

**ALASKA STATE LEGISLATURE
HOUSE RESOURCES STANDING COMMITTEE**

April 14, 2004

1:40 p.m.

MEMBERS PRESENT

Representative Nancy Dahlstrom, Co-Chair
Representative Beverly Masek, Co-Chair
Representative Carl Gatto
Representative Bob Lynn
Representative Nick Stepovich
Representative Kelly Wolf
Representative Beth Kerttula
Representative David Guttenberg

MEMBERS ABSENT

Representative Cheryll Heinze, Vice Chair

COMMITTEE CALENDAR

HOUSE BILL NO. 531

"An Act relating to natural gas exploration and development and to nonconventional gas, and amending the section under which shallow natural gas leases may be issued; and providing for an effective date."

- HEARD AND HELD; ASSIGNED TO SUBCOMMITTEE

HOUSE BILL NO. 395

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

- HEARD AND HELD; ASSIGNED TO SUBCOMMITTEE

PREVIOUS COMMITTEE ACTION

BILL: HB 531

SHORT TITLE: CONVENTIONAL & NONCONVENTIONAL GAS LEASES

SPONSOR(S): RESOURCES

03/04/04	(H)	READ THE FIRST TIME - REFERRALS
03/04/04	(H)	O&G, RES, FIN
03/16/04	(H)	O&G AT 3:15 PM CAPITOL 124
03/16/04	(H)	Heard & Held
03/16/04	(H)	MINUTE(O&G)

03/18/04 (H) O&G AT 3:15 PM CAPITOL 124
03/18/04 (H) Heard & Held
03/18/04 (H) MINUTE(O&G)
03/22/04 (H) RES AT 1:00 PM CAPITOL 124
03/22/04 (H) <Pending Referral>
04/01/04 (H) O&G AT 3:15 PM CAPITOL 124
04/01/04 (H) Moved CSHB 531(O&G) Out of Committee
04/01/04 (H) MINUTE(O&G)
04/05/04 (H) O&G RPT CS(O&G) 7AM
04/05/04 (H) AM: HOLM, KERTTULA, MCGUIRE, ROKEBERG,
04/05/04 (H) CRAWFORD, HEINZE, KOHRING
04/14/04 (H) RES AT 1:00 PM CAPITOL 124

BILL: HB 395

SHORT TITLE: SHALLOW NATURAL GAS/ OIL AND 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
03/09/04 (H) Moved CSHB 395(O&G) Out of Committee
03/09/04 (H) MINUTE(O&G)
03/12/04 (H) O&G RPT CS(O&G) NT 1DP 3NR 1AM
03/12/04 (H) DP: KOHRING; NR: ROKEBERG, CRAWFORD,
03/12/04 (H) HOLM; AM: KERTTULA
03/19/04 (H) RES AT 1:00 PM CAPITOL 124
03/19/04 (H) -- Meeting Canceled --
04/07/04 (H) RES AT 1:00 PM CAPITOL 124
04/07/04 (H) Heard & Held
04/07/04 (H) MINUTE(RES)
04/14/04 (H) RES AT 1:00 PM CAPITOL 124

WITNESS REGISTER

ELEANOR WOLFE, Staff
to Representative Beverly Masek
Alaska State Legislature
Juneau, Alaska

POSITION STATEMENT: Presented HB 531 on behalf of Representative Masek, Co-Chair, House Resources Standing Committee which sponsored HB 531, and answered questions from the members.

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

POSITION STATEMENT: Testified on HB 531 and HB 395, answered questions.

MERLIN THOMPSON, Chairman
Ogan is So Gone Recall
Sutton, Alaska

POSITION STATEMENT: Testified on HB 531 and HB 395.

ROBIN McLEAN, Sutton Community Council
Sutton, Alaska

POSITION STATEMENT: Testified on HB 531 and HB 395.

ROBERT CRANDALL, Petroleum Geologist
Alaska Oil and Gas Conservation Commission
Anchorage, Alaska

POSITION STATEMENT: Answered questions on HB 531.

JEFF ARNDT, Friends of the Mat-Su
Palmer, Alaska

POSITION STATEMENT: Testified on HB 531 and HB 395.

MARY BARRETT
Palmer, Alaska

POSITION STATEMENT: Testified on HB 531 and HB 395.

MIKE McCARTHY
Kachemak Bay Property Owner's Alliance
Homer, Alaska

POSITION STATEMENT: Testified on HB 531 and HB 395.

KEN BOYD, Chairman
Lands Exploration and Operations Committee
Alaska Oil and Gas Association
Anchorage, Alaska

POSITION STATEMENT: Testified on HB 531 and answered questions from the members.

RICK VANDERKOLK, Staff

to Representative John Harris
Alaska State Legislature
Juneau, Alaska

POSITION STATEMENT: Testified on HB 395 on behalf of
Representative Harris, sponsor.

ACTION NARRATIVE

TAPE 04-20, SIDE A

Number 0001

CO-CHAIR BEVERLY MASEK called the House Resources Standing Committee meeting to order at 1:40 p.m. Representatives Masek, Dahlstrom, Gatto, Lynn, Stepovich, Wolf, Guttenberg, and Kerttula were present at the call to order.

HB 531-CONVENTIONAL & NONCONVENTIONAL GAS LEASES

[Also contains discussion of HB 69]

Number 0049

CO-CHAIR MASEK announced that the first order of business would be HOUSE BILL NO. 531, "An Act relating to natural gas exploration and development and to nonconventional gas, and amending the section under which shallow natural gas leases may be issued; and providing for an effective date."

Number 0080

ELEANOR WOLFE, Staff to Representative Beverly Masek, Alaska State Legislature, presented HB 531 on behalf of Representative Masek, Co-Chair, House Resources Standing Committee, which sponsored HB 531, and answered questions from the members.

Number 0100

CO-CHAIR DAHLSTROM moved to adopt CSHB 531, 23-LS1818\U, Chenoweth, 4/12/04, as the working document. There being no objection, CSHB 531, version U, was before the committee.

MS. WOLFE read the sponsor statement as follows:

The intent of original shallow gas leasing legislation in 1995, HB 394, was to expand development of our state's marketable natural gas resources, as well as to promote private-sector employment, generate less

expensive energy alternatives for rural Alaskan consumers, and enhance local tax bases for municipalities. Shallow gas legislation was inspired by the need to tailor the particular economies of this resource opportunity to available market opportunities. This type of gas extraction does not conform to the same economies of scale as conventional deep-hole oil and gas drilling.

Original legislation provided for leasing on a first-come, first-served basis so that development of the resource in areas away from the energy grid could take place. With a well-known shortage of natural gas development opportunities in South Central Alaska, prospects of leasing on-shore fields in the Cook Inlet Basin became very attractive. Two unintended consequences of this sudden interest materialized. One it sparked leasing of the state-owned subsurface mineral estate in uneconomic areas, and two, it encouraged leasing in areas where divergent interests between gas development and established local residential and business activities came into conflict.

Without HB 531, a subsequent gas development entity could immediately lease land relinquished by the original lessee. In addition, land not currently leased remains subject to current over-the-counter standards. This bill initiates a permanent solution to these problems. It has been brought forward in response to strong citizen interest in the Mat-Su and on the Kenai Peninsula, with input from several public meetings held at one time or another by the Alaska Department of Natural Resources (DNR), and the Senate Resources Committee.

MS. WOLFE said that the highlights of the legislation are as follows:

Eliminates over-the-counter, first-come, first-serve shallow gas leases and replaces it with area-wide leasing or exploration licensing.

Requires a best-interest finding before any oil and gas leasing or exploration licensing. This will give DNR control of what land is leased, avoiding

unnecessary surface-owner conflicts. Best-interest finds are a time-tested public process.

Creates a gas-only section of area-wide leasing and exploration licensing identified in a best-interest finding by DNR.

Differentiates conventional and non-conventional gas resources for the purposes of lease rentals.

Defines conventional and non-conventional gas development, and treats each distinctly. Recognizes that lease rights should not be determined by a depth criteria only. Enhances production opportunities.

Encourages exploration licenses with a best-interest finding as the method for non-conventional gas exploration outside of the area-wide leasing in rural Alaska.

Makes leasing and regulatory criteria fit the appropriate activity.

Ensures competitive processes, thereby maximizing the state's interests.

Number 0386

MS. WOLFE said she would be happy to answer any questions, but suggested that technical questions be directed to staff of the Division of Oil and Gas.

Number 0420

REPRESENTATIVE LYNN asked how the best-interest finding is different than what is currently in place.

MS. WOLFE replied that no best-interest finding currently exists for the shallow gas program; it is simply a lease program. Ms. Wolfe commented that there have been some concerns about the hydro fracturing and the aquifers. She told the members that she retrieved a report [Study of Potential Impacts of Hydraulic Fracturing of Coal bed Methane Wells on Underground Sources of Drinking Water, EPA 816-D-02-006, dated August 2002] off of the Internet from the Environmental Protection Agency (EPA) that has determined that there is no damage to water aquifers from hydro fracturing. There were a number of complaints that were

investigated and it was found that the complaints were baseless and there was no need for further investigation, she explained. Ms. Wolfe suggested that this report may put some minds at ease.

Number 0510

REPRESENTATIVE KERTTULA questioned if there was still concern about the fluids used, but not the activity itself. She asked if there was any distinction made on this issue.

MS. WOLFE clarified that the fluids were addressed by the EPA report. She explained that it is maintained that while there are problem fluids used in hydro fracturing, once the water is pumped out of the well a low pressure area exists. Anything could be sucked into it and will not go out of it, she explained. Ms. Wolfe pointed out that there have been no difficulties with this in Colorado, Montana, or Wyoming.

REPRESENTATIVE KERTTULA commented that she will talk with Ms. Wolfe more about this issue later.

Number 0600

REPRESENTATIVE GATTO said it is his understanding that diesel fuel is being used, which is considered a hazardous material. However, when considering the volume of water that is pumped the amount of hazardous material left behind would be virtually immeasurable. He commented that he believes that makes sense.

MARK MYERS, Director, Division of Oil & Gas, Department of Natural Resources, testified on HB 531 and answered questions. He told the members that it is his understanding that the EPA draft report, not final report, found no examples where hydro fracturing had caused problems with the aquifers. Mr. Myers commented that he believes the statements that have been made are pretty accurate. While there are a couple of risks, the mechanics of it have not shown it to be problematic. He clarified that diesel fuel is not used with coal bed methane (CBM).

Number 0790

REPRESENTATIVE GUTTENBERG asked what [is used in] the process of hydro fracturing. Is it an impact hammer or drill.

Number 0842

MR. MYERS responded that the process is usually one where a liquid is pumped down under high pressure. He explained that it is actually the pressure that drives the fracturing of the rock. The purpose is to fracture the coal and make it a more permeable pathway to move the gas out of the coal. In order to commercially produce coal by methane a couple of elements are necessary. One element is that coal with a sufficient quantity of gas must be present; and two, the gas has to have a pathway to get out of the coal, Mr. Myers said. There have to be interconnected pathways, and hydro fracturing is a method of stimulating the removal of gas from the coal, he added.

Number 0882

REPRESENTATIVE STEPOVICH asked what the differences are in the criteria for gas exploration leasing as opposed to oil leasing.

MR. MYERS commented that this eliminates an over-the-counter profit and replaces it with two different processes. One is areawide leasing which provides competitive processes for lands in a specific area that have been approved by the best-interest finding. That is a competitive process that comes up every ten years. He explained that the advantage of that program over the over-the-counter shallow gas program is the biggest thing is defining its self with more public process and a different balancing test on where it is appropriate to lease. It also allows DNR to say that certain areas are beyond limits that are appropriate.

[The quality of the recording for the remaining testimony from Mr. Myers on HB 531 is of poor quality due to background noise in the room.]

MR. MYERS continued his testimony as follows:

The other way to (indisc.) licensing has been used in areas where we do not use the conventional leasing program. That is a program which recognizes that economics are different in rural areas Alaska and in frontier bases where you do not have sufficient information to really hold an areawide sale or the potential isn't there (indisc.) ... It is a worldwide method used, it is a variation on a worldwide method. (indisc.) large amount of land it asks for anywhere between 10,000 and 500,000 acres to a single applicant. Other people can submit competing

(indisc.) so it is and can (indisc.) in fact it is applicant driven. Or the state can open an area up for it. But it allows then for (indisc.) process for the state to issue exclusive rights to explore lands. You don't pay a bonus bid like (indisc.) you pay a one-dollar fee per acre. So if you had a 20,000 acre site, say out in the (indisc.) or whatever then you might pay \$20,000 and then you negotiate the work permit. Then you (indisc.) "X" amount of dollars for the right to explore here. So the state gets (indisc.) per acre, the applicant the for that fee gets (indisc.) hold typically for five or ten years on a license and has an exclusive right to explore, but they have to spend the money they committed to on exploration. So (indisc.) licenses that have been issued have been fairly large and have been (indisc.) acre limit and are typically then commitment to spend a few million dollars in actual exploration work. If the selections were smaller, on the order of a couple of coal bed methane leases, we would expect that the (indisc.) would be much smaller than that in terms of dollars. But that guarantees that the person who is speculating is actually going to do some work or partner with someone else who is going to do work on the sites evaluated. Then after they finish their evaluation and spend the X amount of dollars they committed, they have a right to convert noncompetitively to a lease.

Number 1128

One of the things that this bill does is it recognizes that nonconventional gas does not necessarily have the same economics that conventional gas or conventional oil does. So a lot of the efforts are showing that it is nonconventional in nature and that it will result in the (indisc.) and allow them to have (indisc.) to 12.5 percent royalty (indisc.) if the gas is noncompeting oil and gas. That puts it on the same economic footing as if you had gotten a noncompetitive shallow gas lease. The program recognizes that the role after licensing is better because it brings interest while we talk about (indisc. paper shuffling) process. You can include the right to explore in a substantial area if you desire and then you can convert to a lease in very reasonable terms. We think it is a better way to do nonconventional gas leasing

in rural Alaska. In large part because the applicant has more (indisc.) rights (indisc. noise in room) and then the economic terms are actually more favorable to the applicant because the (indisc.) to occur. So that is why really we prefer licensing in the rural areas and then (indisc.) agency (indisc.) program. I know this is long winded and hopefully that may be (indisc.).

REPRESENTATIVE STEPOVICH commented that he is worried about the local, generational Alaskan being included in the speculative process that major {companies enjoy}. He said he believes that this bill puts the it back where an individual would have to put up millions of dollars in improving the land. He asked Mr. Myers to comment on that.

Number 1339

MR. MYERS replied that he can respond to that. There are a lot of folks that are purchasing leases in the competitive sale that are primarily locally driven. They can be very successful in buying leases, but it can be very competitive so that the state gets the best dollar for the value. Typically the leases are \$5 minimum bid and often the typical fee will be between \$5 and \$10 per acre. A lot of Alaskans are very successful and have made a lot of money reselling the leases. A net profit is still allowed in this process, he said. He explained that the exploration license realistically in a rural energy type project what we have seen is the interest has been by the individuals that really want to get the energy or that is being underfunded by the (indisc.) ... For example, the Red Dog Mine area the interest in the Healy area, the interest in the (indisc.) area, they are all folks that are doing it because they believe they can either make money doing it, or they are directly related to (indisc. coughing) ... So I think it does provide the opportunity. It doesn't create a great market for resellers. But we do have cases where people have picked up a license and the first thing they do after they get the license is go out and look for partners. I have seen it both ways. So people who do not have the money are willing to buy a license and then find partners who do. I do think the program will work successfully and he does think there is plenty of room in the way we are doing competitive bidding ... (indisc. paper shuffling) minimum bid of \$5 per acre that allows for local Alaskans to be involved in the process and there is a history of that.

CO-CHAIR MASEK asked why miners would object to the provision of this bill. She asked for Mr. Myers to comment on ways the miners can protect their interests with respect to HB 531.

Number 1413

MR. MYERS replied that the miners perspective they want to make sure they have the first shot at having access to the gas that might be contained within the surrounding gas and coal leases (indisc. paper shuffling and coughing) Another divider is the Red Dog mine which is really looked at as a separate energy source. Two cases, coal miners who have active coal leases and folks that are mining that need local energy. He explained that the gas does not belong to (indisc.) lease, it does goes with coal lease. It stays with the state until issued in an oil and gas lease, he said. The old shallow leasing program had some exclusivity with respect to the issuance of shallow gases. For example, if you owned the coal lease, no one else could apply or get the shallow gas lease. At the same time nothing precluded someone from getting an exploration license over that exact same acreage and they are not guaranteed that they would get the license unless they did the work on it. In reality what we see the person likely to get the benefit again is the coal miner who is actually mining the coal near it (indisc.). They are very concerned about the conflict there, are better off with a license, and better off with a best interest finding. That is their concern that right now (indisc. paper shuffling and coughing) to get that lease. What they do not realize is that at any time that right can be taken away (indisc.)

Number 1521

REPRESENTATIVE KERTTULA asked if he was saying that in the "old way" if an individual owned the coal lease an individual could get the exclusive right to get the gas.

MR. MYERS replied that under the current shallow gas leasing program there is language that requires that if an individual holds a coal lease the state couldn't issue a shallow gas lease unless the applicant was the same individual who held the coal lease. So it gave exclusive rights to the coal leaseholder, he clarified. There are lots of other areas in the state, Cook Inlet for example, where there are coal leases making conventional oil and gas (indisc.).

REPRESENTATIVE KERTTULA said that there was an exclusive right under the current program.

Number 1616

MR. MYERS replied yes, but only for the shallow gas lease. They do not have exclusive rights on an exploration license for the same land. Another person could come in and get a license over that same coal lease, and that person would own all the gas in the lease, he explained.

REPRESENTATIVE KERTTULA asked for further clarification. If an individual can get an exploration license, how is it that licensee cannot lease the gas.

MR. MYERS responded that we would lease the gas. He explained that by creating the two different programs over the same ground, a conflict situation has been created. Administratively the department has (indisc.) two licenses for shallow gas leases when one exists on the area. The license rights are greater and more valuable because they address all depths and have a greater life span, he commented. What has been created is a high quality program and a low quality program that conflicts with each other, he summarized. There could be a shallow gas lease to a 3,000-foot [depth] and an exploration license over the top, he reiterated.

Number 1708

CO-CHAIR MASEK asked how [shallow gas lease holders] can protect their interests under this bill.

MR. MYERS replied that it can be done in several different ways. The easiest way is to apply for an exploration license. In the case where an individual had existing shallow gas leases and if he/she is making progress toward development and producing the gas would allow the individual to hold those leases, he explained. He summarized that those individuals holding existing leases are grandfathered in and have those rights. All they have to do is drill a well. Nothing will exclude an individual for applying for an exploration license if he/she holds the lease on the land. He posed a hypothetical example where a coal mine held five or six shallow gas leases now, (indisc.) they could apply for a license for the entire area, and then when the license is granted could relinquish the shallow gas leases. (indisc. paper shuffling)

CO-CHAIR MASEK commented that in a letter to the editor it has been stated that leases could be bought back by the state for

approximately \$200,000 to \$300,000. She asked Mr. Myers if that is a true statement.

Number 1854

MR. MYERS replied that would be determined by how the buy back was structured. If that is the amount of money that was paid for the leases that would be a true statement. The bill also allows for compensation for the amount of work done on the leases. For example, in the Matanuska-Susitna valley millions of dollars have been spent. (indisc. paper shuffling) If that was not adequate the state could reclaim the leases under eminent domain which means that just compensation would be paid for the lease, he said. There is a series of evaluations or a standard methodology which is used to determine the value of the lease. He summarized that he could not say what the numbers would be but it could be quite substantial under the eminent domain claim.

Number 2089

MERLIN THOMPSON testified on HB 531. He told the members that he has not been able to get a copy of the latest CS so his comments are based upon an older version of CSHB 531. Mr. Thompson said that he opposes the (indisc.) of the best interest finding (BIF). He urged the members to add a provision to repeal the local over ride provision of HB 69, and add a provision (indisc.) moratorium over the reissuance of leases that are on non-producing wells. Mr. Thompson told the committee that he had a meeting with the AOGCC recently and found that the commission does not oppose the use of toxic extracting fluids. He commented that he would like to see a mail notice provision and a bill of rights added to the bill. Mr. Thompson said he supports a buy back provision, but is not sure about the eminent domain provision. There needs to be some sort of mechanism in the bill which provides for the buy back, he reiterated.

CO-CHAIR MASEK asked Mr. Thompson if he is located near a legislative information office (LIO).

MR. THOMPSON responded that he was at the LIO earlier today, but the offices are under construction and it was not possible to get a room. The new version of HB 531 was just coming off the fax when he was there, but he said he left because he feared he would miss the meeting.

CO-CHAIR MASEK stated that this is the first hearing of HB 531, and last week there was a meeting on HB 395. She announced that the two bills will be sent to a subcommittee where all the changes will be made. Co-Chair Masek appointed members of the subcommittee; Co-Chair Dahlstrom will serve as chair and Representatives Stepovich and Kerttula will also serve. The subcommittee will bring back new versions of both bills to the committee. There will be adequate time for review and testimony then, she added.

Number 2273

ROBIN McLEAN, Sutton Community Council, testified on HB 531. She asked if she understands correctly that interested parties will be able to testify in front of the subcommittee.

CO-CHAIR MASEK replied that is up to the chair of the [subcommittee]. In response to Co-Chair Dahlstrom's response, Co-Chair Masek told Ms. McLean that she would be able to testify before the subcommittee.

MS. McLEAN reiterated her comments during an earlier meeting [April 7, 2004] on HB 395. She told the members that she believes that the most important elements to be included in these bills is the mail notification to property owners and the owners' bill of rights. She said she is opposed to the best interest finding because it makes citizens who live in rural areas of the state second-class citizens. Ms. McLean shared that she was at a meeting in Healy a month ago and found that the people there are just as concerned about their homes and water wells as those who live in Matanuska-Susitna Borough. She stated that these people want the same protections as other citizens in the state.

MS. McLEAN told the members that she very much favors provisions that would repeal the (indisc.) of HB 69 from last year. That is a very repugnant provision to many people, she commented. She said we (indisc.) provisions from Representative Seaton's bill, HB 364, which would put a moratorium on (indisc.). She said she supports the prohibition of the use of toxic fracturing fluids. Ms. McLean said that during the Senate Resources Standing Committee meeting the commissioner [of DNR] stated that the use of these fluids is fine; however, she urged the members to amend any bill that allows for the use of toxic fracturing fluids. She went on to say that she believes the buy back is fair and right. It is important that all people have the same fair treatment from the government, Ms. McLean summarized.

ROBERT CRANDALL, Petroleum Geologist, Alaska Oil and Gas Conservation Commission (AOGCC), answered questions on HB 531. He told the committee he does not have testimony to present, but is available to answer questions.

REPRESENTATIVE KERTTULA asked if Mr. Crandall heard the previous testifier say that AOGCC stated in a senate hearing that it would not be opposed to the restriction of toxic fracturing fluids. She asked if he would comment on that statement.

MR. CRANDALL said AOGCC would not agree with the term "nontoxic" because he believes a better term for the restrictions would be on "nondiesel." He explained that some of the components of a fracturing fluid are, for example, potassium chloride which can be used as table salt in certain cases. The concentration of it in the fluid could be considered toxic, he commented. Mr. Crandall reiterated that AOGCC does not believe toxic is the appropriate term.

Number 2595

JEFF ARNDT, Friends of the Mat-Su, testified on HB 531. He told the members that he is representing a group called the Friends of the Mat-Su which has about 350 members. He explained that he is handling coal bed methane issues. Mr. Arndt shared that he is in complete agreement with Ms. McLean and Mr. Thompson. He said he believes that by providing an exclusion zone it is creating this two-tiered system to please the citizens in this area, but it is then allowing the trashing of the rest of the state. Friends of the Mat-Su believe the rules should be the same everywhere and that there should be stringent regulations. There should be a best interest finding no matter where it is, he added.

MR. ARNDT commented that he believes Mr. Myers testimony made a very strong case for the buy back provision. He commented that the state basically gave the resources away at \$1 per acre. In looking around the Southwest United States he could not find any lease that sold for less than \$2 per acre. He told the members that he does not agree with the supposition that the state would have to pay the price of the value of the resources in a buyback before the industry has even stated what they want. If the buyback is for the value of the resource, then the state should be taxing the industry on the value of the resource, he said.

MR. ARNDT told the members that he had a talk with Tony Knowles about this issue. Mr. Knowles said it is a bunch of baloney and questioned why the lessees should get any more than they paid for the leases, plus the costs for any activities they have. Right now that is practically nothing, he added. Mr. Arndt said it is waste of time, money, and brainpower in discussing how much money the buyback will be.

MR. ARNDT commented on toxic fluids and said that it is his opinion that anything that would be put in and could come out at any time and destroy any form of life is toxic. This is a bad, secretive system. Make the system as simple as possible by saying only water can be used, he urged. Mr. Arndt said he believes that AOGCC does not look out for the people of Alaska; it is looking out for industry.

CO-CHAIR MASEK asked Mr. Arndt to restrict his comments to HB 531.

MR. ARNDT said in the future he would like to have more than one hour to review new versions of bills because it makes it difficult to address specific points.

CO-CHAIR MASEK commented that there have been many versions of this critical legislation. She added that the best interest finding is no longer in HB 531.

Number 2819

MARY BARRETT testified on HB 531. She said she is very concerned that the state can still override local ordinance such as HB 69. If local governments want stricter regulations to protect the quality of life of a particular area, local governments' wishes should take precedence. Ms. Barrett said she is also concerned that there is no ban on toxic fracturing fluids. If it is not widely used in the industry then there should be no problem with ban fracturing fluids. She commented that she agrees with a previous suggestion offered that just water should be used as a fracturing fluid. She told the members that she remembers when the Clean Air and Clean Water Acts were passed in the 1970s. A common thing that was said is "dilution is not the solution to pollution." Ms. Barrett went on to say that she is still concerned that there is no direct notice being given to landowners that their land is being leased. She said she believes there are still a lot of landowners who are unaware of the fact that their land has been leased. It is difficult to obtain maps of leased areas which is

another reason why landowners need direct notification, she commented. Ms. Barrett went on to say that she believes the buyback of coal bed methane (CBM) leases are important. Ms. Barrett questioned why these leases were sold for a dollar per acre if there are high potential earnings. She also questioned why the taxes are so low if there is such a high value.

Number 2908

REPRESENTATIVE GUTTENBERG asked Ms. Barrett if she could suggest a way to provide adequate notification.

MS. BARRETT responded that a certified letter in the mail with a map showing what areas are leased.

Number 2936

MIKE McCARTHY, Kachemak Bay Property Owner's Alliance, testified on HB 531. He told the members that he represents more than 1,000 members of the Kachemak Bay Property Owner's Alliance. He shared that he is a Homer resident and a retired geologist.

TAPE 04-20, SIDE B

MR. McCARTHY told the members that Jack Chenoweth, Legislative Legal and Research Services, testified that there was nothing in the ten points of the bill of rights that could not be amended in the lawful language and placed in statute form this year. He read a portion of a letter that was written by a local realtor as follows:

I am writing this letter to express my recent professional experience in regard to the coal bed methane lease issue. Because of the leases that were activated without proper public notice or input and the ensuing controversy the markets for raw land in my opinion have been compromised. I have personally experienced a solid buyer, that is an investor who has purchased property through me in the past, who decided to forget several purchases when he found out they were in an area where the subsurface rights had been leased. I also have clients who purchased property through me last summer, call me, and express grave concern and alarm because they had just found out that property that they had purchased off East (indisc.) Road was part of the lease. They had anticipated moving their young family to this property to enjoy a

quiet rural lifestyle not available to them in southern Massachusetts. They are now discussing changing their plans and selling their property. However, the threat now of not being able to resell and recoup their losses is very real, since more and more buyers are refusing to purchase properties affected by these leases. In my opinion this was a very ill advised decision made within the state of Alaska bureaucracy and it is impacting me personally and my ability to do business as well as impacting the property values and the ability of owners to sell their property.

Number 2882

MR. McCARTHY commented that he would skip a few paragraphs in the letter and continued to read the letter as follows:

The Homer leases have impacted owners in 32 separate states who were never notified by the state, but in turn were notified by the Kachemak Bay Property Owner's Alliance at our own expense and time. The assessed value of these 1,029 properties amounted to \$66,432,700, and for that the state received, for 22,000 acres, a total of \$28,000. That seems like a very poor cost benefit ratio especially when you consider that director Mark Myers testified earlier, last month I believe, that approximately half of all royalty would be used to administer CBM development and at present there are not sufficient personnel on staff to do that job. This again does not take into account the property values that would impact the borough property tax intake which would be several million dollars. Again, a far larger amount than what it's going to generate in terms of royalty. We are not unrealistic in our concern for improperly regulated CBM development. We have obtained resolutions from the City of Homer dated 12/1/03, resolution 03-0147, and another resolution from Kachemak City, resolution number 2003-1280.

Number 2799

CO-CHAIR MASEK interrupted Mr. McCarthy and explained that there are others who wish to testify. She asked if he would submit any written testimony to the committee.

MR. McCARTHY continued:

Kachemak City passed a similar resolution, as did the Kenai Peninsula Borough, which is extremely impressive if you consider the percent of tax base, et cetera, that the Kenai Peninsula Borough has involved in oil and gas. They passed that on 12/16/03. A resolution to place a moratorium on CBM development and also call attention to improper public notice by which it was started.

MR. McCARTHY said he would like to end his testimony by saying he believes there needs to be a moratorium on coal bed methane development in the state until regulations are in place to properly proceed.

Number 2728

KEN BOYD, Chairman, Lands Exploration and Operations Committee, Alaska Oil and Gas Association (AOGA), testified on HB 531 and answered questions from the members. He told the members that AOGA is a private non-profit trade organization whose 19 member companies represent the majority of the oil and gas operations in the state. He commented that he just got a copy of version U of the bill a little earlier this afternoon and prefaced his comments by saying that AOGA is very much in favor of this legislation.

MR. BOYD told the members that he has a problem with language on page 40, line[s] 8 [and 9], which reads as follows:

(3) for a nonconventional gas lease, if a bond is sought under AS 38.05.130, ...

MR. BOYD explained that this language was largely removed from version S of the bill, but seems to have reappeared. He commented that there has to be a bond before a lease can be issued. Mr. Boyd referred to page 40, line [10 and] 11, which reads as follows:

(A) before the amount of the surety bond to be posted is determined by the director, require, as a condition for issuing the lease, ...

MR. BOYD pointed to additional language on page 40, lines [17] through 19 as follows:

(B) in addition to the coverage for actual damages required by that section, provide for payment of reasonable compensation to the owner for any loss by the owner of the owner's use and enjoyment of the property.

MR. BOYD told the committee that terms such as "reasonable compensation" and "use and enjoyment" are undefined terms. He said that other than these sections AOGA can support the bill. Mr. Boyd stated that AOGA is on record as supporting the best interest finding for oil and gas leasing and exploration licensing which is contained in HB 531. Alaska Oil and Gas Association believes there are adequate safeguards for shallow gas leasing under existing law, but also believes that a higher level of public policy is achieved by adopting the best interest finding approach. A best interest finding is used in all oil and gas programs in Alaska and works well for both the members of the public and the private companies that are investing in Alaska, he stated. The best interest finding process allows the state to incorporate all public input into a single legally defensible document that will address all concerns in a comprehensive manner, Mr. Boyd summarized. The existing shallow gas-leasing program was crafted with bipartisan support during a democratic administration. This support was justified since this program has the potential to provide new sources of clean efficient energy to the state as well as provide jobs and taxes for local economies, he said. He told the members that AOGA hopes that further discussion of these issue will facilitate a better understanding of the environmental and property right protections already in place and the historical successes in state development. Mr. Boyd said the Department of Natural Resources has conducted extensive workshops and discussions related to CBM shallow gas development in the Matanuska-Susitna valley.

Number 2567

CO-CHAIR MASEK welcomed Marilyn Crockett who is present in the audience listening to testimony.

CO-CHAIR MASEK reiterated that HB 531 will be assigned to a subcommittee. That ends public testimony on the bill for the day, she said.

REPRESENTATIVE KERTTULA stated for the record that she may have a conflict of interest in HB 531 because her family owns land in

the Matanuska-Susitna valley. She said it appears that one piece of land is in a leased area.

HB 395-SHALLOW NATURAL GAS/ OIL AND GAS

[Also contains discussion of HB 69.]

Number 2507

CO-CHAIR MASEK 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 2488

CO-CHAIR DAHLSTROM moved to adopt CSHB 395, 23-LS1314\O, Chenoweth, 4/13/04, as the working document. There being no objection, CSHB 395, version O was before the committee.

CO-CHAIR MASEK directed the members attention to written testimony included in their packets from a [Ms]. Wieland of Homer, as follows:

[original punctuation provided]

Thank you for hearing this bill and opening it to public testimony - glancing quickly at HB 395, there seems to be a number of good provisions. I'd like to see removal of use of fracturing fluids to protect our aquifers. I'm still concerned about the amount of power the DNR commissioner has, and I'd like to see that lessened. Please allow a second opportunity for public to testify.

Although this bill provides several good provisions, I'd still like to see all the leases bought back so we don't have this sword hanging over our South Peninsula and Mat-Su heads. Then, consider starting over with a best interest finding and stay far away from private property unless owners want (indisc.). Thank you.

Number 2469

RICK VANDERKOLK, Staff to Representative John Harris, Alaska State Legislature, testified on HB 395 on behalf of Representative Harris, sponsor. He told the members that in compliance with Co-Chair Masek's request a review has been done

on comments by John Norman of the Alaska Oil and Gas Conservation Commission (AOGCC). A couple of housekeeping changes have been made with respect to that review. He pointed to page 3, line 23, the word "punitive" was removed and replaced with the word "actual", so it now reads as follows:

(c) If a developer fails to give notice as provided in this section, the surface owner may seek any appropriate relief in the court of proper jurisdiction and may receive actual damages.

MR. VANDERKOLK explained that the prior language was redundant because it is already covered under AS 38.05.130.

MR. VANDERKOLK then referred to page 4, line [10 and] 11, as follows:

(4) "oil and gas operations" means an activity for which a permit is required by AS 31.05.090 that requires entry upon the surface estate;

MR. VANDERKOLK explained that the AOGCC was concerned that the language be very specific as to the definition of oil and gas operations so the reference to AS 31.05.090 was inserted which refers to permits and fees to drill wells. Mr. VanderKolk summarized that those are the only two changes made to version 0.

Number 2333

JEFF ARNDT, Friends of the Mat-Su, testified on HB 395. He said he likes that the 3,000-foot well depth limitation was reinserted in the bill, rather than the convoluted language about waivers. In Section 6, [page 5,] beginning on line 12, there is language which discusses the water well testing requirements which states it is limited to one-quarter mile radius around the drill site. He said he does not believe that even comes remotely close to taking into account how water travels. He stated he believes this is way too small an area. Section 10 still does not provide direct notification of property owners in leased areas. He asked that there be a certified letter to every landowner in the area. Mr. Arndt commented that he likes Section 11 where there is a repeal of the state's override policy. He told the members that he believes the committee should consider limiting DNR's discretion to reissue current leases. He reiterated that he would like to see the bill amended to include the buyback of the leases

because none of the bills address the 230,000 acres of the Matanuska-Susitna valley that have already been leased.

Number 2215

MARY BARRETT testified on HB 395. She told the members that she agrees with what was just said and wishes that HB 69 be repealed. Ms. Barrett emphasized that she believes a certified letter of notification to all landowners in the leased areas is appropriate. All wells should be tested, not just the one-quarter area around drill site, she said. People are very concerned about their wells being contaminated or their wells drying up. The property owners' bill of rights should be adopted because that would provide the protection the property owners' desire. It would remove the perception that industry's rights take precedence over property owners, Ms. Barrett stated. The bill doesn't address current CBM leases and urged the buy back of these leases. Please tax the companies on what is owed until the buy backs are done, she asked.

Number 2131

MERLIN THOMPSON, Chairman, Ogan is So Gone Recall, testified on HB 395. He told the committee that he supports the comments made by the prior testifiers. Mr. Thompson referred to page 5, line 19, and said he believes that testing should be expanded beyond the drill site. He suggested that testing include conductivity as well as solvents. There should be extra concern and testing for any disposal well because of the amount of contaminants that are put in them, he emphasized. Mr. Thompson commented that he believes the \$1 per acre cost in leasing is extremely low. He added that he believes that there should be a buyback provision included in the bill. The bonds that have been posted are outrageously low, he said. Mr. Thompson stated for the record that he received a copy of version O of the bill at 1:53 p.m., a copy of version U at 2:40 p.m., and this committee was scheduled to start at 1 p.m. He stated that it makes it tough to testify on the particulars of any bill if an individual does not receive the bill until after the meeting starts.

Number 1977

ROBIN McLEAN, Sutton Community Council, testified on HB 395. She told the members that she spoke last week and gave a couple of specific suggestions, as did Mr. Norman from the AOGCC. It is troubling when hundreds of people have testified at meetings

and workshops in the valley and the people speaking today are speaking for them. They unanimously agree on many things, but none of those suggestions that were made to the committee last week have been included in the new version, whereas the AOGCC representative's suggestions were addressed. Ms. McLean said she wanted to note that point. She emphasized that the people in the valley want actual notices for these leases before they happen. People want a letter, she stated. Ms. McLean said she hopes the subcommittee will include that element in the bill. There is concern about the vague language in the bill. For example on page [5, lines 27 through 29] which reads:

...the terms of the lease must require the lessee or lessee's agent to negotiate to meet the requirement of this paragraph, but the owner may not unreasonably withhold agreement;

MS. McLEAN emphasized that the language is very vague and strongly urged the committee to revise it. This language creates an amazing feeling of insecurity with people. She urged the committee and subcommittee to add the buy back provision and a moratorium on the reissuance of leases of nonproducing (indisc.). She commented that Mr. Myers testified that 60 percent of the leases were bought on speculation. If the leases aren't valuable let the property owners have the weight off their mind that the leases will sunset in two and a half years. It would be a great relief to many property owners, she reiterated. Ms. McLean suggested that someone besides DNR testify on the buyback provision because hundreds of people in the valley want the buyback.

Number 1763

MIKE McCARTHY, Kachemak Bay Property Owner's Alliance, testified on HB 395. He reiterated that he is in agreement with the prior testimony. Mr. McCarthy pointed to page 5, [lines 12 through 18], Section 6, subsection (2), which reads as follows:

(2) a water well testing requirement for each lease that contains one or more wells that serve as a source of potable water; the testing requirement of this paragraph applies to each water well that is located within a square that bounds a circle with a radius of one-quarter mile around the drill site and the sides of which are parallel or perpendicular to the four cardinal directions and are tangent to the circle; under this paragraph, the lessee shall, before

commencement of production testing and production activities on the lease, ...

MR. McCARTHY commented that he does not believe that is equivalent when thinking about hydrologic fracturing pressure that can be as much as 10,000 pounds per square inch. He stated that is a phenomenal amount of pressure to contain in one-quarter mile and is not adequate. Mr. McCarthy reminded the members of the alliance's desire for all property owners to be notified by certified mail. He said that is the same standard by which Minerals Management Services operates and he said he believes the state should do no less.

REPRESENTATIVE GUTTENBERG commented that he has not heard much in the way of testimony on setbacks, terminations, and abandonment's of exploration and development operations. He questioned what the position is of Kachemak Bay Property Owner's Alliance on these issues. Does the bill adequately address the alliance's concerns, Representative Guttenberg asked.

Number 1615

MR. McCARTHY responded that he received the latest draft five minutes before testimony began so he cannot comment on the difference between this version and the prior one. The problem of abandonment and the possibility of companies going under, which in the typical lifespan of the lower 48 CBM business the initial companies that come in are the cream of the crop. They are the best of the CBM producers. As they draw down on the reserves the property gets passed down to less and less reputable companies. The potential for a company that is not financially solvent just walking off and leaving all sorts of potential danger to the property owner needs to be taken into account, he said. Mr. McCarthy summarized that he does not know if that point is addressed in the latest version of the bill.

Number 1584

MARK MYERS, Director, Division of Oil & Gas, Department of Natural Resources (DNR), during bill hearing on HB 395, provided information and answered questions. He explained that what the state has adopted has been a policy of having bonded (indisc.), but recognizing that the transfer of the property that delves sinking funds or bonding mechanisms to get the significant bonding requirements. The problem that Mr. McCarthy mentioned is one that is commonly seen in conventional oil and gas leasing in places like Texas where companies will sell its property when

it reaches the end of field life to smaller operators that are less financially secure and not capable of doing the reclamation work, he commented. The department has two mechanisms, he said. When leases are transferred it is required that there be bonding or sinking funds particularly for the financially weaker companies. Secondly, the liability does not go away with the transfer. The parent company of the original lessee is still held responsible, he explained. The division is very cognizant of the issue and has done a good job of avoiding the abandonment risk. It has been accomplished through the way the leases are written and the bonding process, he added.

MR. MYERS told the members that DNR supports HB 395 as written. There are a lot of protections in HB 395. The department sees HB 395 as a companion bill to HB 531 which addresses the leasing issues, while HB 395 addresses the overall regulation of CBM activity, he said. Where there is CBM activity, no matter where it is in the state, these are the kinds of requirements that provide additional protections, he said.

MR. MYERS commented that the water-testing requirement where there is a quarter-mile issue is not that clear. There is no magic number, he added. Mr. Myers explained that the quarter-mile was established because if there are effects from these activities these wells would be the first to experience problems. Mr. Myers pointed out that this does not preclude other testing. He reiterated that DNR supports this bill. The process is advancing in the [Matanuska-Susitna] valley and there will be a draft next week which will reflect the public's recommendation.

Number 1246

REPRESENTATIVE KERTTULA asked what he said about next week.

MR. MYERS replied that the division expects to have the draft report from the five meetings in the [Mat-Su] valley available next week. It will be available for a period of time and the division will accept public comment on the recommendations. Those comments will be finalized and final findings and regulations will be issued by the DNR commissioner.

CO-CHAIR MASEK asked if Mr. Boyd would like to comment.

Number 1186

MR. BOYD replied that he has no additional comments on HB 395.

CO-CHAIR MASEK announced that HB 395 will be held in committee. The subcommittee will work on HB 531 and HB 395 and report back to the chair with revised bills, she said.

ADJOURNMENT

There being no further business before the committee, the House Resources Standing Committee meeting was adjourned at 3:02 p.m.