

SENATE CS FOR CS FOR HOUSE BILL NO. 394(RES)

IN THE LEGISLATURE OF THE STATE OF ALASKA

NINETEENTH LEGISLATURE - SECOND SESSION

BY THE SENATE RESOURCES COMMITTEE

Offered: 4/28/96

Referred: Finance

Sponsor(s): REPRESENTATIVES OGAN AND ROKEBERG, James, Kohring, Kubina

SENATORS Sharp, Kelly, Leman, Miller, Green, Pearce

A BILL

FOR AN ACT ENTITLED

1 "An Act authorizing shallow natural gas leasing from sources within 3,000 feet
2 of the surface; relating to regulation of natural gas exploration facilities for
3 purposes of preparation of discharge prevention and contingency plans and
4 compliance with financial responsibility requirements; addressing the relationship
5 between shallow natural gas and other natural resources; and adding, in the
6 exemption from obtaining a waste disposal permit for disposal of waste produced
7 from drilling, a reference to shallow natural gas."

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

9 * **Section 1. LEGISLATIVE FINDINGS AND PURPOSE.** (a) The legislature finds that
10 (1) there exist throughout the state sizeable deposits of coal and small but
11 commercially significant amounts of natural gas located close to the earth's surface that are
12 usually, though not always, associated with and emitted from coal deposits;
13 (2) the methane derived from this coal and other sources and that is found in

1 reservoirs at depths of less than 3,000 feet could be tapped to serve as a principal or a chief
2 supplemental energy source of benefit to residents of areas in which they are found;

3 (3) the methane derived from this coal and other shallow gas reservoirs could
4 be developed without interfering with the development and transportation of the state's vast gas
5 reserves available for interstate and foreign markets; and

6 (4) it is in the best interests of the state and its people that this natural gas should
7 be identified and developed, especially to serve as a source of natural gas for use in rural
8 communities and remote locations within the state, especially when this natural gas can be
9 delivered to consumers at less cost than alternative energy sources.

10 (b) In authorizing a program of leasing shallow natural gas from state land, it is the
11 legislature's purpose to provide both a means and an incentive by which that gas may be
12 identified and developed at low cost for the direct benefit of residents of remote or sparsely
13 populated areas for which connection to the in-place gas pipeline transmission and distribution
14 system serving population centers in Southcentral Alaska is not economically feasible.

15 * **Sec. 2.** AS 38.05.035(e)(6) is amended to read:

16 (6) before a public hearing, if held, or in any case not less than 21 days
17 before the sale, lease, or other disposal of available land, property, resources, or
18 interests in them other than a sale, lease, or other disposal of available land or an
19 interest in land for oil and gas under (5) of this subsection, the director shall make
20 available to the public a written finding that, in accordance with (1) of this subsection,
21 sets out the material facts and applicable statutes and regulations and any other
22 information required by statute or regulation to be considered upon which the
23 determination that the sale, lease, or other disposal will best serve the interests of the
24 state was based; however, a written finding is not required before the approval of

25 (A) a contract for a negotiated sale authorized under
26 AS 38.05.115;

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

28 (C) a permit or other authorization revocable by the
29 commissioner;

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

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

32 (F) a production license issued under AS 38.05.207;

1 (G) an exempt oil and gas sale under AS 38.05.180(d) of
2 acreage offered in a sale that was held within the previous five years if the sale
3 was subject to a written best interest finding, unless the commissioner
4 determines that new information has become available that justifies a revision
5 of the best interest finding; [OR]

6 (H) a lease sale under AS 38.05.180(w) of acreage offered in
7 a sale that was held within the previous five years if the sale was subject to a
8 best interest finding, unless the commissioner determines that new information
9 has become available that justifies a revision of the best interest finding; or

10 **(I) a shallow gas lease authorized under AS 38.05.177 in an**
11 **area for which leasing is authorized under AS 38.05.177;**

12 * **Sec. 3.** AS 38.05.140(a) is amended to read:

13 (a) A person may not take or hold coal leases or permits during the life of coal
14 leases on state land exceeding an aggregate of 46,080 acres, except that a person may
15 apply for coal leases or permits for acreage in addition to 46,080 acres, not exceeding
16 a total of 5,120 additional acres of state land. The additional area applied for shall be
17 in multiples of 40 acres and the application shall contain a statement that the granting
18 of a lease for additional land is necessary for the person to carry on business
19 economically and is in the public interest. On the filing of the application, **except as**
20 **provided by AS 38.05.177(a)(2)(C),** the coal deposits in the land covered by the
21 application shall be temporarily set aside and withdrawn from all other forms of
22 disposal provided under AS 38.05.135 - 38.05.181.

23 * **Sec. 4.** AS 38.05.150 is amended by adding a new subsection to read:

24 (f) Notwithstanding AS 38.05.177, a lease entered into under this section gives
25 the lessee the right to vent or remove methane and other gas held in association with
26 the coal in the land covered by the lease to ensure safe coal mining operations.

27 * **Sec. 5.** AS 38.05 is amended by adding a new section to read:

28 Sec. 38.05.177. SHALLOW NATURAL GAS LEASES. (a) The provisions of
29 this section

30 (1) apply to gas, whether methane associated with and derived from coal
31 deposits or otherwise, developed from a source that is onshore and within 3,000 feet of
32 the surface; and

1 (2) do not apply to authorize lease of

2 (A) land

3 (i) that is subject to an oil and gas exploration license or
4 lease issued under AS 38.05.131 - 38.05.134; or

5 (ii) that is leased under AS 38.05.180;

6 (B) the land (i) that is proposed to be subject to an oil and gas
7 exploration license or lease issued under AS 38.05.131 - 38.05.134; or (ii) that
8 is described in and part of a proposed oil and gas leasing program prepared under
9 AS 38.05.180(b); however, the commissioner may waive the limitations of this
10 subparagraph;

11 (C) the land that is held under a coal lease entered into under
12 AS 38.05.150, unless the applicant for a shallow natural gas lease is also the
13 lessee under AS 38.05.150 of that land; or

14 (D) the valid existing selections of the Alaska Mental Health
15 Trust Authority made for the purpose of reconstituting the mental health trust
16 established under the Alaska Mental Health Enabling Act, P.L. 84-830, 70 Stat.
17 709 (1956), that become subject to management under AS 38.05.801, or of land
18 that has been designated by law for or is subject to designation for conveyance
19 to the Alaska Mental Health Trust Authority; however, after consultation with
20 the Alaska Mental Health Trust Authority, the commissioner may waive the
21 limitations of this subparagraph.

22 (b) For the purpose of exploring for and developing shallow natural gas
23 reservoirs, upon application, the director may lease to a person land for which the state
24 owns the subsurface rights. A person applying for a lease under this subsection

25 (1) shall specify the area to be leased; the area to be leased may not
26 exceed 5,760 acres; a lessee may not hold more than 46,080 acres of land under leases
27 entered into under this section;

28 (2) may be required to pay a reasonable application fee of up to \$500.

29 (c) Within 20 days of receipt of a lease application, the director shall give
30 notice under AS 38.05.945 of receipt of the lease application and call for comments
31 from the public. The director's call for public comments must provide opportunity for
32 public comment for a period of 60 days. If, after review of information received

1 during the public comment period, the director determines that the discovery of a local
2 source of natural gas would benefit the residents of an area, the director shall execute
3 a lease for the area described in (b) of this section. The director shall execute the
4 lease within 90 days after the close of the public comment period or, if review is
5 required under AS 46.40, within 30 days after the final consistency determination is
6 made under AS 46.40, whichever is later. A lease entered into under this subsection
7 gives the lessee the exclusive right to explore for, develop, and produce, for a term of
8 three years, natural gas on the state land described in the lease; the right to explore for,
9 develop, and produce is limited to gas derived from natural gas within 3,000 feet of
10 the surface.

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

28 (e) The director may, following the procedures described in (c) of this section,
29 adjust the boundaries of a lease entered into under this section as may be necessary
30 to ensure development of natural gas within a reasonably compact area; a lease as
31 adjusted under this paragraph remains subject to the acreage limitations set out in

(b)(1) of this section.

(f) A shallow gas lease must provide for payment to the state of annual rent in the amount of 50 cents per acre. The rent is due and payable on the dates determined in the lease. The director shall mail the lessee one written notice, certified return receipt requested, three weeks before the due date of the rent. If the lessee fails to pay rent, the director shall terminate the lease.

(g) The royalty payable on natural gas produced from a lease

(1) is

(A) 12.5 percent of the value of production removed or sold from the lease for gas exported from the state or gas that is produced in direct competition with gas on which a royalty at a rate of at least 12.5 percent is payable; and

(B) except as provided in (A) of this paragraph, 6.25 percent of the value of the production removed or sold from the lease; and

(2) shall be based upon production delivered in pipeline quality and free of all lease expenses, including but not limited to separation, cleaning, dehydration, gathering, salt water disposal, and preparation for transportation off the lease.

(h) A lease issued under this section is subject to the following terms and conditions and may be terminated by the director in the event of a breach of a term or condition:

(1) the lessee may surrender the lease or relinquish part of the lease at any time;

(2) the lease may not be transferred or assigned until a well capable of production of gas in paying quantities has been drilled on the lease; however, this paragraph does not prohibit the lessee from entering into a farm out agreement or similar arrangement with a third party under which the third party assists in exploration and development of production from the lease if the agreement or arrangement does not require a payment of consideration by the third party to the lessee, except that the lessee may retain an overriding royalty interest in the lease or may retain a net profit or other production payment.

(i) The applicant for a lease is responsible for conducting a title search for the

1 area described in the lease application.

2 (j) A lease does not give the lessee the right to produce oil. A lease does not
3 give the lessee the right to produce gas from sources that are not within 3,000 feet of the
4 surface. If a well drilling for natural gas under a lease authorized by this section
5 penetrates a formation capable of producing gas below 3,000 feet of the surface or
6 penetrates a formation capable of producing oil, the owner or operator

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

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

14 (k) The commissioner of natural resources may adopt only the regulations that
15 are reasonable and that are necessary to implement, interpret, or make specific the
16 provisions of this section or to establish procedures to govern application of the
17 provisions of this section.

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

25 (m) Except as otherwise specifically provided in this section, the provisions
26 of AS 38.05.135 - 38.05.184 apply to leases entered into under this section.

27 (n) In this section, "lease" means a shallow gas lease authorized by this section.

28 * **Sec. 6.** AS 38.05.180(f) is amended to read:

29 (f) Except as provided by AS 38.05.131 - 38.05.134 and 38.05.177, the
30 commissioner may issue oil and gas leases on state land to the highest responsible
31 qualified bidder determined by competitive bidding under regulations adopted by the
32 commissioner. Bidding may be by sealed bid or according to any other bidding

1 procedure the commissioner determines is in the best interests of the state. Whenever,
2 under any of the leasing methods listed in this subsection, a royalty share is reserved
3 to the state, it shall be delivered in pipeline quality and free of all lease or unit
4 expenses, including but not limited to separation, cleaning, dehydration, gathering, salt
5 water disposal, and preparation for transportation off the lease or unit area. Following
6 a pre-sale analysis, the commissioner may choose at least one of the following leasing
7 methods:

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

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

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

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

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

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

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

1 * **Sec. 7.** AS 46.03.100(f) is amended to read:

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

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

8 (2) landscaping;

9 (3) water well drilling, geophysical drilling, or coal bed methane
10 drilling **or other natural gas drilling to recover gas from a reservoir at a depth of**
11 **less than 3,000 feet;** or

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

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

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

21 * **Sec. 8.** AS 46.04.030(b) is amended to read:

22 (b) A person may not cause or permit the operation of a pipeline or an
23 exploration or production facility in the state unless an oil discharge prevention and
24 contingency plan for the pipeline or facility has been approved by the department and
25 the person is in compliance with the plan. **This subsection does not apply to an**
26 **exploration facility used solely to explore for shallow natural gas by means of**
27 **drilling a well on a lease authorized under AS 38.05.177.**

28 * **Sec. 9.** AS 46.04.040(b) is amended to read:

29 (b) A person may not cause or permit the operation of a pipeline or an
30 exploration or production facility in the state unless the person has furnished to the
31 department, and the department has approved, proof of financial ability to respond in

1 damages. Proof of financial responsibility required for

2 (1) a pipeline or an offshore exploration or production facility is
3 \$50,000,000 per incident;

4 (2) an onshore production facility is

5 (A) \$20,000,000 per incident if the facility produces over
6 10,000 barrels per day of oil;

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

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

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

13 (3) an onshore exploration facility is

14 (A) \$25,000 per incident for a facility used solely to explore
15 for shallow natural gas by means of drilling a well to explore for gas,
16 whether methane associated with and derived from coal deposits or
17 otherwise, from a source that is within 3,000 feet of the surface; and

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