

**ALASKA STATE LEGISLATURE
HOUSE SPECIAL COMMITTEE ON OIL AND GAS**

March 9, 2004

3:17 p.m.

MEMBERS PRESENT

Representative Vic Kohring, Chair
Representative Jim Holm
Representative Norman Rokeberg
Representative Harry Crawford
Representative Beth Kerttula

MEMBERS ABSENT

Representative Cheryll Heinze
Representative Lesil McGuire

COMMITTEE CALENDAR

CS FOR SENATE BILL NO. 265(RES)

"An Act relating to the schedule of proposed oil and gas lease sales and to a related report to the legislature; and providing for an effective date."

- MOVED CSSB 265(RES) OUT OF COMMITTEE

SENATE BILL NO. 266

"An Act approving an interim classification by the commissioner of natural resources closing certain land within the area of the proposed Bristol Bay (Alaska Peninsula) competitive oil and gas areawide lease sale to oil and gas exploration licensing and shallow natural gas leasing; and providing for an effective date."

- MOVED SB 266 OUT OF COMMITTEE

HOUSE BILL NO. 395

"An Act relating to shallow natural gas leasing and the regulation of shallow natural gas operations."

- MOVED CSHB 395(O&G) OUT OF COMMITTEE

SPONSOR SUBSTITUTE FOR HOUSE BILL NO. 364

"An Act establishing a moratorium on the issuance of state shallow natural gas leases in the vicinity of Kachemak Bay, and precluding the commissioner of natural resources from reissuing

or otherwise extending leases within the moratorium area if the leases fail to produce gas in paying quantities within the terms of the lease or if there is a breach of a term or condition of the lease; and providing for an effective date."

- HEARD AND HELD

PREVIOUS COMMITTEE ACTION

BILL: SB 265

SHORT TITLE: OIL&GAS LEASE SALE SCHEDULE/NOTIFICATION

SPONSOR(S): RULES BY REQUEST OF THE GOVERNOR

01/14/04	(S)	READ THE FIRST TIME - REFERRALS
01/14/04	(S)	RES
02/04/04	(S)	RES AT 3:30 PM BUTROVICH 205
02/04/04	(S)	Moved CSSB 265(RES) Out of Committee
02/04/04	(S)	MINUTE(RES)
02/06/04	(S)	RES RPT CS 5DP 1AM SAME TITLE
02/06/04	(S)	DP: OGAN, SEEKINS, WAGONER, DYSON,
02/06/04	(S)	ELTON; AM: STEVENS B
02/25/04	(S)	TRANSMITTED TO (H)
02/25/04	(S)	VERSION: CSSB 265(RES)
02/26/04	(H)	READ THE FIRST TIME - REFERRALS
02/26/04	(H)	O&G, RES
02/26/04	(H)	O&G AT 3:15 PM CAPITOL 124
02/26/04	(H)	Scheduled But Not Heard
02/27/04	(H)	RES AT 1:00 PM CAPITOL 124
02/27/04	(H)	-- Meeting Canceled --
03/02/04	(H)	O&G AT 3:15 PM CAPITOL 124
03/02/04	(H)	Heard & Held
03/02/04	(H)	MINUTE(O&G)
03/09/04	(H)	O&G AT 3:15 PM CAPITOL 124

BILL: SB 266

SHORT TITLE: BRISTOL BAY OIL & GAS LEASE SALE CLOSURE

SPONSOR(S): RULES BY REQUEST OF THE GOVERNOR

01/14/04	(S)	READ THE FIRST TIME - REFERRALS
01/14/04	(S)	CRA, RES
02/02/04	(S)	CRA AT 1:30 PM FAHRENKAMP 203
02/02/04	(S)	Moved SB 266 Out of Committee
02/02/04	(S)	MINUTE(CRA)
02/04/04	(S)	CRA RPT 3DP 2NR
02/04/04	(S)	DP: STEDMAN, WAGONER, STEVENS G
02/04/04	(S)	NR: LINCOLN, ELTON
02/04/04	(S)	RES AT 3:30 PM BUTROVICH 205

02/04/04 (S) Moved Out of Committee
 02/04/04 (S) MINUTE(RES)
 02/06/04 (S) RES RPT 6DP
 02/06/04 (S) DP: OGAN, SEEKINS, STEVENS B, WAGONER,
 02/06/04 (S) DYSON, ELTON
 02/25/04 (S) TRANSMITTED TO (H)
 02/25/04 (S) VERSION: SB 266
 02/26/04 (H) READ THE FIRST TIME - REFERRALS
 02/26/04 (H) O&G, RES
 02/26/04 (H) O&G AT 3:15 PM CAPITOL 124
 02/26/04 (H) Scheduled But Not Heard
 02/27/04 (H) RES AT 1:00 PM CAPITOL 124
 02/27/04 (H) -- Meeting Canceled --
 03/02/04 (H) O&G AT 3:15 PM CAPITOL 124
 03/02/04 (H) Heard & Held
 03/02/04 (H) MINUTE(O&G)
 03/09/04 (H) O&G AT 3:15 PM CAPITOL 124

BILL: HB 395

SHORT TITLE: SHALLOW NATURAL GAS

SPONSOR(S): REPRESENTATIVE(S) HARRIS

01/23/04 (H) READ THE FIRST TIME - REFERRALS
 01/23/04 (H) O&G, RES, JUD, FIN
 02/05/04 (H) O&G AT 1:00 PM CAPITOL 124
 02/05/04 (H) Heard & Held
 02/05/04 (H) MINUTE(O&G)
 02/24/04 (H) O&G AT 3:15 PM CAPITOL 124
 02/24/04 (H) Heard & Held
 02/24/04 (H) MINUTE(O&G)
 02/26/04 (H) O&G AT 3:15 PM CAPITOL 124
 02/26/04 (H) Heard & Held
 02/26/04 (H) MINUTE(O&G)
 03/09/04 (H) O&G AT 3:15 PM CAPITOL 124

BILL: HB 364

SHORT TITLE: NATURAL GAS LEASES ON THE KENAI PENINSULA

SPONSOR(S): REPRESENTATIVE(S) SEATON

01/12/04 (H) PREFILE RELEASED 1/2/04
 01/12/04 (H) READ THE FIRST TIME - REFERRALS
 01/12/04 (H) O&G, RES, FIN
 02/19/04 (H) SPONSOR SUBSTITUTE INTRODUCED
 02/19/04 (H) READ THE FIRST TIME - REFERRALS
 02/19/04 (H) O&G, RES, FIN
 03/09/04 (H) O&G AT 3:15 PM CAPITOL 124

WITNESS REGISTER

ERIC MUSSER, Staff
to Representative Vic Kohring
Alaska State Legislature
Juneau, Alaska

POSITION STATEMENT: Explained changes in the proposed CS to
HB 395.

MARK MYERS, Director
Division of Oil & Gas
Department of Natural Resources (DNR)
Anchorage, Alaska

POSITION STATEMENT: Answered questions pertaining to HB 395 and
SSHB 364.

REPRESENTATIVE PAUL SEATON
Alaska State Legislator
Juneau, Alaska

POSITION STATEMENT: Testified as the sponsor of SSHB 364.

PATRICIA MACK
Wasilla, Alaska

POSITION STATEMENT: Testified during the discussion of SSHB
364.

MYRL THOMPSON, Member
Ogan is So Gone
Wasilla, Alaska

POSITION STATEMENT: Testified during the discussion of SSHB
364.

EMILY WARD
Homer, Alaska

POSITION STATEMENT: Testified during the discussion of
SSHB 364.

BRIAN HIRSCH, Member
Kachemak Bay Property Owners Alliance
Homer, Alaska

POSITION STATEMENT: Testified during the discussion of
SSHB 364.

NINA FAUST, Member
Kachemak Bay Property Owners Alliance
Homer, Alaska

POSITION STATEMENT: Testified during the discussion of SSHB 364.

VIOLA JERREL, Ph.D.
Homer, Alaska

POSITION STATEMENT: Testified during the discussion of SSHB 364.

CHRIS WHITTINGTON-EVANS, President
Friends of Mat-Su Board
Palmer, Alaska

POSITION STATEMENT: Testified during the discussion of SSHB 364.

JOHN MARTIN
Homer, Alaska

POSITION STATEMENT: Testified during the discussion of SSHB 364.

ACTION NARRATIVE

TAPE 04-8, SIDE A

Number 0001

CHAIR VIC KOHRING called the House Special Committee on Oil and Gas meeting to order at 3:17 p.m. Representatives Kohring, Holm, Rokeberg, and Kerttula were present at the call to order. Representative Crawford arrived as the meeting was in progress.

SB 265-OIL&GAS LEASE SALE SCHEDULE/NOTIFICATION

Number 0067

CHAIR KOHRING announced that the first order of business would be CS FOR SENATE BILL NO. 265(RES), "An Act relating to the schedule of proposed oil and gas lease sales and to a related report to the legislature; and providing for an effective date."

CHAIR KOHRING asked whether there was any discussion. [None was offered.]

Number 0097

REPRESENTATIVE ROKEBERG moved to report CSSB 265(RES) out of committee with individual recommendations and the accompanying fiscal notes. There being no objection, CSSB 265(RES) was reported from the House Special Committee on Oil and Gas.

SB 266-BRISTOL BAY OIL & GAS LEASE SALE CLOSURE

Number 0151

CHAIR KOHRING announced that the next order of business would be SENATE BILL NO. 266, "An Act approving an interim classification by the commissioner of natural resources closing certain land within the area of the proposed Bristol Bay (Alaska Peninsula) competitive oil and gas areawide lease sale to oil and gas exploration licensing and shallow natural gas leasing; and providing for an effective date."

Number 0161

REPRESENTATIVE KERTTULA noted that on March 4, 2004, the committee received a letter [addressed to Representative Kerttula from Thomas E. Irwin, Commissioner, Department of Natural Resources (DNR)] which clarifies that the administration's intent is not to allow offshore drilling in Bristol Bay.

CHAIR KOHRING acknowledged the arrival of Representative Crawford.

Number 0222

REPRESENTATIVE ROKEBERG moved to report SB 266 out of committee with individual recommendations and the accompanying fiscal notes. There being no objection, SB 266 was reported from the House Special Committee on Oil and Gas.

HB 395-SHALLOW NATURAL GAS

Number 0246

CHAIR KOHRING announced that the next order of business would be HOUSE BILL NO. 395, "An Act relating to shallow natural gas leasing and the regulation of shallow natural gas operations."

Number 0286

REPRESENTATIVE ROKEBERG moved to adopt the proposed committee substitute (CS), Version 23-LS1314\C, Chenoweth, 3/9/04, as a work draft. There being no objection, Version C was before the committee.

Number 0334

ERIC MUSSER, Staff to Representative Vic Kohring, Alaska State Legislature, explained that Version C has two changes. "A water component enacting an exaction fee and setting out criteria for testing wells and establishing a restoration fund was removed from the work draft," he explained. The second change is on page 1, Section 1, and takes the previous hydraulic fracturing language and splits it out, giving the Department of Natural Resources (DNR) the authority to regulate it on its own, he said. A provision is inserted to say that if reinjection of produced water is required, then reinjection would be done to depths below known sources of drinking water for consumption or agricultural purposes, he continued. It also gives DNR direct authority to regulate the disposal of waste produced during the operation. [Version C] addresses considerable public concern about protecting well water supplies and drinking water, he concluded.

Number 0540

MARK MYERS, Director, Division of Oil & Gas, Department of Natural Resources (DNR), said he hoped the Alaska Oil and Gas Conservation Commission (AOGCC) was available to answer questions also. He mentioned regulations of hydraulic fracturing to protect ground water. He said Section 1 prohibits the practice of producing gas from an aquifer where water is used for drinking water, such as has been done in the Lower 48. Referring to the reinjection changes in Version C, he said produced water must now be reinjected at depths below the aquifer zone, which provides for strong protection of drinking water. The ability by the department to regulate the disposal of waste is also clearly stated in the proposed CS. Overall, Version C provides clarity and adds protection to ground water, he concluded.

CHAIR KOHRING asked Mr. Myers to address the water fee issue.

MR. MYERS replied that the biggest water-risk issue is when the gas is being produced from the same aquifer zone that is used for drinking water. In the Lower 48, in arid regions, there are cases where the coal seams are actually the drinking water aquifers, he noted. This [proposed CS] makes it clear that this activity would not be allowed in Alaska, he said. He asked Chair Kohring if that answers his question.

CHAIR KOHRING replied that it helps. He asked if there was any further discussion on the bill. [None was offered.]

Number 0822

REPRESENTATIVE ROKEBERG moved to report CSHB 395 [Version 23-LS1314\C, Chenoweth, 3/9/04] out of committee with individual recommendations and the accompanying fiscal notes. There being no objection, CSHB 395(O&G) was reported from the House Special Committee on Oil and Gas.

HB 364-NATURAL GAS LEASES ON THE KENAI PENINSULA

Number 0880

CHAIR KOHRING announced that the final order of business would be SPONSOR SUBSTITUTE FOR HOUSE BILL NO. 364, "An Act establishing a moratorium on the issuance of state shallow natural gas leases in the vicinity of Kachemak Bay, and precluding the commissioner of natural resources from reissuing or otherwise extending leases within the moratorium area if the leases fail to produce gas in paying quantities within the terms of the lease or if there is a breach of a term or condition of the lease; and providing for an effective date."

The committee took an at-ease from 3:29 p.m. to 3:32 p.m.

Number 0960

REPRESENTATIVE PAUL SEATON, Alaska State Legislature, sponsor, explained the bill's history. Back in 1976, the State of Alaska bought back the leases on the offshore portions of Kachemak Bay and included in that definition the lands south of the township and the waters east of Cook Inlet, he related. In 1996 the shallow natural gas program was passed, which provided for a low-cost lease sale - \$500 per lease - designed for remote areas. In 1999 the State of Alaska excluded the lands of the lower Cook Inlet peninsula in the areawide lease sale for Cook Inlet, and in June of 2003, the State of Alaska issued shallow natural gas leases to the subsurface rights in the Homer area, he said. He referred to a map that show the leased areas, "a hodge-podge of state-owned leases and private leases interspersed throughout the urban area of the Homer bench."

REPRESENTATIVE SEATON continued to say that the shallow natural gas programs had no competitive bidding for the leases, nor best interest findings, except for one assumed under the 1996

program. There was no consideration for local comments, effective notification, or operational regulations. The goal of the proposed sponsor substitute is to make sure that the current leases in the Homer area are not extended or reissued and to exclude these lands from future shallow natural gas lease sales. He said it in no way complicates the future leasing of this area under an areawide lease sale for gas. In fact, it would actually simplify it, he explained.

Number 1160

REPRESENTATIVE SEATON pointed out:

Section 1 [of the proposed sponsor substitute] is the legislative findings. Section 2 excludes certain lands in the vicinity of Kachemak Bay from leasing under the shallow natural gas program. Section 3 prohibits the issuance or re-issuance of shallow natural gas leases entered into before the effective date, if it turns out that there is a failure to produce payable quantities of gas, or if these leases are relinquished or illegally transferred. Section 4 gives an immediate effective date of this bill.

REPRESENTATIVE SEATON remarked that there are other bills that look at the shallow natural gas program, plan to terminate it for the future, and go to a gas-only sale. He spoke of Homer's long exclusion from gas production when it was excluded from the areawide lease sales, which somehow made Homer available for the shallow natural gas program, a program more appropriate for rural areas.

Number 1251

REPRESENTATIVE SEATON spoke about Amendment 1, which gives discretionary guidelines to the director of the Division of Oil & Gas [DNR] so that "if someone has not produced paying quantities of gas and has not started activity on the leases, if they haven't satisfied the director that they really intend to go into production and are willing to put some money up for exploration, then the commissioner has the authority to not extend the leases." Under the current term there is a three-year rollover, and these could be extended for three years, he added. It gives the director the ability to weigh whether gas production is probable or not, he concluded. He added that the people in Homer are overwhelmingly in favor of an immediate

solution to the problem, which would be a buy-out. This is not a buy-out bill, he emphasized.

REPRESENTATIVE SEATON indicated that there is an indeterminate section in the fiscal note, however, and said, "The director would not be extending the leases if he doesn't anticipate the development will take place, so there's really not a loss of revenue because the director would have to determine that the leases are not going to be produced on anyway." He said it is a zero fiscal note other than the revenues, and [Amendment 1] would make that zero, as well.

Number 1480

REPRESENTATIVE CRAWFORD said he was comparing Version Q [a proposed CS labeled 23-LS1464\Q, Chenoweth, 3/4/04, that hadn't been adopted] with Version H [SSHB 364] and the amendment in both versions seems to be identical. He asked if there is any difference between them.

REPRESENTATIVE SEATON said there are a few differences. He referred to the bold writing in [Amendment 1] and related that there are a few clean-ups in the language suggested by DNR.

REPRESENTATIVE CRAWFORD asked for clarification, but then said, "Under (B) it says 'likely prospect' as opposed to 'probability'."

REPRESENTATIVE SEATON concurred.

Number 1587

CHAIR KOHRING asked for clarification about the area affected by the bill.

REPRESENTATIVE SEATON said the boundaries are the same as the original buy-back of 1976 and are acceptable to DNR. He mentioned the Harding Icefield to the east as a possible addition. He said that lands in the current areawide lease sale are excluded.

CHAIR KOHRING asked if the boundary extended south to the three-mile limit.

REPRESENTATIVE SEATON said it only deals with lands and not with waters.

CHAIR KOHRING asked what the square mileage is.

REPRESENTATIVE SEATON replied that there are eight leases of nine square miles each, the area of the Homer bench from Anchor Point to East Homer.

CHAIR KOHRING inquired if conventional oil is involved.

REPRESENTATIVE SEATON said no, strictly shallow gas, except in an unintended consequence "if a producer could show that a reservoir started above 3,000 feet and then went down, they could use this an excuse to actually do conventional drilling and conventional gas production, but they would have to be able to prove that for each reservoir that they were trying to tap."

CHAIR KOHRING opened public testimony and asked that testimony be limited to three minutes.

Number 1882

PATRICIA MACK spoke as a 53-year resident of Alaska who lives in the Matanuska-Susitna area. She asked that the bill be expanded to include Matanuska-Susitna urban areas in order to place the shallow gas in an area away from people's back yards.

Number 1926

MYRL THOMPSON, Member, Ogan is So Gone, agreed that the bill should be extended to include the Matanuska-Susitna area. He remarked that he is in favor of a buy-back.

Number 1960

EMILY WARD related that she owns property outside of Homer that has been leased. She said she received no notice prior to the lease's happening and didn't find out until after three months that the lease took place. She voiced concern that the bill does not do enough, and said she favors a buy-back so that "we can start over and do it right."

Number 2055

BRIAN HIRSCH, Member, Kachemak Bay Property Owners Alliance, a group of people who strongly advocate a buy-back, noted he has over 1,000 signatures to that effect. He thanked Representative Seaton for pushing SSHB 364 forward and stated his support for a moratorium on shallow natural gas development in the area,

however; he said he also feels that the bill doesn't go far enough and enshrines the current situation, which is not acceptable to many people. He called the bill "window dressing" and asked for an inclusion of a buy-back. He voiced a concern about the amount of discretion given to the commissioner.

Number 2206

NINA FAUST, Member, Kachemak Bay Property Owners Alliance, said she firmly believes a buy-back is the only way to address property owners' concerns. She noted that the state, through this lease sale, has declared 22,000 acres of Homer's residential areas an industrial zone. As a property owner, she spoke of her resentment of de facto zoning. She mentioned that Homer has an economy and demographics different from the rest of the Kenai Peninsula and has fought oil and gas development since the early 1970s. She opined that the area could best support itself and contribute to the state's economy without heavy industrial development. She stated her appreciation for Representative Seaton's efforts through SSHB 364 and her disappointment that there is no buy-back provision. She also voiced a concern about the bill's giving too much discretion to the commissioner and having no appeal process.

Number 2420

REPRESENTATIVE HOLM asked if the Kachemak Bay Property Owners Alliance has taken into consideration that all of the subsurface rights and the gas are owned by all of Alaska, not just the people who live in the Homer area.

MS. FAUST said she understands that, but feels they are entitled to due process, which they did not receive.

REPRESENTATIVE HOLM suggested Ms. Faust is not against the utilization [of the gas], just the process that has taken place.

MS. FAUST replied that Homer has worked for years to keep out heavy industrial development, and every place in the state should not have to have it.

REPRESENTATIVE HOLM said he thought that argument could be made everywhere in the state, but thanked Ms. Faust for her testimony.

CHAIR KOHRING asked if she and her organization are opposed to coal bed methane in general or just want to achieve a buy-back.

MS. FAUST responded that after seeing all the problems it caused in the Lower 48, she is opposed to coal bed methane development in Alaska.

CHAIR KOHRING asked where Ms. Faust thought Alaska should get its coal bed methane from.

MS. FAUST said in appropriate, nonresidential areas.

Number 2535

REPRESENTATIVE SEATON, directing his explanation to Representative Holms, stated that part of the problem is that there was no notification given in the Homer area and any comments made by the owners could not be considered by DNR. Under the original bill there was an assumed best interest of developing shallow natural gas wherever it occurred in this state, he explained. It said if there was any benefit to lease production, then the leases had to be granted, which is different than any other leases in Alaska, he added. It was an unintended consequence, he concluded.

Number 2646

VIOLA JERREL, Ph.D., saying her family has land within the leased area in Homer, stated opposition to the drilling for coal bed methane and support of a buy-back, but said she isn't anti-oil. She echoed some of the same concerns as the previous two speakers.

CHAIR KOHRING asked Dr. Jerrel if she is aware of the state constitution's allowing the state to override local regulations, go in, and develop if it is deemed in the best interests of the state.

DR. JERREL asked, "How does that protect us?"

CHAIR KOHRING clarified that he is just making the point that "that ultimate right was not anything that was bestowed upon the state through any statute that we recently passed; that's per the constitution."

DR. JERREL replied, "We need to have legislators who will protect our rights." She thanked Representative Seaton and Senator Gary Stevens for their help to the Homer area.

TAPE 04-8, SIDE B

Number 2965

CHRIS WHITTINGTON-EVANS, President, Friends of Mat-Su Board, stated his group's support for Homer's attempts to push for reacquisition of leases, recognizing that their situation is similar to Mat-Su's. He related that the people in the Matanuska-Susitna area feel this bill should extend to their area for the same reasons: not being given due process, no best interest finding, noncompetitive leasing, and virtually no notification. The same considerations regarding conflicts between shallow and deep well gas should be taken into consideration, he said. The valley leases deserve the same remedies, he opined, whether they are a reacquisition or a lease sunset.

MR. WHITTINGTON-EVANS also stated opposition to giving a great deal of discretion to the director in terms of lease sunset. Future legislative remedies that might include best interest findings and competitive leases are not very comforting to those who live on land that has already been leased without due process. The idea of a sunset is a compromise, but only as a last remedy if a complete reacquisition does not happen, he opined.

Number 2757

JOHN MARTIN also thanked Representative Seaton and Senator Stevens for their help on this issue. He related that he is one of the property owners whose land was leased by the state without any prior notice. He spoke of his support for a buy-back in Homer and in the Matanuska-Susitna area.

Number 2719

CHAIR KOHRING closed public testimony.

REPRESENTATIVE KERTTULA asked Mr. Myers if the language that deals with the discretion is so that in the future if the leases don't prove up, which the residents would hope that they don't, then the director can pull the leases back. She asked if that language is parallel to current language that gives discretion in other areas.

Number 2654

MR. MYERS, Director, Division of Oil & Gas, Department of Natural Resources (DNR), replied that Representative Kerttula is correct and that there is some confusion by the public. Right now there is discretion to extend [the leases] three years, but the discretion is broad and has no sidebars. The language in SSHB 364 narrows the director's discretion in some specific cases, he explained.

REPRESENTATIVE KERTTULA said:

If we don't do this, we leave the discretion so broad that if you tried to use your discretion there could conceivably be a takings case, and that the language in Representative Seaton's bill and in other bills that are pending in the legislature, it seems counterintuitive, but what happens is we've restricted that so that you've got the guidelines to be able to follow. And I'm sure for the residents' side, hopefully this plays out, and you could then look at things under these guidelines and enforce the leases being returned. Is that right?

Number 2591

MR. MYERS said that is correct. Basically, it shows clearly what the legislature intended - or intends now - for that discretion to be and how that discretion is being used, he said. It wouldn't give him the ability to renew a lease if no activity has occurred, and it would prevent him from issuing a decision that would be for political or other reasons, he explained. "It's the legislature narrowing the focus and limiting my authority," he concluded.

Number 2560

REPRESENTATIVE HOLM asked when all these leases were sold, for how much, and how much a buy-back would cost.

MR. MYERS replied that the leases in the Homer area were applied for in 2000 and issued in June 2003 with a purchase price, at the time, of \$500 per lease, but the fees have since been raised to \$5,000.

REPRESENTATIVE HOLM asked what that translates to.

MR. MYERS responded that all eight leases went for a total of \$4,000, but there is also a rental fee of \$1 per acre. There

are 22,000 acres, so that's \$22,000 in rental fees. The exact figure of total rentals is \$20,641 per year, he noted.

REPRESENTATIVE HOLM asked if the maximum amount of money this year is \$24,000.

MR. MYERS said that is correct unless production occurs, and then there would be royalties and severance tax.

REPRESENTATIVE HOLM asked what the potential for drilling is, and stated that it is an awfully low price for tying up 22,000 acres for endless speculation.

MR. MYERS said that was one of the issues of the original shallow gas-leasing program. He opined that legislation was passed to provide a very low threshold so there could be accelerated exploration and development for rural energy, particularly for natural gas, in areas where they are using diesel fuel and didn't have a reasonable alternative source of energy. All land outside of areawide lease sales or current exploration licenses in the state was eligible for the program, so the leases went for less than the cost of conventional leases and they were noncompetitive. The administrative costs are higher than the money received, he added.

MR. MYERS continued, saying the other side of the equation is that the [Homer] area does have potential for conventional gas and the coal seams are of the right type so coal bed methane could be extracted. The intent of Union Oil Company of California (Unocal) would be to look at conventional gas, as it appears to no longer be interested in coal bed methane in Alaska, he said. There is reasonable potential for fairly significant quantities of gas, he concluded.

Number 2337

REPRESENTATIVE HOLM asked if a different type of lease would be needed for natural gas extraction.

MR. MYERS stated that one of the confusions is that the shallow gas lease allows for any gas production on that lease, but it allows it only at specified depths. The way the current lease reads it requires some of the geologic field to be above 3,000 feet. "The intent was that if you drilled something at 3,000 feet and it was in communications with parts of a field that geologically dips downward below 3,000 feet, that you could continue to produce that same field or that same reservoir."

Conventional gas and cold bed methane is included in that concept. He termed this "depth-limited leases," which means that some of the geological potential at deeper depths could not be realized and the state would retain 100 percent ownership of that resource. If part of the coal bed methane were above 3,000 feet, then it could continue to be developed from deeper depths, he said. All gases could be developed under one lease, but only to a certain depth, he concluded.

REPRESENTATIVE HOLM asked, if coal bed methane gas is found between 3,000-4,000 feet, whether the state could change the lease process and add another type of lease requirement for conventional gas.

MR. MYERS replied:

Right now, because there is no best interest finding in the areas that have shallow gas leases, we have no vehicle to lease the land except for potentially an exploration license that might be granted, but, basically, it would be difficult to come in and lease on the top, and in some cases we legally couldn't do it, and other cases where we could it, would probably not be advisable because of what's called correlative rights problem. There would be arguments about whose gas is really there between 3,000-4,000 feet or between 3,000-5,000 feet. There would be trouble with legal challenges and enough geological data would have to be acquired to try to sort it out.

MR. MYERS continued to say that it makes more sense to drill as few wells as possible and have all of the rights explored simultaneously.

REPRESENTATIVE HOLM thanked Mr. Myers for all of his information.

Number 2031

REPRESENTATIVE SEATON noted that Amendment 1 has not been offered. He pointed out that in the members' packets are resolutions from all of the government entities that support this bill or the buy-back. He pointed out on the map the extent of the leases to show that there are many leases which are not opposed. "It's not as if the people in this area are uniformly against anything happening," he remarked. He called the Homer area extremely unique in that it has consistently come forward

with a different plan for economic development in Alaska. He continued to point out urban areas that are affected by the leases and noted that the Kenai Borough gave [Homer] extraterritorial control over the watershed to protect it, and now it is leased out for coal bed methane with no drilling restrictions. He requested that the committee "let us constrain this time frame from a 6-year-time window to a 3-year-time window," and give that authority to the commissioner.

CHAIR KOHRING asked where "5 south and 14 west" are on the map.

[Representative Seaton indicated those boundaries on the map.]

CHAIR KOHRING asked for closing remarks.

REPRESENTATIVE SEATON said he would appreciate the consideration of the committee of [Amendment 1], which adds to the bill, and he said he believes that [SSHB 364] is a bill that House Special Committee on Oil and Gas could support.

CHAIR KOHRING said his intent is not to take action to move the bill out of committee today.

Number 1781

REPRESENTATIVE HOLM suggested that since [Amendment 1] would be contained in the [proposed] CS, the committee could adopt the CS.

REPRESENTATIVE SEATON pointed out that some of the language of [Amendment 1] has been changed to reflect DNR's preferences on language from the proposed CS. He requested that [Amendment 1] be adopted so a new CS could be drafted.

Number 1735

REPRESENTATIVE HOLM [moved to adopt Amendment 1], which read [original punctuation provided]:

Page 3, line 10; Insert new Section 3; renumber sections accordingly.

***Sec. 3.** AS 38.05.177(d) is amended to read:

(d) A lease

(1) shall be automatically extended if and for so long thereafter as gas is produced in paying

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

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

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

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

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

Number 1720

CHAIR KOHRING asked whether there was any objection. Hearing no objection, he indicated Amendment 1 was adopted. [SSHB 364 was held over.]

ADJOURNMENT

There being no further business before the committee, the House Special Committee on Oil and Gas meeting was adjourned at 4:34 p.m.