in various references in title 46; this title of the Alaska Statutes generally deals with environmental matters.

AUTHORIZING THE DEPARTMENT OF NATURAL RESOURCES TO LEASE FOR "GAS ONLY" UNDER THE CONVENTIONAL OIL AND GAS LEASING PROCEDURES, WITH LIMITED RESERVATIONS GOVERNING ACTIVITY INVOLVING NONCONVENTIONAL GAS LEASES, AND MAKING CONFORMING CHANGES:

AS 38.05.180(ff), added by bill section 40, explicitly authorizes the Department of Natural Resources to "issue leases for gas only" under the conventional oil and gas leasing program.

Out of an abundance of drafting caution, the following revise or delete existing references to "oil and gas," "oil and gas lease," or substantially similar terms and references to acknowledge the alternative authorization of "gas only" leasing:

-- bill sections 1, 3, 7 - 9, 10 (except the repeal of AS 38.05.035(e)(6)(G) [page 12, lines 4 - 6]), 11, 13, 28 - 31, 32 (except the addition of AS 38.05.180(f)(3)(H) [page 24, line 31 - page 25, line 4]), 33 - 37, 39, 41 - 43, 45 - 49, and 55.

AUTHORIZING THE DEPARTMENT OF NATURAL RESOURCES TO USE EXPLORATION LICENSING AND LEASING FOR "GAS ONLY" UNDER AS 38.05.131 - 38.05.134, AND MAKING CONFORMING CHANGES:

Bill section 14, amending AS 38.05.131(a), explicitly authorizes the Department of Natural Resources to issue exploration licenses and leases for "gas only." The following provisions make related conforming changes:

-- bill sections 2, 12, 15 - 21, 22 (except the language of new subparagraph (B) [page 19, lines 2 - 7]), and 24.

PROVISIONS ALTERING OR REPEALING SPECIFIC PARTS OF AS 38.05.177, ADDRESSING SHALLOW NATURAL GAS LEASING:

These remarks principally address the content added by bill sections 26 and 27 and the repeal of certain subsections of AS 38.05.177, the existing shallow natural gas leasing section.

Certain subsections are amended with the intent that their specific provisions override comparable provisions in the conventional oil and gas leasing section, AS 38.05.180. So,

-- AS 38.05.177(a) (bill section 26): The change substitutes reference to "nonconventional gas" and amends to delete the content of the balance of the subsection; and

-- AS 38.05.177(l) (bill section 27): The insertion in this subsection amends the existing protections for mineral deposits and coal in situations in which a lessee secures a lease under AS 38.05.180(ff) (gas only leases) and this section (nonconventional gas).

As to other parts of AS 38.05.177, bill section 56 repeals the following:

-- AS 38.05.177(b): This subsection currently sets maximum acreage limitations (paragraph (1)) and levies an application fee (paragraph (2)). If gas only leases are to be issued for unconventional gas under AS 38.05.180, then acreage limits of AS 38.05.180(m) should apply, and maximum holding provisions for oil or gas leases set out in AS 38.05.140(c) should also. In the main, oil and gas leases are offered as competitive leases, so there would not be an application process and, hence, a separate application fee for a noncompetitive lease would not be collected. Consequently, this subsection is to be repealed in its entirety.

-- AS 38.05.177(c): This subsection sets out the notice and public comment provisions. Conventional oil and gas leases have different notice provisions, AS 38.05.945(a)(3), and those should operate in lieu of the expedited notice/public comments of this subsection. Again, this subsection is to be repealed in its entirety.

-- AS 38.05.177(d) and (e): These subsections are the lease extension and lease boundary adjustment provisions. Comparable provisions for conventional oil and gas leases appear in AS 38.05.180(m) and should operate in lieu of sec. 177(d) and (e). These subsections are therefore to be repealed.

-- AS 38.05.177(f): This subsection establishes a flat rent at the rate of one dollar per year. The comparable provision appears in AS 38.05.180(n)(2), so this subsection is to be repealed.

-- AS 38.05.177(g): This subsection describes material relating to the royalty payable on shallow natural gas. The comparable provision is addressed in an amendment

to AS 38.05.180(f)(3)(H) (page 24, beginning at line 31), so this subsection is to be repealed.

-- AS 38.05.177(h): This is the lease surrender or relinquishment provision. As leasing would occur under AS 38.05.180, provisions covering these subjects under authority of that section would apply, so this subsection may be repealed.

-- AS 38.05.177(j): This subsection lays out a contingency for oversight by the Alaska Oil and Gas Conservation Commission if a shallow natural gas well penetrates a formation capable of producing oil. The comparable provision appears in the concluding part of AS 38.05.177(ff), added by bill section 40 (page 37, beginning at line 29), so the language in this subsection is to be repealed.

-- AS 38.05.177(k): The current subsection establishes a bonding requirement for shallow natural gas leasing to secure the payment of damages, together with limitations on the bond requirement statewide. The comparable bonding requirement in the Alaska Land Act is the general bonding requirement of AS 38.05.130. For exploration licensing activities, there are special bond requirements in AS 38.05.132(c)(4) and (5) and 38.05.132(e). The bond requirements for shallow natural gas leasing are to be repealed. Also proposed for deletion by the repeal of this subsection is language speaking to standards for regulations applicable to the shallow natural gas leasing program.

-- AS 38.05.177(m): This is the lease extension provision. Again, because leasing would occur under the conventional oil and gas leasing procedures of AS 38.05.180, provisions covering these subjects under authority of that section would apply, so that this subsection is being repealed.

-- AS 38.05.177(o): Repeal of this subsection eliminates the definition of "lease" in the context of a "shallow gas lease."

OTHER BILL SECTIONS THAT ARE NOT ADDRESSED OR CONSIDERED ABOVE:

Bill section 10: The repeal of AS 38.05.035(e)(6)(G), page 12, lines 4 - 6, drops the exemption for shallow natural gas leasing from the written finding requirements of that subsection. Before nonconventional gas leasing may occur, proposed nonconventional leases would be required to be supported by a written best interest finding.¹

Bill sections 22 (page 19, lines 2 - 7) **and 32** (page 24, line 31 - page 25, line 4): For purposes of retention of the reduced royalty authorized for certain gas, these two amendments add, as to nonconventional gas exploration licensing and leasing and nonconventional gas leasing under the leasing program of AS 38.05.180, provisions for a reduced royalty for nonconventional gas "not produced in direct competition with gas on

¹ In the draft, the lead-in to AS 38.05.035(e)(6) setting out the required written best interest finding appears in the text of the bill at page 10, line 29 - page 11, line 6.

which a royalty at a rate of at least 12.5 percent is payable." Similar language in the existing provision, AS 38.05.177(g), is to be repealed.

Bill sections 23 and 25: Both provisions are concerned with the relationship between coal and coal bed generated methane. The amendments delete references to shallow natural gas (coal bed methane) leasing under AS 38.05.177.

Bill section 38: AS 38.05.180(n) currently spells out the rent payable on oil and gas leases. Those rental rates are proposed to be retained for conventional oil and gas leases, but the subsection is proposed to be amended to carry over from existing AS 38.05.177(f) authority for payment of a fixed rent of \$1.00 per acre per year if the lease is shown to contain only sources that are reasonably estimated to contain only nonconventional gas. The burden of making that demonstration is assigned to the lessee.

Bill section 56: In addition to the repeal of specific subsections of AS 38.05.177 described above, the section would repeal paragraphs setting out definitions of "shallow natural gas" in AS 31.05 and AS 46.04. Each repeal is matched (bill sections 6 and 53) with addition of definitions for the substituted term, "nonconventional gas."

Bill section 57: This transitional provision directs the Department of Natural Resources to deal with shallow natural gas leases executed and lease applications received by December 31, 2003, under the provisions of AS 38.05.177 as it read before its amendment by this Act.

Bill section 58 gives the measure an immediate effective date.

JBC:med
04-199.med

23-LS1552\Q
Chenoweth
2/16/04

CS FOR SENATE BILL NO. 312()

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

BY

**Offered:
Referred:**

Sponsor(s): SENATE RESOURCES COMMITTEE BY REQUEST

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

1 an [OIL AND GAS] exploration license issued under AS 38.05.131 -
 2 38.05.134; the commissioner may not refuse to convey title to land to the
 3 University of Alaska under this subparagraph for more than two years after its
 4 first selection by the University of Alaska; or

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

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

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

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

13 (2) for the reauthorization of leases that were in effect on January 1,
 14 1994, for nonresidential purposes within the following development nodes:

15 (A) Coldfoot:

16 Township 28 North, Range 12 West, Fairbanks Meridian

17 Sections 3 - 4

18 Sections 9 - 10

19 Sections 15 - 16

20 Sections 20 - 22

21 (B) Yukon River Crossing:

22 Township 12 North, Range 10 West, Fairbanks Meridian

23 Sections 6 - 7

24 Township 12 North, Range 11 West, Fairbanks Meridian

25 Sections 1 - 2

26 Section 12

27 Township 13 North, Range 10 West, Fairbanks Meridian

28 Sections 29 - 32

29 Township 13 North, Range 11 West, Fairbanks Meridian

30 Section 22

31 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 the purposes of AS 46.04.030(b), the commission shall determine whether a nonconventional gas well [DRILLED FOR SHALLOW NATURAL GAS] may penetrate a formation capable of flowing oil and, if so, whether the volume of oil encountered will be of such quantities that an oil discharge prevention and contingency plan will be required.

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

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

1 be heard. In the exercise of its authority to issue the variance,

2 (1) the commission may approve the variance if

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

5 (B) the commission determines that the request is more
6 appropriate to the proposed operation than compliance with the requirement of
7 the regulation; and

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

12 (A) the nature of the operation involved;

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

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

17 * Sec. 6. AS 31.05.170 is amended by adding a new paragraph to read:

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

19 * Sec. 7. AS 36.30.850(b)(25) is amended to read:

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

22 * Sec. 8. AS 36.30.850(b)(33) is amended to read:

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

29 * Sec. 9. AS 38.04.065(i) is amended to read:

30 (i) An oil and gas lease sale or gas only lease sale is not subject to this
31 section. Oil and gas lease sales and gas only lease sales are subject to the planning

1 process established under AS 38.05.180.

2 * Sec. 10. AS 38.05.035(e) is amended to read:

3 (e) Upon a written finding that the interests of the state will be best served, the
4 director may, with the consent of the commissioner, approve contracts for the sale,
5 lease, or other disposal of available land, resources, property, or interests in them. In
6 approving a contract under this subsection, the director need only prepare a single
7 written finding. In addition to the conditions and limitations imposed by law, the
8 director may impose additional conditions or limitations in the contracts as the director
9 determines, with the consent of the commissioner, will best serve the interests of the
10 state. The preparation and issuance of the written finding by the director are subject to
11 the following:

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

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

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

22 (i) applicable statutes and regulations;

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

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

1 and

2 (C) may, if the project for which the proposed disposal is
3 sought is a multiphased development, limit the scope of an administrative
4 review and finding for the proposed disposal to the applicable statutes and
5 regulations, facts, and issues identified in (B)(i) - (iii) of this paragraph that
6 pertain solely to the disposal phase of the project when

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

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

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

18 (iv) the department describes its reasons for a decision
19 to phase;

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

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

26 (B) issues based on the statutes and regulations referred to in
27 (1)(B)(i) of this subsection and on the facts described in (1)(B)(ii) of this
28 subsection;

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

31 (4) a contract for the sale, lease, or other disposal of available land or

1 an interest in land is not legally binding on the state until the commissioner approves
2 the contract, but if the appraised value is not greater than \$50,000 in the case of the
3 sale of land or an interest in land, or \$5,000 in the case of the annual rental of land or
4 interest in land, the director may execute the contract without the approval of the
5 commissioner;

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

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

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

29 (6) before a public hearing, if held, or in any case not less than 21 days
30 before the sale, lease, or other disposal of available land, property, resources, or
31 interests in them other than a sale, lease, or other disposal of available land or an

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 would
13 be served by issuing an [OIL AND GAS] exploration license, the finding must (1)
14 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(l) is amended to read:

12 (l) A lessee obtaining a lease under AS 38.05.180(ff) and this section may
13 exercise the rights authorized by this section and the lease. The rights granted by the
14 lease must be exercised in a manner that does not unreasonably interfere with eventual
15 development of other mineral deposits on the land leased. However, in a lease entered
16 into under AS 38.05.150 for land that is already leased under this section, coal may
17 not be mined or extracted by the coal lessee from the coal lease without prior
18 agreement with the lessee holding the lease issued under this section.

19 * Sec. 28. AS 38.05.180(a) is amended to read:

20 (a) The legislature finds that

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

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

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

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

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

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

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

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

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

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

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

13 * **Sec. 29.** AS 38.05.180(b) is amended to read:

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

21 * **Sec. 30.** AS 38.05.180(c) is amended to read:

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

27 * **Sec. 31.** AS 38.05.180(d) is amended to read:

28 (d) The commissioner

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

31 (2) may issue [OIL AND GAS] leases in an area that has not been

1 included in a leasing program prepared, in accordance with (b) of this section, if the
2 land to be leased

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

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

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

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

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

22 * Sec. 32. AS 38.05.180(f) is amended to read:

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

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

31 (2) whenever, under any of the leasing methods listed in this

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

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

7 (A) 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;

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

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

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

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

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

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

31 (H) for nonconventional gas that will not be produced in

1 direct competition with gas on which a royalty at a rate of at least 12.5
2 percent is payable, a royalty share reserved to the state of at least 6.25
3 percent in amount or value of the production removed or sold from the
4 lease;

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

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

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

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

1 a reduced royalty under the discovery royalty provisions of former
2 AS 38.05.180(a) in effect before May 6, 1969; and

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

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

20 (A) Falls Creek;

21 (B) Nicolai Creek;

22 (C) North Fork;

23 (D) Point Starichkof;

24 (E) Redoubt Shoal; and

25 (F) West Foreland;

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

1 field located offshore in Cook Inlet and described in (G) of this paragraph,

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

8 (i) Dolly;

9 (ii) Grayling;

10 (iii) King Salmon;

11 (iv) Steelhead; and

12 (v) Monopod;

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

22 (i) for production of at least 1,200 barrels a day but not
23 more than 1,300 barrels a day - seven percent;

24 (ii) for production of more than 1,300 barrels a day but
25 not more than 1,400 barrels a day - 8.5 percent;

26 (iii) for production of more than 1,400 barrels a day but
27 not more than 1,500 barrels a day - 10 percent; and

28 (iv) for production of more than 1,500 barrels a day -
29 12.5 percent;

30 (C) shall pay a royalty of five percent on oil produced from the
31 platform if oil production that equaled or exceeded a volume of 975 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 975
4 barrels a day; the provisions of this subparagraph apply to

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

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

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

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

1 (i) Granite Point;

2 (ii) Anna; and

3 (iii) Bruce;

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

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

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

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

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

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

28 (H) shall pay a royalty calculated under this subparagraph if the
29 volume of oil produced from the field that was certified by the Alaska Oil and
30 Gas Conservation Commission under (G) of this paragraph later increases to
31 750 or more barrels a day and remains at 750 or more barrels a day for a period

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

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

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

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

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

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

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

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

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

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

1 preventing drilling or exploration were beyond the lessee's reasonable ability to
2 foresee or control or that the lessee has demonstrated through good faith efforts an
3 intent and ability to drill or develop the lease during the term of the waiver.

4 * Sec. 34. AS 38.05.180(i) is amended to read:

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

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

21 (j) The commissioner
22 (1) may provide for modification of royalty on individual leases, leases
23 unitized as described in (p) of this section, leases subject to an agreement described in
24 (s) or (t) of this section, or interests unitized under AS 31.05
25 (A) to allow for production from an oil or gas field or pool if
26 (i) the oil or gas field or pool has been sufficiently
27 delineated to the satisfaction of the commissioner;
28 (ii) the field or pool has not previously produced oil or
29 gas for sale; and
30 (iii) oil or gas production from the field or pool would
31 not otherwise be economically feasible;

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

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

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

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

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

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

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

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

31 (6) shall require the lessee or lessees to submit, with the application for

1 the royalty reduction, financial and technical data that demonstrate that the
2 requirements of this subsection are met; the commissioner

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

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

17 (7) may

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

30 (B) with the mutual consent of the lessee or lessees making
31 application for the royalty reduction under (1)(B) or (1)(C) of this subsection,

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

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

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

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

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

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

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

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

31 (A) prepare a summary of the public response to the

1 commissioner's preliminary findings and determination;

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

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

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

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

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

15 * **Sec. 36.** AS 38.05.180(l) is amended to read:

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

25 * **Sec. 37.** AS 38.05.180(m) is amended to read:

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

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

18 * Sec. 38. AS 38.05.180(n) is amended to read:

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

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

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

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

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

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

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

31 (2) if the lessee under a gas only lease demonstrates to the

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

5 * Sec. 39. AS 38.05.180(p) is amended to read:

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

23 * Sec. 40. AS 38.05.180 is amended by adding a new subsection to read:

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

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

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

8 * Sec. 41. AS 38.05.860(a) is amended to read:

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

21 * Sec. 42. AS 38.05.860(c) is amended to read:

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

25 * Sec. 43. AS 38.05.945(a) is amended to read:

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

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

30 (2) zoning of land under applicable law;

31 (3) issuance of a

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

4 (B) [REPEALED

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

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

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

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

16 * Sec. 44. AS 38.05.965 is amended by adding a new paragraph to read:

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

19 * Sec. 45. AS 38.06.080(2) is amended to read:

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

22 * Sec. 46. AS 38.35.020(a) is amended to read:

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

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

4 * **Sec. 47.** AS 43.20.072(c) is amended to read:

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

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

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

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

25 * **Sec. 48.** AS 43.55.025(a) is amended to read:

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

30 (1) 20 percent of the total exploration expenditures that qualify under
31 (b) and (c) of this section, 20 percent of the total exploration expenditures that qualify

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

3 (2) 40 percent of the total exploration expenditures that qualify under
4 (b) and (e) of this section, for a total production tax credit that does not exceed 40
5 percent of the total qualified exploration expenditures.

6 * Sec. 49. AS 43.55.900(9) is amended to read:

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

9 (A) a mineral interest,

10 (B) a leasehold interest,

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

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

19 * Sec. 50. AS 46.03.100(f) is amended to read:

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

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

26 (2) landscaping;

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

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

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

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

10 * Sec. 51. AS 46.04.030(b) is amended to read:

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

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

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

23 * Sec. 52. AS 46.04.040(b) is amended to read:

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

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

30 (2) an onshore production facility is

31 (A) \$20,000,000 per incident if the facility produces over

1 10,000 barrels per day of oil;

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

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

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

8 (3) an onshore exploration facility is

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

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

16 * Sec. 53. AS 46.04.900 is amended by adding a new paragraph to read:

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

18 * Sec. 54. AS 46.40.205 is amended to read:

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

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

29 * Sec. 55. AS 46.40.210(12) is amended to read:

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

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

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

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

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

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

20 * Sec. 56. AS 31.05.170(14); AS 38.05.177(b), 38.05.177(c), 38.05.177(d), 38.05.177(e),
21 38.05.177(f), 38.05.177(g), 38.05.177(h), 38.05.177(j), 38.05.177(k), 38.05.177(m),
22 38.05.177(o); and AS 46.04.900(25) are repealed.

23 * Sec. 57. The uncodified law of the State of Alaska is amended by adding a new section to
24 read:

25 CERTAIN SHALLOW NATURAL GAS LEASES AND LEASE APPLICATIONS
26 TO BE ADMINISTERED UNDER FORMER LAW. The provisions of AS 38.05.177(a) and
27 (l), amended by secs. 26 and 27 of this Act, as those provisions read on the day before the
28 effective date of amendment of those sections, and the provisions of AS 38.05.177(b) - (h),
29 (j), (k), (m), and (o), repealed by sec. 56 of this Act, as those provisions read on the day
30 before the effective date of the repeal of that section, apply to shallow natural gas

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

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

3 * Sec. 58. This Act takes effect immediately under AS 01.10.070(c).

LEGAL SERVICES

DIVISION OF LEGAL AND RESEARCH SERVICES
LEGISLATIVE AFFAIRS AGENCY
STATE OF ALASKA

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

State Capitol
Juneau, Alaska 99801-1182
Deliveries to: 129 6th St., Rm. 329


MEMORANDUM

February 9, 2004

SUBJECT: Senate Bill 312, relating to natural gas exploration and development and to nonconventional gas, and amending the section under which shallow natural gas leases may be issued -- sectional analysis (Work Order No. 23-LS1552I)

TO: Senator Scott Ogan, Chair
Senate Resources Committee

FROM: Jack Chenoweth
Assistant Revisor of Statutes



The measure treats comprehensively with the exploration and development of natural gas. It contains changes that

-- convert references and substantive provisions covering shallow natural gas leasing into a leasing policy covering "nonconventional gas" and provide a definition of that term;

-- authorize the Department of Natural Resources to lease for "gas only" under the conventional oil and gas leasing procedures, with limited reservations governing activity involving nonconventional gas leases;

-- expand the use of exploration licensing and leasing under AS 38.05.131 - 38.05.134 to cover "gas only" licenses and leases; and

-- amend or repeal specific parts of AS 38.05.177, the section of the Alaska Land Act (AS 38.05) that currently authorizes and guides shallow natural gas leasing.

PROVISIONS ESTABLISHING A "NONCONVENTIONAL GAS" LEASING POLICY, SUPPLYING A DEFINITION FOR THAT TERM, AND MAKING CONFORMING CHANGES:

The definition of "nonconventional gas" is added in **bill section 31**. It replaces a pair of definitions for "shallow natural gas" and a working reference to shallow natural gas in the language of AS 38.05.177(a)(1), appearing at page 20, lines 10 - 13. Please note that the definition of "nonconventional gas" proposed in the measure covers "coalbed methane, shales containing gas, or gas hydrates."

With the substitution of the new term and a definition for it, each of the following makes conforming changes:

-- bill sections 4 - 6, amending or adding to provisions in AS 31.05 (Alaska Oil and Gas Conservation Commission);

-- references in bill section 26 - 31, amending various subsections of AS 38.05.177; and

-- bill sections 52 - 56, substituting "nonconventional gas" in various references to "shallow natural gas" in title 46; this title of the Alaska Statutes generally deals with environmental matters.

AUTHORIZING THE DEPARTMENT OF NATURAL RESOURCES TO LEASE FOR "GAS ONLY" UNDER THE CONVENTIONAL OIL AND GAS LEASING PROCEDURES, WITH LIMITED RESERVATIONS GOVERNING ACTIVITY INVOLVING NONCONVENTIONAL GAS LEASES, AND MAKING CONFORMING CHANGES:

AS 38.05.180(ff), added by bill section 43, explicitly authorizes the Department of Natural Resources to "issue leases for gas only" under the conventional oil and gas leasing program.

Out of an abundance of drafting caution, the following revise or delete existing references to "oil and gas," "oil and gas lease," or substantially similar terms and references to acknowledge the alternative authorization of "gas only" leasing:

-- bill sections 1, 3, 7 - 9, 10 (except the repeal of AS 38.05.035(e)(6)(G) [page 12, lines 4 - 6]), 11, 13, 32 - 35, 36 (except the addition of AS 38.05.180(f)(3)(H) [page 26, lines 18 - 23]), 37 - 42, 44 - 51, and 57.

AUTHORIZING THE DEPARTMENT OF NATURAL RESOURCES TO USE EXPLORATION LICENSING AND LEASING FOR "GAS ONLY" UNDER AS 38.05.131 - 38.05.134, AND MAKING CONFORMING CHANGES:

Bill section 14, amending AS 38.05.131(a), explicitly authorizes the Department of Natural Resources to issue exploration licenses and leases for "gas only." The following provisions make related conforming changes:

-- bill sections 2, 12, 15 - 21, 22 (except the language of new subparagraph (B) [page 19, lines 2 - 7]), and 24.

PROVISIONS ALTERING OR REPEALING SPECIFIC PARTS OF AS 38.05.177, ADDRESSING SHALLOW NATURAL GAS LEASING:

These remarks principally address the content of bill sections 26 - 31 and the repeal of certain subsections in AS 38.05.177, the shallow natural gas leasing section.

Certain subsections are amended with the intent that their specific provisions override comparable provisions in the conventional oil and gas leasing section, AS 38.05.180. So,

-- AS 38.05.177(a) (bill section 26): In addition to substituting reference to "nonconventional gas," the measure is amended to eliminate the language in it that prohibits shallow gas as something that may be addressed under the existing oil and gas exploration licensing and leasing sections;

-- AS 38.05.177(f) (bill section 27): In addition to substituting reference to "nonconventional gas," the subsection is amended to retain the one dollar rent schedule covering nonconventional gas leases, notwithstanding a different schedule in AS 38.05.180(n);

-- AS 38.05.177(g) (bill section 28): In addition to substituting reference to "nonconventional gas," this subsection deletes material relating to the royalty payable on the gas; this element is, instead, addressed in an amendment to AS 38.05.180(f)(3)(H);

-- AS 38.05.177(j) and (k) (bill sections 29 and 30): These subsections are amended to substitute the reference to "nonconventional gas";

-- AS 38.05.177(o) (bill section 31): Note the new definition here of "nonconventional gas."

As to other parts of AS 38.05.177, bill section 58 repeals the following:

-- AS 38.05.177(b): This subsection currently sets maximum acreage limitations (paragraph (1)) and levies an application fee (paragraph (2)). If gas only leases are to be issued for unconventional gas under AS 38.05.180, then acreage limits of AS 38.05.180(m) should apply, and maximum holding provisions for oil or gas leases set out in AS 38.05.140(c) should also. In the main, oil and gas leases are offered as competitive leases, so there would not be an application process and, hence, a separate application fee for a noncompetitive lease would not be collected. Consequently, this subsection is to be repealed in its entirety.

-- AS 38.05.177(c): This subsection sets out the notice and public comment provisions. Conventional oil and gas leases have different notice provisions, AS 38.05.945(a)(3), and those should operate in lieu of the expedited notice/public comments of this subsection. Again, this subsection is to be repealed in its entirety.

-- AS 38.05.177(d) and (e): These subsections are the lease extension and lease boundary adjustment provisions. Comparable provisions for conventional oil and gas leases appear in AS 38.05.180(m) and should operate in lieu of sec. 177(d) and (e). These subsections are therefore to be repealed.

-- AS 38.05.177(h): This is the lease surrender or relinquishment provision. As leasing would occur under AS 38.05.180, provisions covering these subjects under authority of that section would apply, so this subsection may be repealed.

-- AS 38.05.177(m): This is the lease extension provision. Again, because leasing would occur under the conventional oil and gas leasing procedures of AS 38.05.180, provisions covering these subjects under authority of that section would apply, so that this subsection is being repealed.

OTHER BILL SECTIONS THAT ARE NOT ADDRESSED OR CONSIDERED ABOVE:

Bill section 10: The repeal of AS 38.05.035(e)(6)(G), page 12, lines 4 - 6, drops the exemption for shallow natural gas leasing from the written finding requirements of that subsection. Before nonconventional gas leasing may occur, proposed nonconventional leases would be required to be supported by a written best interest finding.¹

Bill sections 22 (page 19, lines 2 - 7) and 36 (page 26, lines 18 - 23): For purposes of retention of the reduced royalty authorized for certain gas, these two amendments add, as to nonconventional gas exploration licensing and leasing and nonconventional gas leasing under the leasing program of AS 38.05.180, provisions for a reduced royalty for nonconventional gas "not produced in direct competition with gas on which a royalty at rate of at least 12.5 percent is payable." Similar language in the existing provision, AS 38.05.177(g), is to be repealed.

Bill sections 23 and 25: Both provisions are concerned with the relationship between coal and coal bed generated methane. The amendments remove references to shallow natural gas (coal bed methane) leasing under AS 38.05.177.

Bill section 58: In addition to the repeal of specific subsections of AS 38.05.177 described above, the section would repeal paragraphs setting out definitions of "shallow natural gas" in AS 31.05 and AS 46.04. Each repeal is matched (bill sections 6 and 55) with addition of definitions for the substituted term, "nonconventional gas."

Bill section 59: This transitional provision directs the Department of Natural Resources to deal with shallow natural gas leases executed and lease applications received by December 31, 2003, under the provisions of AS 38.05.177 as it read before its amendment by this Act.

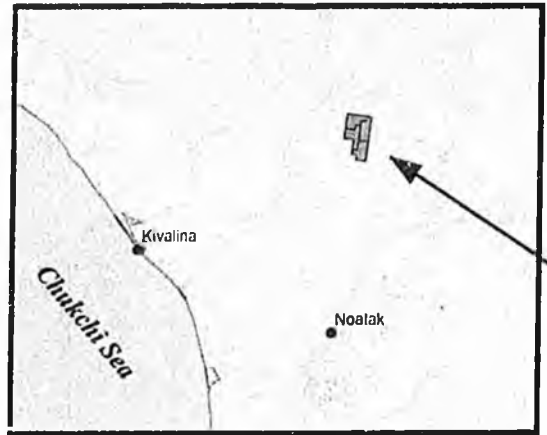
Bill section 60 gives the measure an immediate effective date.

JBC:lmb
04-027.lmb

¹ The lead-in to AS 38.05.035(e)(6) setting out the required written best interest finding appears in the text of the bill at page 10, line 29 - page 11, line 6.

Shallow Natural Gas Leases

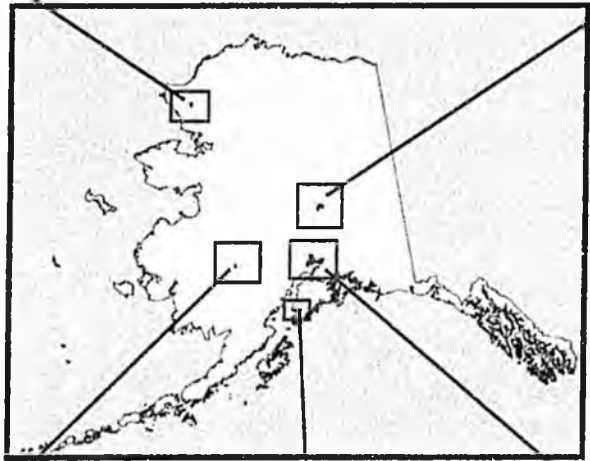
■ Issued Leases
□ Applications



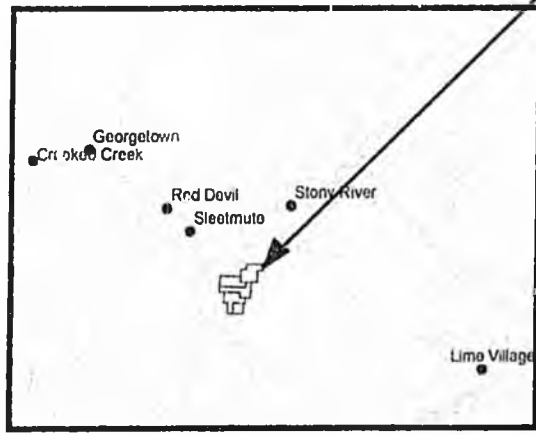
Red Dog



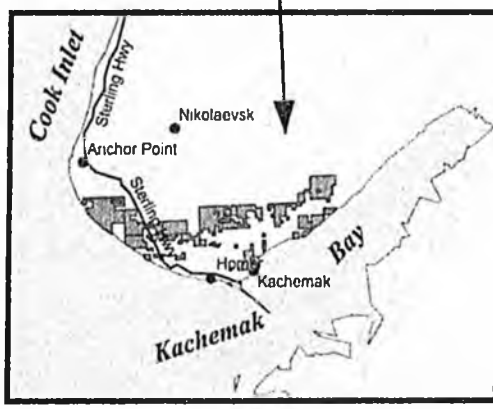
Healy



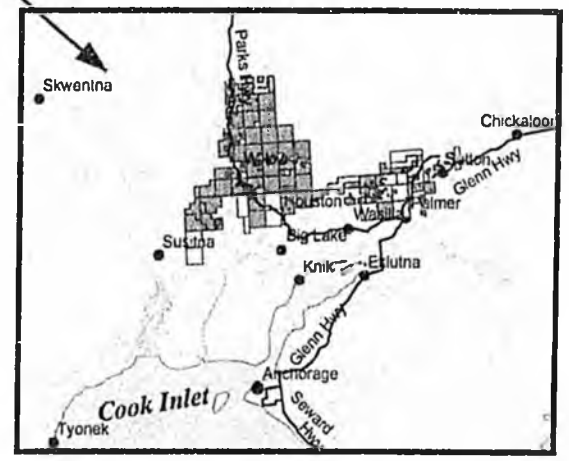
Holitna Basin



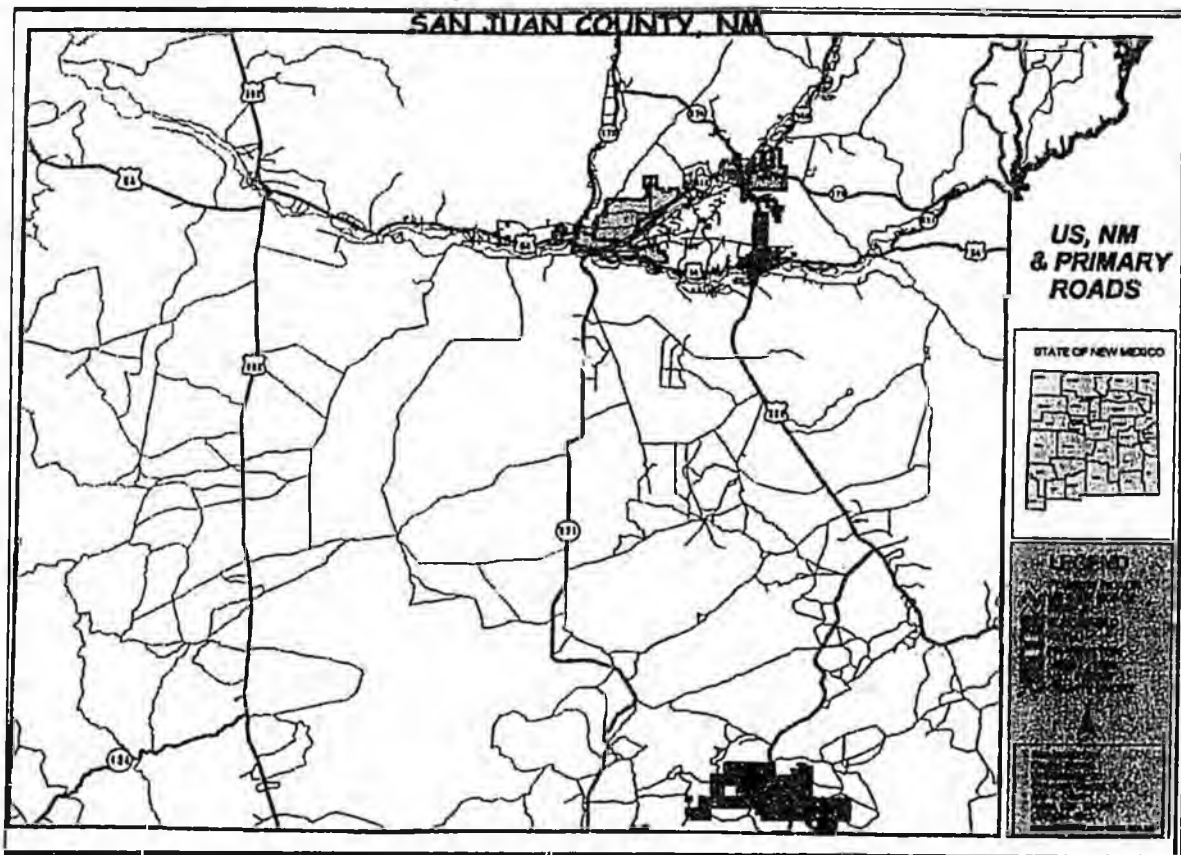
Kenai Peninsula



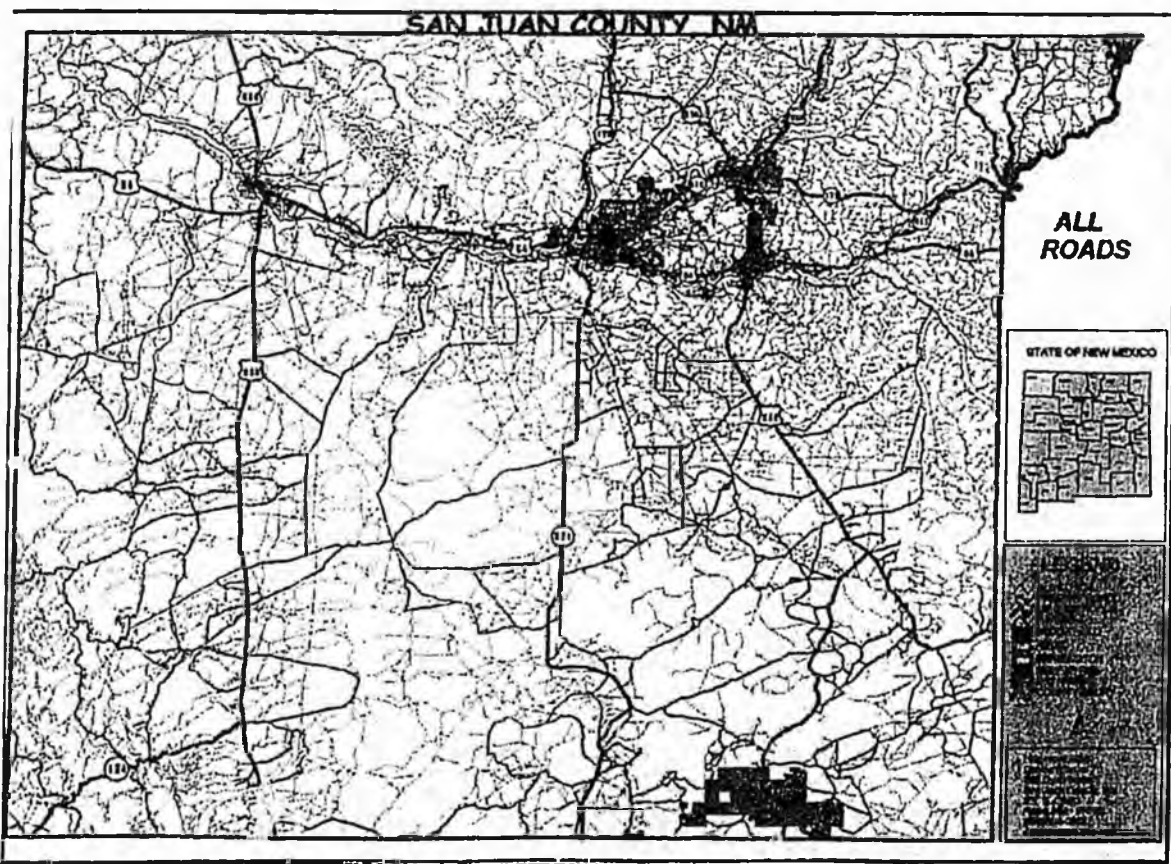
Mat-Su



Fifteen Years of Coalbed Methane Before



After



The Future of the Matanuska Moose Range?

Sponsors: Colver and Kvalheim
Amended by Substitution: 03/02/04
Amended: 03/02/04
Adopted: 03/02/04
Motion to Reconsider Failed: 03/02/04

MATANUSKA-SUSITNA BOROUGH
RESOLUTION SERIAL NO. 04-035 (SUB) (AM)

A RESOLUTION OF THE MATANUSKA-SUSITNA BOROUGH ASSEMBLY MAKING
RECOMMENDATIONS TO THE GOVERNOR AND LEGISLATURE CONCERNING COAL BED
METHANE LEGISLATION AND REGULATIONS.

WHEREAS, various bills have been introduced in the Alaska
Legislature addressing shallow gas issues in the state of Alaska;
and

WHEREAS, the public is concerned about surface impacts from
coal bed methane activity on privately owned properties; and

WHEREAS, the Alaska State Department of Natural Resources is
holding coal bed methane workshops to involve the public in making
recommendations to state and local governments for the adoption of
regulations; and

WHEREAS, the Matanuska-Susitna Borough Assembly supports best
practices for coal bed methane exploration, drilling, and
production operations.

NOW, THEREFORE, BE IT RESOLVED, that the Matanuska-Susitna
Borough Assembly respectfully requests that the Governor and
Legislature consider coal bed methane legislation that includes the
following surface protections:

- noise mitigation requirements for compressor stations;

- minimum setbacks from residences and property lines for wellheads and compressor stations;
- require lessees to submit a master plan locating all facilities and improvements to afford the opportunity for comments by the public; and
- require safety buffers.

BE IT FURTHER RESOLVED, that the Matanuska-Susitna Borough Assembly respectfully requests that coal bed methane legislation include the following surface landowner protections:

- surface owners should have the ability to negotiate fair and equitable terms for surface use of their property;
- require an Alaska State Department of Natural Resources and Alaska State Oil and Gas Conservation Commission permit before entry or construction upon on a privately owned parcel; the permit shall provide for negotiation and location of any improvements; and
- adequate bonding to make the surface landowner whole if water resources or other impacts to the property affects the use, enjoyment, and value of their property.

BE IT FURTHER RESOLVED, that the Matanuska-Susitna Borough Assembly will support legislation that accomplishes the intent of this resolution.


BE IT FURTHER RESOLVED, that the Matanuska-Susitna Borough Assembly respectfully requests that coal bed methane legislation include the following subsurface and water quality protections:

require regulations to be adopted by the Alaska State Oil and Gas Conservation Commission requiring:

- o re-injection of produced water well below known drinking and agricultural water aquifers; and
- o neutral party testing and monitoring at the expense of the state or developer of all re-injected fluids and drinking water before, during, and after drilling activity.

BE IT FURTHER RESOLVED, that the Matanuska-Susitna Borough Assembly respectfully requests that the Alaska State Legislature amend State statutes to repeal the authority of the Commissioner of Natural Resources to override local government regulations.

ADOPTED by the Matanuska-Susitna Borough Assembly this 2 day of March, 2004.


TIMOTHY L. ANDERSON, Borough Mayor

ATTEST:


SANDRA A. DILLON, CMC, Borough Clerk

(SEAL)

PASSED UNANIMOUSLY: Bush, Allen, Colberg, Kvalheim, Simpson, Colver, and Vehrs

Sponsors: Colver and Kvalheim
Adopted: 03/02/04
Motion to Reconsider Failed: 03/02/04

MATANUSKA-SUSITNA BOROUGH
RESOLUTION SERIAL NO. 04-036

A RESOLUTION OF THE MATANUSKA-SUSITNA BOROUGH ASSEMBLY MAKING RECOMMENDATIONS TO THE GOVERNOR AND LEGISLATURE CONCERNING REFORM OF SHALLOW GAS LEASING FOR COAL BED METHANE.

WHEREAS, various bills have been introduced in the Alaska Legislature addressing shallow gas issues in the state of Alaska; and

WHEREAS, the state of Alaska's shallow gas leasing program does not require a "Best Interest Finding," which is required before competitive oil and gas leases are offered; and

WHEREAS, the Matanuska-Susitna Borough Assembly supports reform of the way in which state-owned subsurface estates are leased for shallow gas coal bed methane exploration and production; and


WHEREAS, the Matanuska-Susitna Borough supports public involvement, adequate notice, and incorporation of public comments into a decision whether to offer leases and identifying the location of areas for leasing for shallow gas.

NOW, THEREFORE, BE IT RESOLVED, that the Matanuska-Susitna Borough Assembly supports the reform of the leasing process for shallow gas and supports legislation which:

- requires a competitive lease process for shallow gas;

- requires a "Best Interest Finding" prior to offering leases;
- provides for adequately published public notice and notification to individual property owners within proposed lease areas and hold public hearings;
- provides for public hearings; and
- incorporates public comments received and local government concerns before offering any leases for shallow gas.

ADOPTED by the Matanuska-Susitna Borough Assembly this 2 day of March, 2004.


TIMOTHY L. ANDERSON, Borough Mayor

ATTEST:


SANDRA A. DILLON, CMC, Borough Clerk

(SEAL)

PASSED UNANIMOUSLY: Bush, Allen, Colberg, Kvalheim, Simpson,
Colver, and Vehrs

P.O. Box 766
Talkeetna, AK 99676
February 21, 2004

Senator Scott Ogan
Alaska State Senate

Via Fax: 907-465-3265

Dear Senator Ogan:

These are my thoughts on the pressing need for remedial Coalbed Methane legislation.

There are many provisions in the current CBM statutes that are counter to the public interest,¹ but the most disturbing is the lack of a "best interest finding" requirement as relates to the CBM leasing program. Every oil and gas program in Alaska that I know about requires a best interest finding, or cost-benefit assessment, prior to approving a lease. How else would the State determine whether a lease is in its best interest?

Under current law the only criteria for issuing or denying a CBM lease application, is the poorly crafted statement "if...the discovery of a local source of natural gas would benefit the residents of an area, the director shall execute the lease." This language virtually compels the approval of the lease. This is bad public policy. The present CBM program puts industry in the driver's seat, and subordinates the interests of local government bodies, local communities, private property owners, and, in some cases, even the State itself to the interests of the industry. Remember, these are the State's resources, yours and mine, and it is unconscionable for the legislature to grant industry virtually unfettered discretion to determine when and where these resources are developed. I hope you realize that this must be corrected without further delay.

The best interest finding requirement would mandate consideration of, among other things, the use and value of the surface estate and thus give DNR the discretion to reject a lease application without fear of being sued by the applicant. **The CBM program would yield a lot better result for all concerned if a best interest finding is required, just as it is for every other oil and gas program. Please work to include it in any CBM legislation that comes before the Senate.**

¹ Among these troubling provisions are the override of local control, exemption from important environmental regulations, an unreasonably curtailed public process, failure to consider the uses and value of the surface estate when determining whether to issue a lease, leases are issued on a non-competitive first-come-first-served basis, reducing (subject to narrow exceptions) the normal oil and gas royalty by half... the list goes on.

It is time to hit the rewind button, buy back the existing leases on the Kenai Peninsula and in the Mat-Su Valley, and then apply the best interest finding requirement to all future lease applications. Please support these two vital provisions.

CBM development has exceedingly high surface impacts. Production of a given amount of gas takes a far greater number of wells and well pads than conventional drilling (which can, with directional drilling, drill several wells from the same pad). With CBM, it is one well per pad, and these must all be connected by roads, pipelines, power lines, etc. The adverse impacts to our private property, to our communities, to our hunting and fishing, and to any businesses based on tourism or outdoor recreation are enormous and unacceptable. I want any legislation to contain meaningful, substantive protections for my private property and my community.

I urge inclusion of strong protective provisions regarding better public notice, setbacks from water and wetlands, buffers for homes and cabins, noise level caps, protection of water quantity and quality, land restoration, higher bonding requirements, landowner compensation, stronger negotiating position for the landowner, well density limits, lighting restrictions, and so on. But, having said that, public notice isn't worth a thing if DNR isn't required, or even permitted, to give substantive weight to public comments. And, further, all these protections represent helpful, but in the end, only marginal mitigation in the face of enormous disruption of our lives and our communities. Clearly, there are places where CBM development is simply not appropriate.

.....which gets us back to the best interest finding requirement for the CBM leasing program. This and the lease buyback are absolutely necessary parts of CBM legislation.

Thank you for considering these comments.

Sincerely,



John Strassenburgh

Phil St. George
Holitna Energy Co. LLC
9237 W. Parkview T.Lp.
Eagle River, AK 99577
(907) 694-8728
philstgeorge@msn.com

SENATOR SCOTT OGAN
State Capitol, Room 103
Juneau Alaska 99801

Dear Senator,

February 26, 2004

We support your past work regarding shallow gas leases. These efforts resulted in our application for shallow gas leases in the Holitna basin, southwest Alaska. The existing laws and regulations that were in place at the time of application provided strong motivation for a small company to acquire land and develop the resources on that land.

As a result of the Mat/Su Valley public outcry, the state seems to have over reacted to address the complaints of a few, at the expense of Alaska's future. We wish the state would stay the course and continue to encourage development on State lands. We don't think any new legislation is necessary but we understand the Shallow Gas Lease program will be terminated and you are authoring a new bill, SB 312.

It is obvious that large companies (in both the oil and gas business as well as in mining) have drastically reduced exploration in Alaska. Because of this the state has to encourage small to medium sized companies to explore here.

Small and medium sized companies can not afford to have large expenses or extensive delays prior to acquiring tenure to the land and accomplish the first drill hole. If SB 312 is going to replace the Shallow Gas Leasing program it should not have a "Best Interest Finding" as part of acquiring tenure to the land. If this was required prior to staking a mining claim, all claim staking activities would stop. I think this will have a drastic affect on gas leases in rural locations.

A "Best Interest Finding" is really more of a development issue, and should be addressed in the development stage, when those costs and delays are apart of an EIS or EA process. In rural settings a best interest will undoubtedly find that it's in the states best interest to develop its resources, so why require a study whose outcome is a forgone conclusion. Do the study when there is more information on what the development of the field will entail, during the permitting for the development.

If you are trying to protect local land owners from gas development, certain populated areas in the state could be exempt from leases without a best interest

finding. Keep the best of the Shallow Gas Leasing program in the rural areas and tighten controls in populated areas.

A low royalty rate, such as the existing 6.25% on Shallow Gas Leases is another important aspect of attracting small to medium sized companies. Without this low rate a small company has no opportunity to acquire land, put the information together and finance the property. That difference between 6.25% and 12% is typically all that is left to the original lease holder, and is all we are expecting to retain in the Holitna basin. If that hadn't been the case, there still would not be anyone with leases out in the Holitna basin.

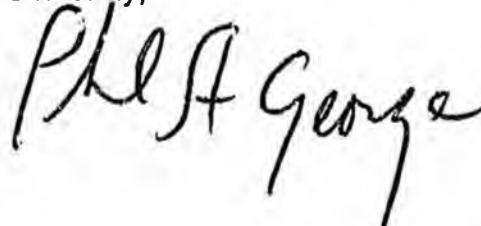
We also hope that the Shallow Gas Leasing program is not terminated until the new legislation is functioning. It would be a shame to have a gap of time prior to a new program taking effect and you are probably well aware how long it took to implement the existing laws.

We feel that DNR does not have sufficient staff to handle these more demanding leases. We suggest additional personnel would speed the lease application process. These new leases will certainly more than pay for the added attention. If we find gas, the royalty to the state from just the Holitna leases will provide approximately \$1.7M per year and after payback approximately \$400K in tax revenues. Also, once gas is taken to Bethel the Federal and State Government will save over \$3M per year on the Power Cost Equalization Program. There will be other saving once Donlin is operating, a local tax base will save on school budgets and other local subsidies from the state.

We feel the current arrangement of permitting and regulating wells will be overwhelmed when a couple of coal bed methane fields go into production. Quite a few states such as Wyoming and Colorado have learned to cope with this problem and we hope DNR can learn from these examples. We know from past history in mining and our recent experience permitting two core holes that there is a conflict between DNR and DEC. This needs to be resolved prior to any large increase in production from shallow gas wells. We suggest the one stop shopping approach, where DNR would have oversight of all permitting with the State of Alaska.

Without the proper incentives other interior basins may be neglected. And as you are probably aware, Alaska is a coal rich terrain with potential for shallow gas in almost any small basin in the state. The Nenana basin will undoubtedly provide gas to Fairbanks. These interior basins could supply energy for almost any significant project that comes along in the future and hopefully will someday power many rural communities.

Sincerely,

A handwritten signature in black ink that reads "Phil A George". The signature is written in a cursive, slightly slanted style.

Subject: comments on SB 312

Date: Thu, 26 Feb 2004 14:57:17 -0900

From: "PHIL ST GEORGE" <philstgeorge@msn.com>

To: "Scott Ogan" <Senator_Scott_Ogan@legis.state.ak.us>

CC: "Gene Piekenbrock" <piekenbrock@gci.net>

<?xml:namespace prefix="v" /><?xml:namespace prefix="o" />
Scott,

Attached is a letter regarding my company's thoughts on SB 312. Please forward this to the other Resource committee members. I think my company could be the poster child for rural shallow gas development. We are developing the Holitna basin to supply gas to Southwest Alaska and the Donlin Creek Mine. We feel the Shallow Gas Program is fantastic and hope its best attributes can be incorporated into SB 312. Alaska will suffer from underdevelopment and will continue its dependence on imported diesel if the best of the Shallow Gas Leasing program is not incorporated. I hope I can testify at the hearings on Monday.

Here is the letter pasted into this text for quick review, but the document will be easier for printing:

Dear Senator,

February 26, 2004

We support your past work regarding shallow gas leases. These efforts resulted in our application for shallow gas leases in the Holitna basin, southwest Alaska. The existing laws and regulations that were in place at the time of application provided strong motivation for a small company to acquire land and develop the resources on that land.

As a result of the Mat/Su Valley public outcry, the state seems to have over reacted to address the complaints of a few, at the expense of Alaska's future. We wish the state would stay the course and continue to encourage development on State lands. We don't think any new legislation is necessary but we understand the Shallow Gas Lease program will be terminated and you are authoring a new bill, SB 312.

It is obvious that large companies (in both the oil and gas business as well as in mining) have drastically reduced exploration in Alaska. Because of this the state has to encourage small to medium sized companies to explore here.

Small and medium sized companies can not afford to have large expenses or extensive delays prior to acquiring tenure to the land and accomplish the first drill hole. If SB 312 is going to replace the Shallow Gas Leasing program it should not have a "Best Interest Finding" as part of acquiring tenure to the land. If this was required prior to staking a mining claim, all claim staking activities would stop. I think this will have a drastic affect on gas leases in rural locations.

A "Best Interest Finding" is really more of a development issue, and should be addressed in the development stage, when those costs and delays are apart of an EIS or EA process. In rural settings a best interest will undoubtedly find that it's in the states best interest to develop its resources, so why require a study whose outcome is a forgone conclusion. Do the study when there is more information on what the development of the field will entail, during the permitting for the development.

If you are trying to protect local land owners from gas development, certain populated areas in the state could be exempt from leases without a best interest finding. Keep the best of the Shallow Gas Leasing program in the rural areas and tighten controls in populated areas.

A low royalty rate, such as the existing 6.25% on Shallow Gas Leases is another important aspect of attracting small to medium sized companies. Without this low rate a small company has no opportunity to acquire land, put the information together and finance the property. That difference between 6.25% and 12% is typically all that is left to the original lease holder, and is all we are expecting to retain in the Holitna basin. If that hadn't been the case, there still would not be anyone with leases out in the Holitna basin.

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Sincerely,

Phil St. George
Holitna/Naniq Energy Co. LLC
9237 W. Parkview T.Lp.
Eagle River, AK 99577
(907) 694-8728 wk/hm
(907) 360-8728 cell
(509)561-7732 fax



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February 23, 2004

Senate Resources Committee
State Capitol
Juneau, AK

Dear Senator Ogan,

Thank you for dealing with the important public issue of coal bed methane leasing.

The *AML Land Use, Resources, and Economic Development Subcommittee* met February 23, 2004 to comment on strengthening the local public participation component of proposed state bills dealing with coal bed methane leasing.

AML Resolution 2004-12 adopted November, 2003 by the membership at the Annual Local Government Conference supports the *"...efficient and economic development of this important resource, while protecting owners' rights and providing for the partnership of local citizens and local governments in developing laws and regulations necessary for the protection of water, air, land use and quality of life..."*

The AML subcommittee believes that it is in the interest of the public for the state to participate fully in the same local review process that would apply to any other landowner or developer. Municipal governments are in the business of not only dealing with such issues in a balanced manner, but in facilitating the notice and participation of affected members of the public. For example, recently the Mat-Su Borough sent notices of state hearings to residents of the borough to facilitate the state's public process.

The two conceptual recommendations of the AML subcommittee are:

- Consider deleting or modifying AS 38.05.177 (n) added last year to allow the DNR Commissioner to "approve a waiver of local planning authority approval and requirements relating to compliance with local ordinances and regulations."
- Add language concerning advance notice to municipalities and coordination of state and municipal processes.

Sincerely

Kevin Ritchie
Executive Director

Cc: AML Board of Directors and Legislative Committee