

OIL TAX REFORM: GROSS REVENUE EXCLUSION

House Finance Committee

April 6, 2013

Department of Natural Resources

- Joe Balash, Deputy Commissioner
- Bill Barron, Director, Division of Oil & Gas



HOW DOES PRODUCTION QUALIFY *for the GRE?*

There are three ways to qualify:

1. Production from a Unit formed after 2003
 - Nikaitchuq Unit, Oooguruk Unit
2. Production from a PA formed after 2012 which is in a unit formed prior to 2003
 - New PA at Prudhoe Bay
3. Production from acreage that was added to an existing participating area by DNR on and after January 1, 2014, and the producer demonstrates to DNR that the volume of oil or gas produced is from acreage added to an existing participating area

LEASING & UNITIZATION

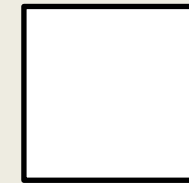
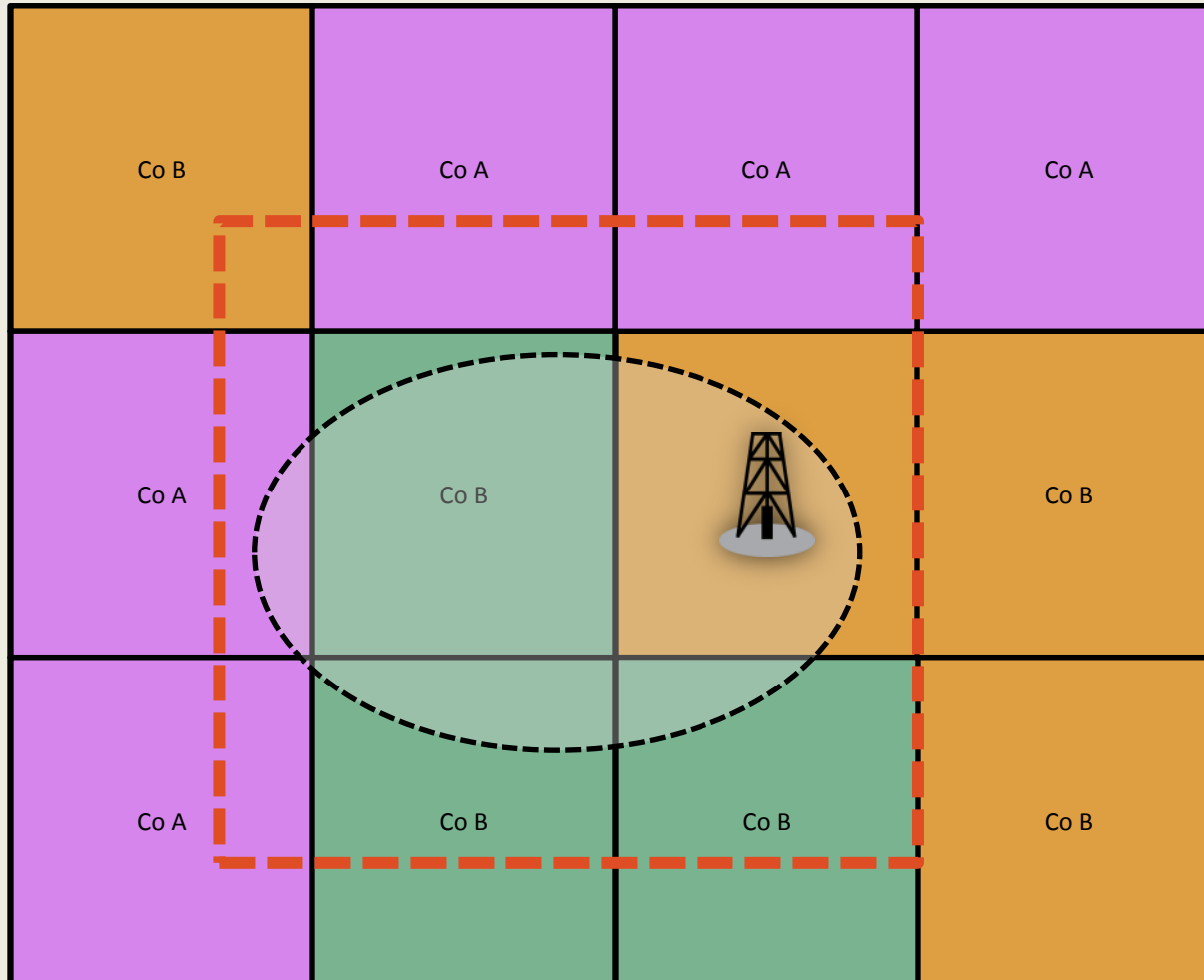
Leasing is the primary mechanism by which the State grants exclusive rights to explore and develop the oil and gas mineral rights of the State to private parties

- Competitive bidding
- Terms and conditions have varied over time
- Tracts are generally 3x3 miles, except in prime shale areas

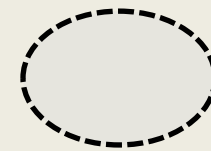
Unitization is the mechanism to join contiguous leased tracts together into a unit in order to

- Protect the interests of all parties, including the state
- Ensure proper reservoir management, and
- Enhance recovery of reserves

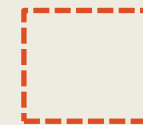
UNITIZATION



Tract Boundaries



Delineated Reservoir



Proposed Unit Boundary

WHAT *is a* PARTICIPATING AREA (PA)?

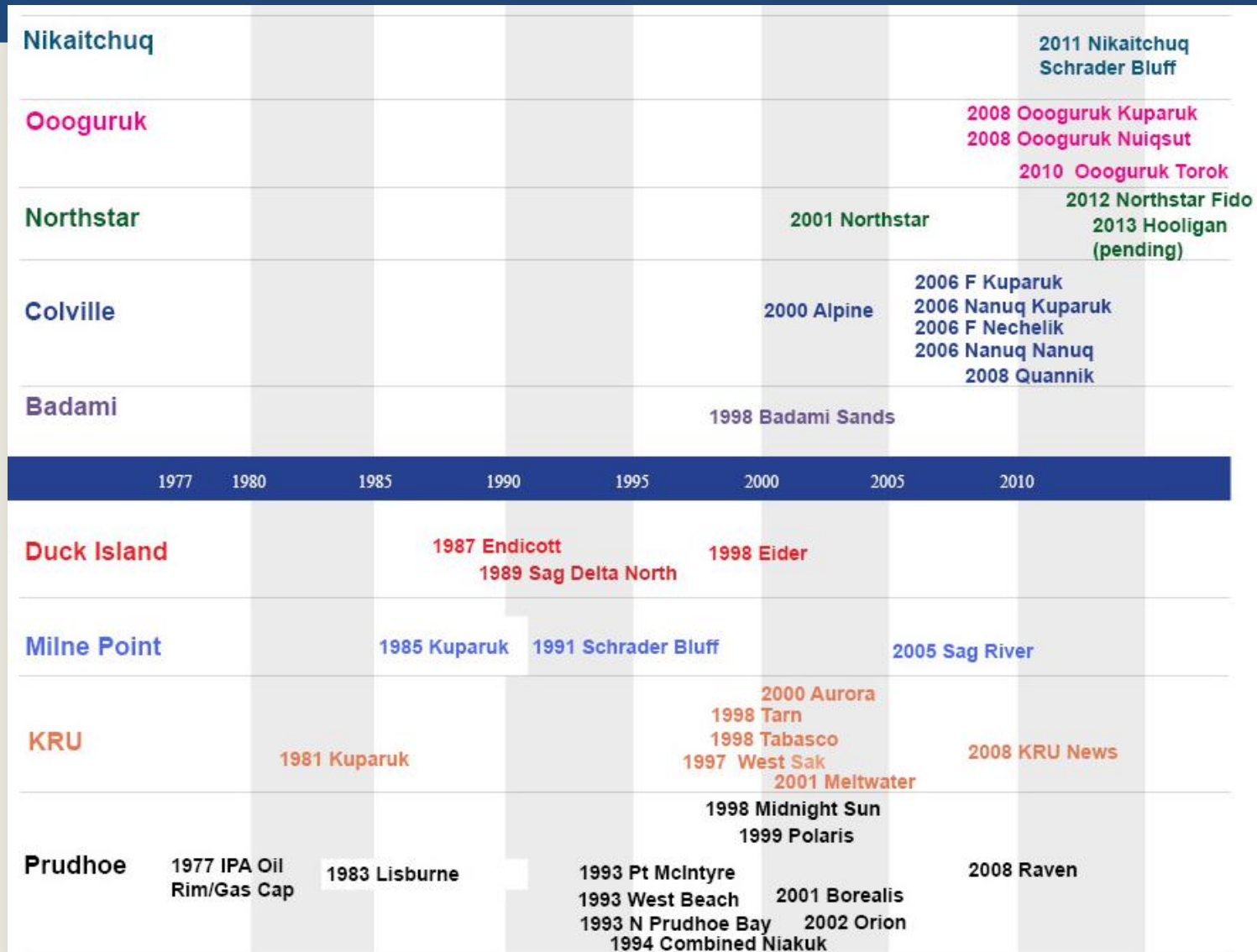
A set of tracts within a Unit, overlying a reservoir which is on sustained production

- North Slope: 18 State Units, 38 PAs
- A unit may have multiple reservoirs at different depths – each PA is defined vertically as well as horizontally
- Leases approved for inclusion into a PA may not be severed
- PA provides mechanism to allocate costs and revenues

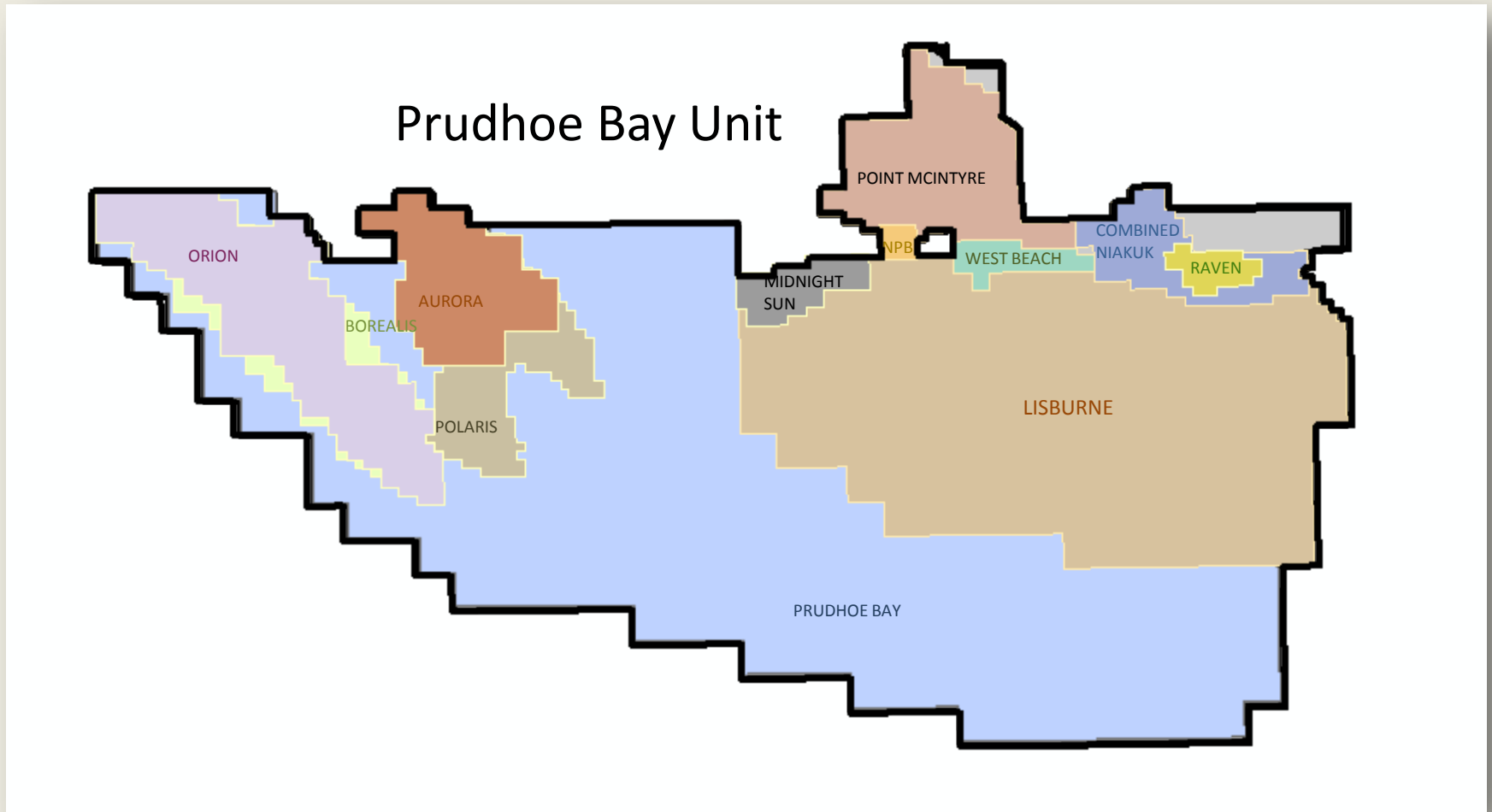
Regulations

- 11 AAC 83.351 PA Formation, Expansion, Contraction
- 11 AAC 83.343 Plans of Development
- 11 AAC 83.371 Allocation of Production and Costs
- 11 AAC 83.303 Protect all parties

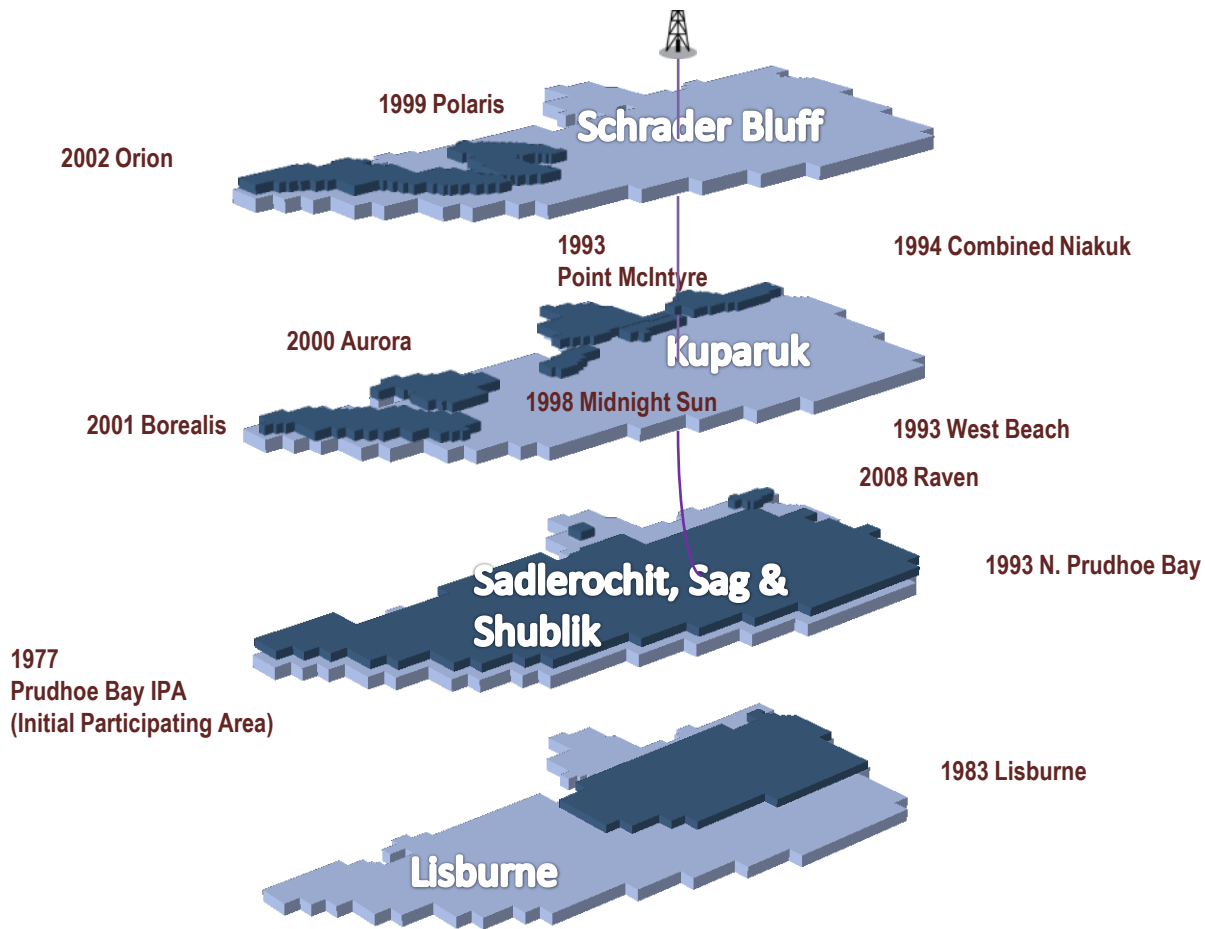
NORTH SLOPE PAs



PRUDHOE BAY UNIT



PRUDHOE BAY UNIT



EVALUATION *and* APPROVAL *of* PAs

11 AAC 83.351: PA Formation, Expansion, Contraction

- PA may include only the land capable of producing or contributing to production of hydrocarbons in paying quantities
- PA must be contracted to exclude acreage incapable of contributing to production of hydrocarbons in paying quantities

11 AAC 83.303 Criteria

- Promote conservation
- Prevent waste
- Protect all parties

EVALUATION *and* APPROVAL *of* PAs

PA application has no regulatory deadline as with unit applications

- Operator submits application no later than 90 days prior to sustained production
- Submittal includes Exhibits C and D, legal description with allocation factors, and map
 - Allocation factors allocate production to each tract
- Must include Exhibits E and F if Net Profit Share (NPS) leases included
 - NPS leases require accounting of costs and revenues to determine “pay out”. Exhibits E and F provides methodology and basis for cost allocation, used by Royalty Accounting and Audit

PA EXHIBITS C and D

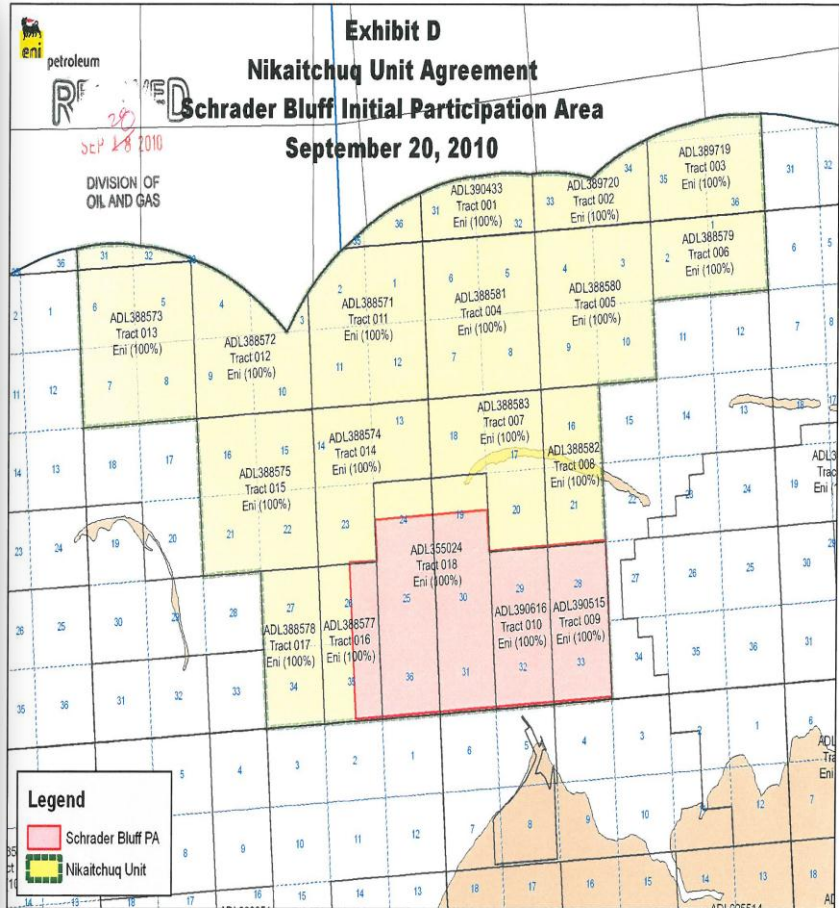
NIKAITCHUQ UNIT AGREEMENT: Exhibit C SCHRADER BLUFF PARTICIPATING AREA Nikaitchuq Unit Area

September 20, 2010

Nikaitchuq Unit Tract Number	Lease/ Royalty Owner Lease Serial No.	Description of Unleased Lands	Unleased Acres Within Participating Area	Royalty Rate	ORRI Owners	Owering Royalty Interest	Working Interest Owners & Percentage Working Interest	Unit/Tract Participation (Based on Surface Area)	
9	350615	THAN, R.B.E., UMAT MERIDIAN Sec: 28 Protracted, AI Sec: 33 Protracted, AI	640.0000	0.18887	GMT Exploration North Slope Royalty Company, LLC	0.13333	Eni 100%	28.19%	
			640.0000			0.72787			
			1280.0000			0.02187			
						0.02187			
						0.02187			
						0.02187			
						0.02187			
						0.02187			
						0.02187			
						0.02187			
	0.02187		0.00887						
		total			0.89999				
10	390816	THAN, R.B.E., UMAT MERIDIAN Sec: 20 Protracted, AI Sec: 32 Protracted, AI	640.0000	0.18887	GMT Exploration North Slope Royalty Company, LLC	0.13333	Eni 100%	28.19%	
			640.0000			0.72787			
			1280.0000			0.02187			
						0.02187			
						0.02187			
						0.02187			
						0.02187			
						0.02187			
						0.02187			
						0.02187			
		total			0.89999				
16	388377	THAN, R.B.E., UMAT MERIDIAN Sec: 28 Protracted, Tide and submerged lands, E2 Sec: 35 Protracted, Tide and submerged lands, E2	320.0000	0.18887	ConocoPhillips	4.200%	Eni 100%	10.08%	
			320.0000						
			640.0000			total			4.200%
18	391283	THAN, R.B.E., UMAT MERIDIAN Segment 2 Sec: 34 Protracted, S2 Sec: 25 Protracted, AI Sec: 35 Protracted, AI THAN, R.B.E., UMAT MERIDIAN Sec: 19 Protracted, S2 Sec: 30 Protracted, AI Sec: 31 Protracted, AI	320.0000	0.13500	ConocoPhillips	3.394%	Eni 100%	48.82%	
			640.0000			30% NPS			2.327%
			640.0000			BP			0.200%
						Exxon			0.287%
						Urocal			0.48810%
			308.8000			William D. Armstrong			0.014580%
			630.0000			Jesse V. Sommer			0.014580%
			623.0000			Edgar Klar			0.014580%
			3151.8000			Jeffrey A. Lytle			0.014580%
						Patricia M. Reed			0.014580%
	Matthew K. Furr	0.014580%							
	Stuart W. Gustafson	0.014580%							
	Chester E. Paris	0.008850%							
	GMT Exploration Company, LLC	0.08850%							
		total	6.848822%						
Total Unleased Land Within Participating Area:			6361.5000						
Total State Land:			6361.5000						
Total NLM Land:			33.0000						
Total Unleased Land:			6,394.50						

1 of 1

RECEIVED
SEP 28 2010
DIVISION OF OIL AND GAS



PA PLAN *of* DEVELOPMENT

Once development activities commence and/or a PA is formed, a Plan of Development (POD) is required under 11 AAC 83.343

- Describes plans to develop the reservoir
 - Development activities: facilities, pipelines, offshore production islands, gathering lines, and permanent drill sites
- POD is submitted annually for review and approval
- If POD deemed insufficient for approval, DNR may propose modifications. If Operator agrees to modification, POD approved
 - If modifications not accepted by Operator and reviewed POD not approved, current POD may expire

TRACT ALLOCATION FACTORS

11 AAC 83.371

- Approval of PA includes approval of Allocation Factors (Tract Factors or TF) to protect all parties
 - Exhibit C designates each PA tract a TF
 - Bases for calculating TF proscribed in Operating Agreement sometimes Unit Agreement or approval decision
 - Acreage
 - Original Oil in Place (OOIP)
 - Recoverable
 - Value Based
- Working Interest Owners receive revenue based on TF
 - Equity negotiations
- State of Alaska receives royalties based on TF
 - Commercial interest evaluation

REVISIONS *to* DIVISION *of* INTEREST: REALLOCATIONS

- **Production is reallocated**

- As PA expands of contracts

- Development wells identified and committed to in Plan of Development
- Expansion of Milne Point Unit Sag River PA
- Contraction of Milne Point Unit Sag River PA

- As basis for allocation changes

- Field matures, more technical information gathered and evaluated, production is reallocated
- Revised Exhibit C designates each PA tract a TF
- Bases for calculating TF proscribed in Operating Agreement sometimes Unit Agreement or approval decision
 - Acreage, OOIP, Recoverable, Value Based

- Resource Evaluation, Commercial, Royalty Accounting, Audit Sections

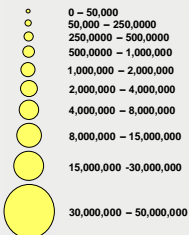
- Evaluation of protection of State's Interest
- Protection of all parties

KUPARUK RIVER UNIT (KRU)

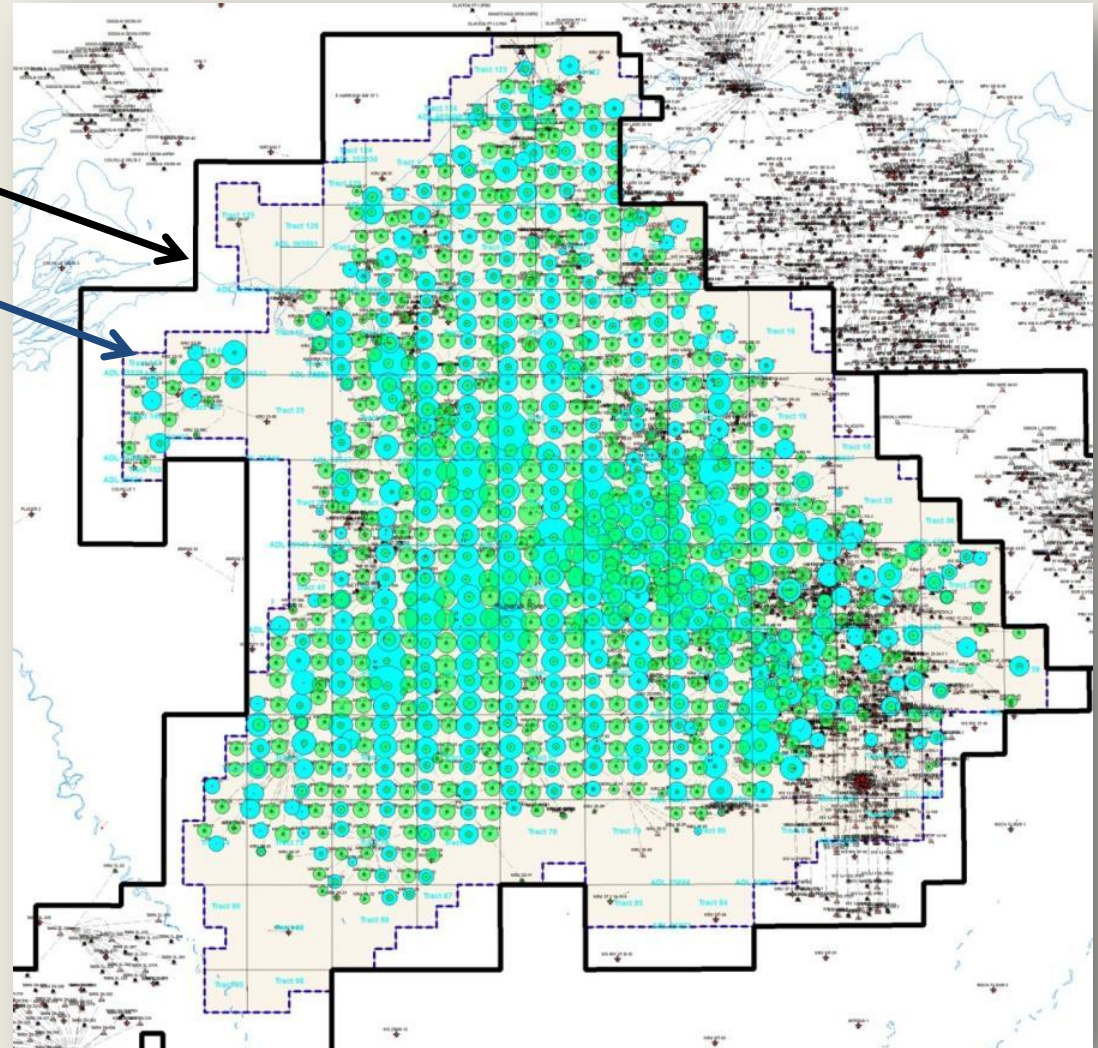
KRU Boundary

Kuparuk PA Boundary

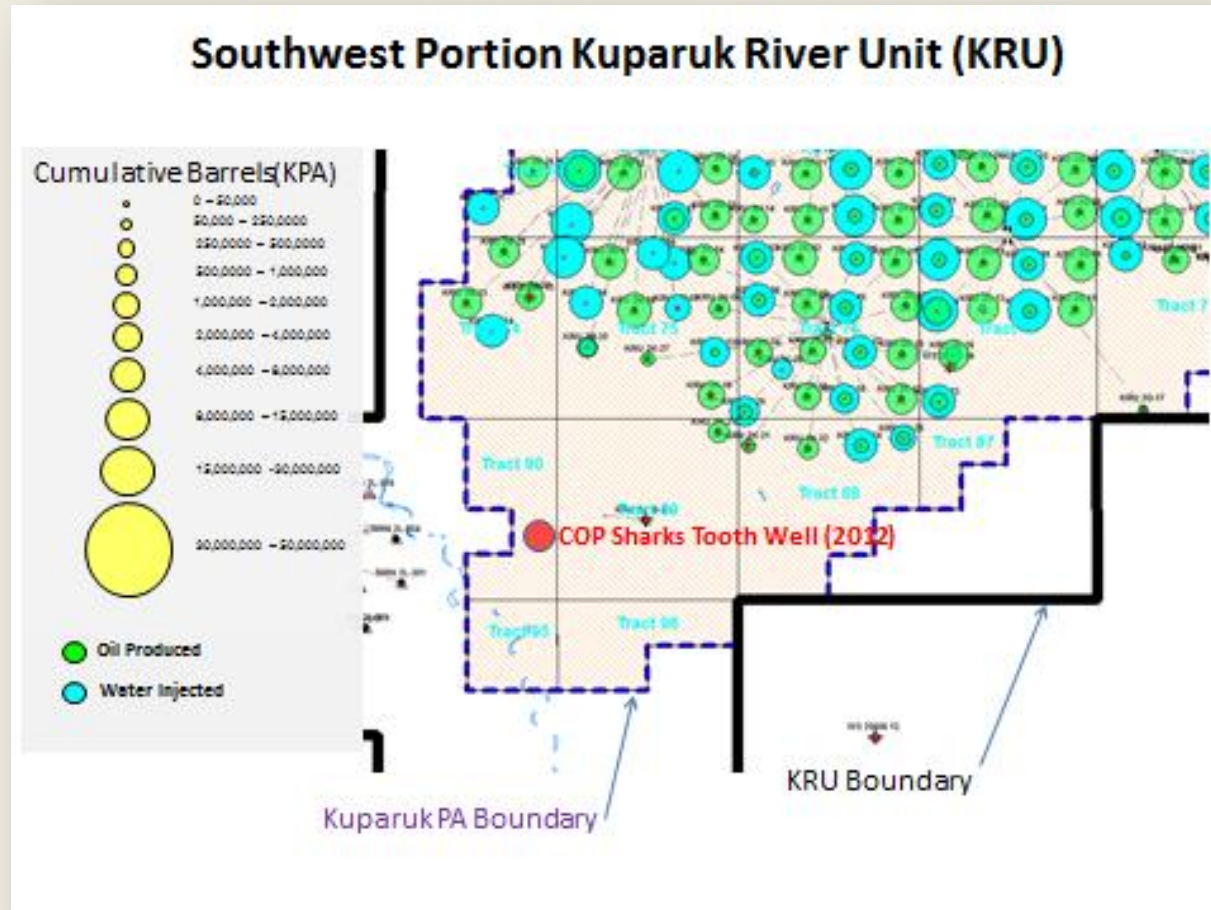
Cumulative Barrels (KPA)



- Oil Produced
- Water Injected



KUPARUK RIVER UNIT (KRU)



QUESTIONS?