

Oil and Gas Royalty Settlement Reopeners**FY2004 Request: \$1,000,000****Reference No: 31371****AP/AL:** Appropriation**Project Type:** Planning**Category:** Development**Location:** Statewide**Contact:** Martin Schultz**House District:** Statewide (HD 1-40)**Contact Phone:** (907)269-5255**Estimated Project Dates:** 07/01/2003 - 06/30/2006**Brief Summary and Statement of Need:**

This project will partially fund the cost of outside legal counsel and outside experts, and the State's cost of reopener arbitrations as the State proceeds with the renegotiation and arbitration of royalty issues.

Funding:	<u>FY2004</u>	<u>FY2005</u>	<u>FY2006</u>	<u>FY2007</u>	<u>FY2008</u>	<u>FY2009</u>	<u>Total</u>
Gen Fund	\$1,000,000						\$1,000,000
Total:	\$1,000,000	\$0	\$0	\$0	\$0	\$0	\$1,000,000

<input type="checkbox"/> State Match Required	<input checked="" type="checkbox"/> One-Time Project	<input type="checkbox"/> Phased - new	<input type="checkbox"/> Phased - underway	<input type="checkbox"/> On-Going
0% = Minimum State Match % Required		<input type="checkbox"/> Amendment	<input type="checkbox"/> Mental Health Bill	

Operating & Maintenance Costs:

	<u>Amount</u>	<u>Staff</u>
Project Development:	0	0
Ongoing Operating:	0	0
One-Time Startup:	0	0
Totals:	0	0

Additional Information / Prior Funding History:

SLA98/CH139 - \$100,000

SLA93/CH79 - \$100,000

Project Description/Justification:**Detailed Project Justification:**

The purpose of this funding request is to enable the State to effectively resolve ongoing and threatened litigation involving Alaska North Slope ("ANS") oil and gas royalties owed the State. All of the major oil companies retain private counsel well versed in oil and gas issues to prosecute royalty disputes against the State. This request is intended to allow the Department of Law to also retain a small body of select private counsel to assist in resolving ongoing disputes regarding oil and gas royalties owed the State.

The major producers entered into royalty settlement agreements with the State in the early 1990s. The agreements provide a methodology for valuing ANS oil for royalty purposes and an arbitration procedure for changing value methodology called a reopener.

In the last year Law has successfully resolved a value reopener against BP and a value and transportation reopener against Phillips. A value and transportation reopener is currently pending against Exxon. The State has been attempting to obtain Exxon data necessary to prosecute the reopener to a conclusion, but as of this date, Exxon has provided no data in response to State requests. It is anticipated that, as in the past, Exxon will retain a large number of outside counsel to litigate this reopener with the State. In the last major oil and gas proceeding with Exxon, it retained several separate law firms and also utilized in-house counsel and staff to litigate against the State. It is necessary that the State have access to outside counsel in order to adequately deal with the Exxon reopener, which is scheduled to restart in March of 2003 on a very short time line.

In addition, Law anticipates two other reopeners against various producers focused on transportation costs. The producers are buying new double-hulled tankers to comply with federal law (OPA 90). In connection therewith they are seeking significantly increased transportation deductions. One disputed issue is the treatment of tax benefits such as the capital construction fund program which allows producers to obtain vessels with tax deferred dollars. At least one of the producers has taken the position that the State is not entitled to share in the tax benefits. This type of litigation will require the retention of tax counsel and experts in vessel financing and other issues.

In addition to outside counsel, expert advice and opinions are essential to match the resources marshaled by the producers and to advance the State's own position before an arbitration panel and rebut the expert claims made by the producers.

Once the State or a producer gives notice that it is exercising a reopener provision, the schedules and protocol in the royalty settlement agreements must be followed. These schedules do not follow the State's year-to-year annual budget or appropriation time lines. The Department of Law's oil and gas litigation budget has been reduced over time. The Department of Law does not currently have sufficient funds to handle the needs caused by the reopeners.

Why This Project Is Needed Now:

If this project is not funded, the State will be ill prepared to present a well-reasoned advocacy of a fair royalty value. Because of the "baseball" arbitration rules that govern the process, the arbitration panel may select either the State's or the producer's proposal. The panel does not have the discretion to formulate a remedy based on its own expertise, or to "split the baby." Without proper preparation and vigorous representation before the arbitration panel, the State may not prevail.

Specific Spending Detail:Line Item Expenditures:

Contractual Services \$1,000,000
Personal Services \$0
Travel \$0
Supplies \$0
Equipment \$0

Line Item Detail Description:

Contractual Services – The funding under this CIP will pay for outside counsel and industry expert witnesses to represent the state in a hearing before an arbitration panel.