ALASKA STATE LEGISLATURE
SENATE RESOURCES STANDING COMMITTEE
March 26, 2004
3:40 p.m.

TAPE(S) 04-30, 31

MEMBERS PRESENT

Senator Scott Ogan, Chair
Senator Thomas Wagoner, Vice Chair
Senator Fred Dyson
Senator Ben Stevens
Senator Kim Elton

MEMBERS ABSENT

Senator Georgianna Lincoln
Senator Ralph Seekins

COMMITTEE CALENDAR

SENATE BILL NO. 69
"An Act relating to participation in matters before the Board of Fisheries by members of the board; and providing for an effective date."

MOVED CSSB 69(RES) OUT OF COMMITTEE

SENATE BILL NO. 312
"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

PREVIOUS COMMITTEE ACTION

BILL: SB 69
SHORT TITLE: BOARD OF FISHERIES CONFLICTS OF INTEREST
SPONSOR(s): SENATOR(s) WAGONER

02/14/03	(S)	READ THE FIRST TIME - REFERRALS
02/14/03	(S)	STA, RES
03/25/03	(S)	STA AT 3:30 PM BELTZ 211
03/25/03	(S)	Moved Out of Committee

03/25/03	(S)	MINUTE(STA)
03/26/03	(S)	STA RPT 5DP
03/26/03	(S)	DP: STEVENS G, HOFFMAN, COWDERY,
03/26/03	(S)	DYSON, GUESS
03/19/04	(S)	RES AT 3:30 PM BUTROVICH 205
03/19/04	(S)	-- Rescheduled from 03/08/04 --
03/26/04	(S)	RES AT 3:30 PM BUTROVICH 205

BILL: SB 312
SHORT TITLE: CONVENTIONAL & NONCONVENTIONAL GAS LEASES
SPONSOR(s): RESOURCES BY REQUEST

02/09/04	(S)	READ THE FIRST TIME - REFERRALS
02/09/04	(S)	RES, FIN
02/23/04	(S)	RES AT 3:30 PM BUTROVICH 205
02/23/04	(S)	Heard & Held
02/23/04	(S)	MINUTE(RES)
03/05/04	(S)	RES AT 3:30 PM BUTROVICH 205
03/05/04	(S)	<Above Bill Hearing Postponed>
03/22/04	(S)	RES AT 3:30 PM BUTROVICH 205
03/22/04	(S)	Heard & Held
03/22/04	(S)	MINUTE(RES)
03/26/04	(S)	RES AT 3:30 PM BUTROVICH 205

WITNESS REGISTER

Ms. Amy Seitz
Staff to Senator Thomas Wagoner
Alaska State Capitol
Juneau, AK 99801-1182
POSITION STATEMENT: Commented on SB 69 for sponsor.

Mr. Chris Garcia
Beaver Lake Rd.
Kenai AK
POSITION STATEMENT: Supports SB 69.

Mr. Paul Shadura, President
Kenai Peninsula Fishermen’s Association
Soldotna AK
POSITION STATEMENT: Supports SB 69.

Mr. Ken Boyd, Chairman
Land Exploration and Operations Committee
Alaska Oil and Gas Association (AOGA)
121 West Fireweed Lane
Anchorage, Alaska 99503

POSITION STATEMENT: Commented on SB 312.

Commissioner John Norman
Alaska Oil and Gas Conservation Commission (AOGCC)
333 W. 7th Ave., Ste. 100
Anchorage, Alaska 99501
POSITION STATEMENT: Supports SB 312.

Mr. Bob Crandall, Petroleum Geologist
Alaska Oil and Gas Conservation Commission (AOGCC)
333 W. 7th Ave., Ste. 100
Anchorage, Alaska 99501
POSITION STATEMENT: Supports SB 312.

Commissioner Dan Seamount
Alaska Oil and Gas Conservation Commission (AOGCC)
333 W. 7th Ave., Ste. 100
Anchorage, Alaska 99501
POSITION STATEMENT: Supports SB 312.

Mr. Robert Hall, Vice President
Houston Chamber of Commerce
Houston AK
POSITION STATEMENT: Commented on SB 312.

Ms. Kristin Ryan, Director
Division of Environmental Health
Department of Environmental Conservation
410 Willoughby
Juneau, AK 99801-1795
POSITION STATEMENT: Commented on SB 312.

Mr. Larry Ostrovsky, Assistant Attorney General
Department of Law
PO Box 110300
Juneau, AK 99811-0300
POSITION STATEMENT: Commented on SB 312.

ACTION NARRATIVE

TAPE 04-30, SIDE A
^#SB69

SB 69-BOARD OF FISHERIES CONFLICTS OF INTEREST

CHAIR SCOTT OGAN called the Senate Resources Standing Committee meeting to order at 3:40 p.m. Present were Senators Thomas

Wagoner, Ben Stevens, Fred Dyson, Kim Elton and Chair Scott Ogan. The first order of business to come before the committee was SB 69.

SENATOR THOMAS WAGONER, sponsor, moved amendment 1, which would sunset SB 69 as of June 30, 2009, and stated that the rotation schedule for the Board of Fish hearings runs on a three to four-year basis. The effective date reflects a complete rotation of the hearings.

23-LS0313\H.1
Crawford/Cook
1/7/05

A M E N D M E N T 1

OFFERED IN THE SENATE BY SENATOR WAGONER

TO: SB 69

Page 2, following line 1:

Insert a new bill section to read:

"*** Sec. 3.** AS 39.52.120(c) is amended to read:

(c) In addition to other provisions of this section, a public officer who is a member of the **Board of Fisheries or the** Board of Game may not act on a matter before the board if the public officer has not disclosed in the manner set out in AS 39.52.220 all personal or financial interests in a business or organization relating to **fish or** game resources."

Renumber the following bill sections accordingly.

Page 2, following line 10:

Insert a new bill section to read:

"*** Sec. 5.** AS 39.52.120(e) is repealed."

Renumber the following bill section accordingly.

Page 2, line 11:

Delete "This Act takes"

Insert "Sections 1, 2, and 4 of this Act take"

Page 2, following line 11:

Insert a new bill section to read:

"*** Sec. 7.** Sections 3 and 5 of this Act take effect June 30, 2009."

SENATOR KIM ELTON objected for an explanation. He asked if section 7, in effect, repeals section 3 in 2009 and section 3

provides that the board member may not act without disclosure. He questioned the purpose of the bill is to allow people to declare a conflict and still go ahead and vote that can only happen until 2009.

SENATOR WAGONER indicated that was correct. He let Ms. Amy Seitz elucidate.

MS. AMY SEITZ, staff to Senator Thomas Wagoner, explained that by 2009, if the Legislature decides the proposed amendment is not working, the law would just revert to the way it is now, but if it is working, the Legislature could either repeal the repeal, extend the sunset or get rid of it altogether.

SENATOR ELTON said he liked SB 69 and tended to believe that the bill would work, but if it didn't, the Legislature could fix it. ".... In this case, we'd have to fix it if it is working out."

CHAIR OGAN said he was probably a no-vote without the amendment, because he felt, at a minimum, eyebrows would be raised. "All fish politics are local, as you know." He thought that having a sunset would keep people who are serving on the board mindful that this is being tested for a while and forces the issue to come back before the Legislature for review.

SENATOR ELTON asked for and was granted some latitude in discussing Senator Ogan's concerns, which accrue to the sportfishing component of the board. He didn't think a Mat-Su sportfish board member should conflict himself out when dealing with Cook Inlet fishing issues.

> .... I understand that there are perception issues and sometimes those are very, very dangerous, but we're dealing here with a board of seven people. If you have a person or two people - I would imagine there may even be occasions in which some of the decisions may require three people to conflict themselves out – you're then put in a position where you've got four people making the decision. It makes it difficult, then, to do the board's work....

SENATOR ELTON suggested again that the law could be changed if it doesn't work.

CHAIR OGAN responded that he understands if people are required to conflict themselves out of certain issues, the board would probably lose the person on the board that has the most

knowledge about that particular fishery. He didn't think it was a bad thing to bring expertise to the process.

SENATOR ELTON maintained his objection.

CHAIR OGAN asked for a roll call vote. Senators Ben Stevens, Thomas Wagoner and Chair Scott Ogan voted yea: Senators Fred Dyson and Kim Elton voted nay; and amendment 1 passed.

MR. CHRIS GARCIA, Kenai resident, supported SB 69 except that he wanted to insert a provision to kick any member off the board who might fail to disclose a conflict of interest after being challenged and that person should not be allowed to serve again for 10 years.

MR. PAUL SHADURA, President, Kenai Peninsula Fishermen's Association, supported SB 69.

> What would it be like to not allow beauticians and barbers to comment on regulations within their state industry board? What would it be like to have the Board of Physicians not allow debate on votes by physicians on regulatory changes or have a heart surgeon, more or less, not comment on that particular board on heart surgery because he may have direct or indirect benefits? The point is the public relies on expertise of individuals sitting on boards and commissions to direct and revise for the best practices and management for the state's best interest....

He added that it's really rare that a commercial fisherman active in Cook Inlet has a seat on the Board of Fisheries. Currently, none are and it doesn't seem like there will be one in the foreseeable future.

CHAIR OGAN said he had received letters in opposition to SB 69 from the Mat-Su Valley Fish and Game Advisory Committee, the Alaska Outdoor Council, and the Alaska Sportfishing Association.

SENATOR WAGONER pointed out that he took exception to an e-mail from the representative of the Alaska Sportfishing Association that in part said:

> I have been unable to find out what Senator Wagoner's agenda on this is so I can discuss why he sponsored this bill.

SENATOR WAGONER responded:

> I sponsored this bill number one, because I was asked by the Salmon Task Force to sponsor it. This is a bill that the Salmon Task Force spent a lot of time on and crafted and wanted to go through the Senate. I find it's insulting to have people write those type of e-mails without contacting me first and discussing it. I would have been glad to discuss that with this gentleman and let him know, but he saw fit to use the e-mail this way. I just want to put on the record that I don't appreciate that.

SENATOR WAGONER moved CSSB 69(RES) and accompanying fiscal notes with individual recommendations.

CHAIR OGAN objected. He asked for a roll call vote. Senators Fred Dyson, Thomas Wagoner, Kim Elton and Ben Stevens voted yea; Chair Scott Ogan voted nay; and CSSB 69(RES) moved from committee.
#

4:00 – 4:01 – at ease
^#SB312

SB 312-CONVENTIONAL & NONCONVENTIONAL GAS LEASES

CHAIR SCOTT OGAN announced SB 312 to be up for consideration. He recapped that the committee had a conceptual amendment that wasn't adopted and he intended to finish that discussion and work on getting a CS to consider.

SENATOR ELTON noted that he was having a difficult time dealing with the conceptual amendment and the bill of rights that was drafted in non-bill form and asked Legislative Legal Services to draft an amendment incorporating most of its elements. He wasn't going to move the amendment today, but wanted to make sure everybody saw it. An accompanying memo explains the different elements that didn't go as far as the drafters of the property owners' bill of rights wanted it to go, but Legislative Legal Services pointed out (6)(i) and constitutional problems.

CHAIR OGAN stated for the record that on two occasions two separate individuals who are associated with leadership of a group in the Mat-Su Valley threatened him.

> One said you pass this through both bodies and we'll call off the dogs - and they're referring to my recall - and the other person said that the recall would go away in a heartbeat if I just do this legislation for them.
>
> I just want to state very clearly for the record that this committee is always about good state policy and I think, for the most part, with some maybe minor exceptions, I think to a great degree I want to really commend the members of this committee that when we walk in this door, I think most of our partisan differences get left behind. I really salute the minority for working with me. I try to work with the minority as well as all majority committee members. I will always do what I believe is the best thing policy-wise for the state regardless of the heat I get.

SENATOR ELTON added:

> Because of those remarks, I think it's important that I note for the record that none of those people have talked to my office. I had the amendment drafted, not because of any representations that were made to me by anybody in the Valley, but simply because I was having a very difficult time dealing with how you take something that is in non-legal form and incorporate it conceptually. For me, I needed to have something in writing in amendment form. That's the reason I have brought the amendment to this table, not for any other purpose such as the purposes that you suggested that some people have mentioned to you.

CHAIR OGAN said he didn't mean to infer that Senator Elton had the amendment drafted for any other reason. "I believe you have been very honorable in this committee as all the other members have...."

MR. KEN BOYD, Chairman, Land Exploration and Operations Committee, Alaska Oil and Gas Association (AOGA), said it is a private non-profit trade association whose 19 member companies represent the majority of oil and gas operations in this state.

> AOGA is on record supporting the concept of a best interest finding for oil and gas leasing and exploration licensing as contained in SB 312. While we

believe there are adequate safeguards for shallow gas leasing under existing law, we also believe a higher level of public policy is achieved by adopting a time-tested best interest finding approach for dispositions of state land. A best interest finding is used in all other oil and gas programs in Alaska and works well for both the members of the public and the private companies interested in investing in Alaska.

The best interest findings process allows the state to incorporate all public input into a single document that will address all concerns in a comprehensive manner. We've not had the opportunity to thoroughly review what has been referred to as the Alaska Property Owners' Bill of Rights. However, a first and very quick reading indicates both legal challenges and perhaps some misunderstandings - for instance, about the extent of current protection for property owners, the extent of state laws, local laws, regulations and mitigation measures that already protect Alaska's air, water, fish and wildlife resources, and lastly, the historic benefits to all the citizens of the state when the state owns the subsurface of its selected lands.

As many of you, I presume all of you, know [split-estate] is one of the state issues that is common throughout the western United States. Indeed, there are more than 100 years of case law laying out the rights of both the surface and subsurface owners. One estate occurs when one party owns the surface, which is usually a private citizen or a number of private citizens and one other party owns the subsurface. The subsurface owner is often the federal government or the state, but in Alaska it can also be a Native Regional Corporation. The challenge always is to protect the rights of access to the subsurface while protecting the rights of owners of the surface. In fact, in most cases, agreement has been reached between the surface and subsurface owners.

The existing shallow gas-leasing program was crafted with bi-partisan support during a democratic administration. This support was justified since this program has the potential to bring new sources of clean, efficient energy to the state as well as providing jobs and taxes for local economies. It can

be done in an environmentally safe manner under current law and can be done in a manner that respects the rights of both private property owners and the lessee of the subsurface. In fact, the Department of Natural Resources has conducted extensive workshops and discussions [indisc.] the coalbed methane (CBM) shallow gas development in the Mat-Su Valley and in Homer. We are hopeful that further discussion of these issues will facilitate a better understanding of the environmental and property right protections already in place in a historical success of split estate development. Thanks for your time, Mr. Chairman and members of the committee. AOGA looks forward to this being part of the informed decision-making on this subject and that concludes my testimony.

CHAIR OGAN asked him for his background in the oil and gas industry and in the public sector.

MR. BOYD responded that he was deputy director of the Division of Oil and Gas from 1990 – 1995 and was director of it from 1995 – 2001. In the private sector, he was an exploration geophysicist for 20 years.

CHAIR OGAN said the property owner consent provision of the conceptual amendment basically says that the property owner can just say no and the state must also provide a legal fund for them to hire legal counsel. They must also be protected from retaliatory lawsuits by developers.

CHAIR OGAN asked:

What effect has it on resource development if surface owners could basically say no? Isn't that like just a transfer of an asset that they didn't buy – the subsurface – into their control?

MR. BOYD replied:

Well, in my opinion, Mr. Chairman, I don't think you can make good public policy by demands raised by small groups of citizens, no matter how well-meaning they may be. If I had to base decisions based on every document that came across my desk when I was director, the state would be a hodge-podge of conflicting opinions and conflicting rules and nobody would

benefit from that. That's why AOGA and me, personally, support the notion of a best interest finding.

I believe, Mr. Chairman, when I look at the bill of rights, that we can agree on numbers 4 and 10. Let's have competitive bidding and your bill does that. And in order to have competitive bidding, then we need to have a best interest finding. Fine, let's do that, too. Then let's take the other numbers and let the state go through its process, which they have already begun, in a sense. I mean they've already had a bunch of hearings in a lot of different affected communities - and take these issues one by one, decide what's in the best interest of the state and put it into a legally defensible document and then you have something you can work with instead of a hodge-podge of conflicting notions.

CHAIR OGAN asked if he wanted to comment on the buyback provisions.

MR. BOYD replied that he probably shouldn't comment, but he personally has listened to the director of the Division of Oil and Gas, Mark Myers', testimony and agreed with him that a buyback would come at a cost to the state. He also heard something about the state not getting its full value if it buys back leases for more than it paid for them and refuted, "That's nonsense."

I mean, what would you value Prudhoe Bay at then? What should we have leased Prudhoe Bay at - $150 billion - and had no takers? Companies have to take risks and they put money on the table to take that risk. I think the state, you know, owes them something for that risk and we collect our 12.5 percent share. So, I can't talk to a number, Mr. Chairman. I don't know what the number is. Whatever Mark says, I would support it assuming that he has the backup and I'm sure that he does. So, it will cost him more than just saying, gee, you came to a lease-sale; here's your money back. Here, take your leases. I don't think that's fair. I don't think it's right. I think it's a lousy and terrible precedent for the state.

CHAIR OGAN asked if a buyback had happened in the past – in lower Cook Inlet.

MR. BOYD replied that happened a long time ago, but he noted that the Legislature made Kachemak Bay off limits to gas leasing and it remains off limits to this day. The only buyback he is familiar with is the federal sale in Bristol Bay that was held about 15 years ago when millions and millions of dollars had to be paid back to the companies.

SENATOR WAGONER remembered a Chevron lease buyback in 1972.

SENATOR ELTON recollected that happened in the Hammond administration in 1974.

CHAIR OGAN explained that the Property Owners' Bill of Rights advocates that all 74 leases be bought back and asked what would happen if the state did that. Also, a program on Channel 2 indicated the Agrium Plant might pull out of Cook Inlet because of gas supply issues.

MR. BOYD replied he wasn't sure how Agrium's decision related to this issue, but a buyback just says the state can't be trusted.

> A lease sale is more than just expending money. A lease sale, I mean, people don't even want you to know where they are going to bid. And when they have bid, of course, they've shown their cards, basically. They've said we're willing to pay this many dollars for these acres. When that's done, that goes on a map that becomes a public document and everybody gets to see it – all their competitors. I mean, you've really bared your soul. And then to say oh well, thank you very much, here's your bid back; we already know your strategy. What will you do in the future then? Who's going to trust anybody to do something like that? I think it creates a very bad precedent for the state, Mr. Chairman, and if we're talking about Cook Inlet and the Mat-Su Valley, and I'll just speak very frankly, I think the stakes in terms of dollars are relatively low. But if you take the same situation to the Slope, and I have no reason to believe that if you do it here, you won't do it there, then I think the stakes become enormously high.

CHAIR OGAN said he suspected a buyback would put the state in a bit of a tight position. He invited Mr. Norman to comment.

MR. JOHN NORMAN, Commissioner, Alaska Oil and Gas Conservation Commission (AOGCC), said he had practiced as a lawyer for 33 years and would address the Property Owner's Bill of Rights.

In section 8, which addresses water protection, there are four things that are sought to be accomplished as I read it. One of them is to prohibit production of coalbed methane from aquifers. A second is to prohibit the use of toxic hydraulic fracturing fluids and the third is to require the deep injection of liquids and waste produced in conjunction with coalbed methane. A fourth is to insure that there is no hydrologic connection – no communication between injection zones and fresh water sources. So, looking at those, all of these, I think are attainable goals and many of them, in fact, are consistent with existing law right now.

A prohibition on production from aquifers used as a source of existing or future water perhaps is not good public policy if it were to find its way into law as a blanket prohibition. In some areas, this coalbed methane may be very welcome as the first local fuel that many communities have had and so the commission would suggest that if we were to rule out production from what we refer to as a same source aquifer, that there be an exception for an operator to petition the AOGCC and the commission to make a finding that production would not in any way degrade the aquifer as a source of fresh water. I think we are very confident that we could provide a forum and offer a fair hearing and reach a determination and, if it looked like it would degrade the aquifer, then the exception requested would not be granted, but we would avoid having Alaska paint itself into a corner, because very often aquifers cover large areas and it would not be advisable to rule that out.

As to the second thing, prohibiting the use of toxic hydraulic fracturing fluids – we're certainly supportive of that in this area. If this does make its way into an actual amendment, then we would perhaps have some fine-tuning on the wording to offer, but we see that as doable.

The third objective in section 8 is to require deep underground injection of the liquids and waste produced and we would, here, suggest that it would not

be advisable, again, to make a blanket rule that would absolutely require all produced water, for example, to be reinjected, that there are certainly occasions and examples where the water coming out is of very good quality and might be put to a beneficial use on the surface. But, insofar as injection is the choice of the operator and the land owner and is the sensible thing to do, then we think it's very workable that that requirement would be imposed – to be injected deeply, the idea being that it would be well below any aquifer that's used as a source of fresh water.

The term 'existing or future water wells' is used and, of course, future water wells is open-ended and we might suggest 'existing or which could reasonably be expected as a source of future fresh water' be substituted.

Finally, a fourth objective is insure no hydrological connection between the waste water injection zones and present and future drinking water sources. And here, we have no problem with that; in fact, we do that already and have done that and the statutory authority for that already exists in AS 31.050.30, (d)(3).

In summary, on section 8, we think there are some goals there that if the committee did want to move this forward, they're attainable and we'd be happy to work with you to fine-tune the wording of the bill to make sure it's workable.

I guess working backwards in numerical order, then, the next section 6 is local control and in principle, the AOGCC has no opposition to providing for a measure of local control. We would want to make sure that there is coordination with the AOGCC. Our primary area of jurisdiction is subsurface regulatory activity and also, we would want to make sure that the local control did not result in waste of a resource.

CHAIR OGAN asked Mr. Norman if he was a geologist by profession and to touch on the water protection issues.

MR. NORMAN replied that he has worked in the industry, but the other AOGCC commissioner, Dan Seamount, is a geologist and Mr. Bob Crandall is one of AOGCC's senior geologists.

CHAIR OGAN asked, “To your knowledge, has any toxic fluid been used for hydraulic fracturing for coalbed methane in Alaska?”

MR. BOB CRANDALL, AOGCC Petroleum Geologist, replied as far as he knows toxic fluids haven’t been used for hydraulic fracturing.

> There has been a treatment to the well prior to fracturing called an acid wash where a relatively small volume of dilute hydrochloric acid is used to clear the perforations in the well prior to injecting the hydraulic fracturing fluid.

CHAIR OGAN asked if acid reacts to the formation by neutralizing it into CO2, salt and water.

MR. CRANDALL replied that’s true, but he doesn’t see that as a significant toxic component.

CHAIR OGAN asked if it worked something like baking soda neutralizing acid.

MR. CRANDALL replied basically that’s right.

CHAIR OGAN stated for the record that a libelous article was printed by a couple of local papers that talked about how an operator used hydrochloric acid gas in Texas wells to enhance production and it somehow leaked out and killed a lot of people. He thought the article’s author was mistakenly calling hydrogen sulphide (H2S) hydrochloric acid gas. He asked Mr. Crandall to clarify that.

MR. CRANDALL answered:

> The occurrence of H2S is in a Tyonek formation, which has been a target for coalbed methane in the Mat-Su Valley. It has only been encountered in undetectable levels in the wells that have been drilled so far. There is no history of H2S in the Mat-Su Valley based on previous drilling. In future drilling, there will be H2S detectors and that, of course, even though it hasn’t been observed in the past, will always be treated by us as a potential threat. I think you’re correct.
>
> As far as the reference in the article that you referred to as a gas, that’s something that I’m really

not aware of. Sometimes large concentrations of H2S is present in natural gas. That happens frequently, for instance, in the Canadian Rockies, and that's referred to typically in the industry as sour gas.

CHAIR OGAN interrupted to say there is some of that in Texas.

MR. CRANDALL agreed and added, "Acid gas, I think, is a misstatement by someone."

TAPE 04-30, SIDE B
4:30

CHAIR OGAN said the fear in some places is that diesel is used to "frac," but all the petroleum engineers he talked to say that diesel is commonly used for oil wells, because it has an oil base; it is rarely used, if ever, for coalbed methane. He asked what the likelihood was for other toxic fluids being used for fracturing.

MR. CRANDALL replied that petroleum-based frac fluids are not used in Alaska for coalbed methane. It is not commonly used in any coalbed methane operations.

In fact, there is a memorandum of understanding (MOU) between the two largest commercial well fracing companies in the EPA that they will not use hydrocarbon-based frac fluids in USDWs, which is the EPA term for water that has less than 10,000 parts per million total dissolved solids. There is this recognition by the industry that by and large, diesel-based frac fluids are inappropriate for coalbed methane.

CHAIR OGAN asked if the theory is that you can use it in water that's already polluted, but you can't use it in anything fresh.

MR. CRANDALL replied that the underground injection control is in the Safe Drinking Water Act. He thought the EPA established the total dissolved solids threshold at 10,000 parts per million because that represents the type of water that's good enough to be treated for human consumption.

CHAIR OGAN moved on to another issue.

One of the criticisms has been that there isn't specific statutory requirements to inject water. My

understanding is that, while it's not addressed specifically in the statutes, it is required to inject the water if you get a certain amount of dissolved solids and I don't know if that's 10,000 parts per million or what. So, there is a requirement to inject it unless you're getting drinking water quality and then you can get an NPDS permit to discharge on the surface along with DEC and Fish and Game and a few other things. Could you clarify what is required now if it's produced water.

MR. NORMAN stepped in and said:

It's generally exactly as you stated it, that if it is of drinking water quality, it can be disposed of on the surface. Otherwise, it's reinjected into wells and those wells, the State of Alaska has been given, and specifically this agency, the AOGCC, primacy for oversight over these labeled class 2 wells. The water is injected and those wells are very carefully monitored and it's the responsibility and, I believe, carried out very well, to insure that when water is reinjected, it absolutely will not pollute fresh water in any way.

CHAIR OGAN said another requirement is to reinject all liquids and wastes including ground-up rock from drilling the hole.

MR. NORMAN agreed.

CHAIR OGAN said if this requirement was drafted literally, it would require that the ground-up rock be reinjected and coalbed methane wells don't have annular rings [the pad area that remains after a well hole is drilled through it] like the deep-hole, high-pressure wells on the North Slope and Cook Inlet. He asked if it was technically possible to reinject ground-up rock into a well.

MR. CRANDALL answered:

There is a very large-scale slurry injection project up on the North Slope where exactly that happens – where old reserved beds are ground-up very small and, then, injected through the well into the subsurface.

CHAIR OGAN said a literal interpretation of that is, then, that a coalbed methane operation, no matter where it was located,

would have to get one of those wells on-line and grind up rock in a slurry and reinject it.

MR. CRANDALL responded that's how he reads this and that is not a practical requirement.

CHAIR OGAN asked what class well that would be.

MR. CRANDALL replied that is labeled a class 2 injection well. A class 1 is for hazardous sorts of waste.

CHAIR OGAN asked what a class 2 well costs to build.

MR. CRANDALL replied that it could be very expensive. It would depend on the stratography, the sequence of rocks in an area and a number of other things. His experience indicates having a large number of class 2 disposal wells wouldn't be practical.

CHAIR OGAN asked if the life of the well would be fairly short since the slurry would be pumped into it.

MR. CRANDALL replied, again, that would depend on the nature of the formations. "Wells on the Slope actually perform quite well."

CHAIR OGAN asked what other items were under the AOGCC purview.

MR. NORMAN briefed the committee that the commission sees local control as an attainable goal and encouraged:

> ... a close coordination with the AOGCC and other regulatory agencies so we don't bump into each other and we get into questions of conflicts with state law and we would also encourage that coordination and try to minimize, eliminate and prevent waste – that is the waste of a valuable resource. We think there are ways to do that and I think, on the subject of local control, I'll just leave it there and see if there are any questions.

CHAIR OGAN said the Mat-Su Borough is proposing an ordinance that would require well spacing no closer than 360 acres or one per section. What would happen if that passed and the commission determined that well spacing that far apart would create waste? Is that a local control override?

MR. NORMAN replied that could happen right now.

I'm assuming the 360 is actually intended to be 320. Half of a 640-acre section would be 320.... There is the potential for conflict. I think what needs to be clarified is our regulation of spacing and the professional staff here normally thinks in terms of subsurface spacing patterns.... It's a pretty fundamental distinction. Whereas, I think, probably the borough, and the proponents of the bill of rights, are more concerned with surface spacing and facilities. That's a first distinction that has to be kept in mind and sorted through in properly drafting any legislation. But it is possible that if the spacing were such depending upon the host reservoir, it could result in waste.

An operator would probably try to drill as efficiently as they could. The nature of the industry has been to have a smaller and smaller footprint and there have been magnificent strides in the area of directional drilling and production from lateral wells. So, there are an awful lot of technological innovations that right now even in a few years may give operators the ability to reach out. Coalbed methane is slightly different, but the area where we would see it might bump in – that's one potential area – is on the spacing of wells.

CHAIR OGAN remembered Jack Chenoweth's (Legislative Legal Services) testimony that state authority is already implied in the statutes and constitution to override local control in situations like this. He asked if directional drilling is feasible with coalbed methane operations.

MR. NORMAN replied that Mr. Chenoweth referred to the doctrine of preemption, which states if a superior government entity – in this case, the State of Alaska – has a body of law in place for a purpose for the benefit of all the citizens of the state, then a lesser (a more confined geographic area) governmental entity generally should not be allowed to interfere with that larger state purpose.

I think, probably, there would be a way to work with the borough to enact an ordinance to insure that waste would not take place.

> On directional drilling, of course, on conventional [vertical] wells in production there have been some truly mind-boggling innovations in that area. In so far as coalbed methane and directional drilling is concerned, my understanding...is that probably we will see those, but I don't think we have quite the directional drilling capability now in the area of coalbed methane that we see, for example, on the North Slope, where you can have these very small footprints that reach out or even in Cook Inlet or other areas where you're drilling for deeper oil or conventional gas.

MR. NORMAN asked Mr. Seamount, with his experience, if he wanted to comment on the ability for directional drilling with coalbed methane development.

MR. DAN SEAMOUNT, AOGCC Commissioner, added that incredible drilling patterns have been made from one mother bore in some areas of the country. But, the geology of the Mat-Su area has up to 24 different coal seams and he doubted that technology was ready for areas like that at this time. He elaborated that economic production has already happened from a conventional type well bore before technological experimentation has taken place. Actually, very economic producing wells have happened through drilling patterns that look like herring-bones and feathers.

MR. NORMAN concluded that the last section of the proposed bill of rights that would interface with the powers and duties of the commission is section 5, baseline studies.

> Right now, we don't think it's workable and some suggestions we would have is that rather than putting the obligation on the state to measure the baseline, that that obligation be placed upon an operator and that would be just a part of the development project.
>
> Secondly, we would think that that type of baseline information could be required prior to commencement of commercial production, because a lot of the wells drilled will not involve any type of commercial production. So, to avoid a lot of work that may not be useful at all, we would recommend that it be tied to commencement of commercial production and that the sampling of wells involve a radius of about a quarter mile around each producing well. There are different

ways to look at that, but if you think in terms of a quarter mile radius around a well, that's a huge volume of potential water under there and that generally is a distance that the AOGCC works with when we administer the Safe Drinking Water Act, for example.

The request in here for a monitoring program on methane seepage – we don't really think it's practical and that it would really yield a lot of useful information. That is, it tends to be somewhat sporadic and, if you try to draw scientific conclusions from some sort of a broad areawide sniffing of methane, it would not be useful and so, should this make its way in to law, we would recommend more that that focus be upon monitoring wells and sampling for methane and that is the most practical way to do this.

The proposal here in section 5 talks about a possibility of an operation causing contamination within a well and an allocation of the burden of proof. I don't know that we have an opinion on the burden of proof. I think you could argue that one either way. An operator probably would be in possession of the best information, but on the other hand, a shifting of the burden of proof like this is counter, generally, to what are considered general principles of due process of law. But in any event, it raises a question, then: would a property owner file presumably in the Superior Court and, if so, it does raise a specter of a number of possible filings. And we think right now that the AOGCC, because of our ongoing responsibilities to monitor from cradle to grave, if you will, every well drilled, that this agency would be in a position to take testimony from citizens. And, after all, that's our ultimate client – the citizens of the State of Alaska - and we could serve as a forum to receive such complaints, adjudicate them. Then, there would always be an appeal right that any private property owner would have into the court system. My thought is that that would be preferable to allowing these to just be thrown into the court system and then requiring individual property owners to engage their hydrologists and the company's. You might over a period of time get inconsistent results. So, that is just a suggestion if section 5 were to find its way in. I'll stop here, Mr.

Chairman, and we can answer questions on any of the points that we've touched on.

CHAIR OGAN said that section 5 requires a baseline water quality and quantity study on all surface and well waters that may be affected and asked if that means everything in the lease would be tested.

MR. NORMAN replied that he read the language to be even broader than that.

It's not necessarily confined to the lease. As a practical matter, this zone of influence - we're suggesting a quarter mile - may or may not equate with the lease.... It would make a lot more sense and be a lot more efficient if it were tied to a producing well. And once there was a producing well, prior to production, they would have to secure this baseline information and make that an operator responsibility as a condition to commencement of commercial production. I think we're set up to monitor that and keep an eye on it and if the operations are on state lands, certainly the State Division of Oil and Gas could likewise do so.

CHAIR OGAN said that Article 8, Section 9, of the State Constitution currently has a property owner's bill of rights providing protection for surface owners in terms of trespass for people who are unduly deprived of use of their property and damages. He asked what would happen if a coalbed methane well operation affects someone's well water in a negative way.

MR. NORMAN replied:

We think the likelihood of that occurring is not great in the experience in other areas that we're familiar with. That is an understandable bit of anxiousness on the part of property owners, so I don't mean to disparage that, but the reality of it we don't think is high. But, if an operation did interfere with the well and damaged that well, then, I think as an agency, we would have the grid, the pattern of all the wells and we could make a determination.

There are a couple of ways in which a well could theoretically be interfered with. One of them would be that there might be some methane that might find its

way into the water. Again, we don't think that would occur given the constraints and requirements imposed on drilling. But if it did, it's something that we are certainly able to watch and to make a fair determination on. I think we could do it in an efficient way and a fair way to Alaskans.

The second part of that would be - let's say - that a well flowed at a certain rate, so many gallons per minute or per hour, and at some point, it went dry, in an extreme example. Then the question is did that occur because of the operations being conducted by the coalbed methane operator or did the well simply go dry and it might have gone dry anyway. Again, I think we could monitor that and if it was necessary, we could provide a forum; we have all the tools to issue the subpoenas, to adjudicate fairly and to enter an order and then there is always the possibility of judicial oversight on that. To conclude on that, a property owner potentially would have a claim for damages if somehow their well were interfered with in that unlikely event.

CHAIR OGAN pointed out that the presumption for water quality in the property owners' bill of rights is:

Within five years after coalbed methane operations on or around his or her property, there shall be a presumption that such operations cause diminishment or pollution and the coalbed methane operator shall carry the burden of proving otherwise.

CHAIR OGAN called that a refutable presumption.

I personally know people whose wells have gone dry after earthquakes and personally we don't have too much of a problem with drought in Alaska, although I know my well behavior has changed over the years. My well doesn't produce as much water as it used to.

He thanked the AOGCC members for providing their time and expertise to the committee. Next he took testimony from the Mat-Su Valley.

MR. ROBERT HALL, Vice President, Houston Chamber of Commerce, said Houston has four test wells recently drilled by Evergreen

Resources. In the late 1990s, Alaska's first CBM well was drilled there by an Australian company.

> Overall the experience has been positive. It's a new industry and we recognize the need for additional refined state regulations. We'd like to offer some comments in three areas. One has to do with the private surface owner property rights – and they vary from state to state. Alaska doesn't have the strongest surface property owner rights statute. We recognize that what you do on private property might have some impact on the North Slope and in other ways it's a complicated issue. A couple of ideas – one is that if the property owner and the subsurface lessee cannot reach a surface owner agreement, the DNR should only in essence institute one for them and allow them to post a bond when there's no reasonable alternative....
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> Second, if they're allowed on the property, they should be required to minimize the impact and only impact the property as much as is reasonably necessary.
>
> Third, some reasonable compensation for loss of use and enjoyment. An example is in some states that if you have a farm and you lose – up here they grow carrots and potatoes – and if you lose 30% of your acreage, a couple of acres of farmland to the CBM thing, you should receive some reasonable compensation.

MR. HALL said there are a lot of misconceptions about what local governments can and cannot do and that needs to be clarified. He said the original purpose of the CBM program in Alaska was to jump-start the industry, which it has done in the populated areas of Southcentral, but it still needs to happen in the rural areas. He suggested offering local governments the option to opt in or opt out of the program or tailoring it to different regions.

CHAIR OGAN said he was considering bifurcating the issue by geology and population to minimize conflicts in highly populated areas. Energy needs in rural Alaska need to be addressed; there's just no economy at all in the central area. He admitted there were some unintended consequences to the original program and he didn't want to react to those without first thinking the

situation through. He then asked Ms. Kristin Ryan to comment on the areas her department would have purview over.

MS. KRISTIN RYAN, Director, Division of Environmental Health, Department of Environmental Conservation (DEC), replied that she hadn't seen the conceptual amendment, but she could comment based on testimony she has heard today. She corrected that the federal legislation that allows the protection of surface water is not the Safe Drinking Water Act; it's the Clean Water Act, which determines what levels of certain contaminates can be discharged to the surface water or into the ground that would get into the ground water.

> That determination is based on the use of the water. Actually, drinking water usage is not the most stringent standard – actually, fish habitat is. So, depending on what the water body that the discharge could potentially get into is what determines the standard that has to be met and they vary significantly based on the use of the water body.

CHAIR OGAN noted that someone stated produced water is required to be reinjected and was assuming that it wouldn't be drinking water or fish water quality.

MS. RYAN responded:

> The standards could not be broken if the discharge was to occur, but what could happen – they wouldn't have to reinject it necessarily. They could treat the water so that it met the minimum standards. The problem is that tends to be more expensive than reinjecting it. So, they choose to reinject, usually.

CHAIR OGAN asked if most of the produced water in Cook Inlet is discharged into the Inlet after it's treated.

MS. RYAN replied that she wasn't familiar with those leases, but was focused on the CBM development.

> The concept that the rocks and solid material that would come up in the exploratory phase as the well developed – similar to our clean water standards. We would not allow that material to be discharged onto the surface if it violated any of the state's standards for that kind of material. Sometimes, that rock or debris can be low enough in any contaminants

> or heavy metals that they may want to use it for beneficial use – for example, building a road or work on the pad. So, DEC is not supportive of a blanket standard that would eliminate that function. The standard for protection should be what's used to determine the disposal method of a material.

CHAIR OGAN asked if she supported testing rocks coming out of the wells.

MS. RYAN replied:

> We just propose that there be that flexibility, that based on the level of contamination determines the usage of the material. The landfill out in Mat-Su Valley has been approved to be a recipient of hazardous waste. So, they may prefer to be the recipient of the material because they can use it as fill in their landfill, for example.

CHAIR OGAN remembered that the landfill received federal funding to install a liner and recalled a press release justifying it for coalbed methane waste disposal.

MS. RYAN said that is correct.

MR. LARRY OSTROVSKY, Assistant Attorney General, offered to address any particulars the committee would like.

CHAIR OGAN asked if he agreed with Mr. Chenoweth that the Property Owners' Bill Of Rights was going to run into constitutional and statehood compact issues.

MR. OSTROVSKY said he agreed with him.

> Giving surface owners a veto over the use of subsurface mineral estate could be construed as a partial alienation to surface owners of the state's ownership of the mineral estate and I think it could be contrary to the requirements of (6)(i) of the Statehood Act that requires the state to retain mineral ownership of lands granted to the state – subject to leasing the mineral rights for development. I think it does raise a significant issue.

CHAIR OGAN said he is looking for a way to help his constituents and asked if a constitutional amendment giving the state the

ability to dispose of the subsurface was feasible and if the state could sell subsurface estate to a surface owner who was worried about development or a surface owner who wanted to develop the subsurface.

MR. OSTROVSKY replied that such an amendment might be possible if (6)(i) of the Statehood Act was amended first.

SENATOR FRED DYSON asked what issues are involved if the state, as owner of the subsurface, declines to make available for lease an area that promises to be rich in subsurface resources.

MR. OSTROVSKY replied:

> Not every acre of state subsurface is open for lease. I mean, the state does areawide plans and designates certain areas as critical habitat areas, parks, etc....

SENATOR DYSON asked if issues are involved if a landowner takes action against the State of Alaska to force DNR to make available some of their subsurface treasure arguing that not putting it on the market denies him a beneficial use.

MR. OSTROVSKY replied:

> I believe the Legislature could, under the constitution. Really, the Legislature manages the disposition of the state resources.

SENATOR DYSON asked if citizens have no recourse except through the Legislature to bring an action to get their resources developed if DNR does not make them available.

MR. OSTROVSKY replied that it wouldn't be a viable lawsuit. "I think ultimately it's a legislative determination that in some cases its decisions are delegated to a state agency...."

SENATOR DYSON asked if citizens could bring an action if they believe the DNR has opened land that is inappropriate for critical habitat or that there is a detrimental effect to the surface owners.

MR. OSTROVSKY replied that issue could have standing. People challenge DNR decisions all the time regarding oil and gas lease sales, mining permits, etc.

TAPE 04-32, SIDE A

SENATOR DYSON asked if someone could bring action if he thought DNR inappropriately listed an areawide lease sale.

MR. OSTROVSKY replied that he did not think DNR inappropriately listed property. Theoretically a person could take that position, but he would have little chance of prevailing.

CHAIR OGAN asked if the state enters into a lease with a producer and the state buys back that lease, "Is that a violation of the contract?"

MR. OSTROVSKY replied that would be condemnation or use of eminent domain.

> Right now, I don't think DNR has legislative authority to use eminent domain power. That's something they would have to be given by statute and, of course, we haven't had a situation quite like this in Alaska, but normally, eminent domain, the state would buy property back at fair market value – what a willing seller would sell for and what a willing buyer would buy it for. And, of course, there would likely be disputes over what that value is.

CHAIR OGAN asked if some of the disputes could be loss of potential income from resources.

MR. OSTROVSKY replied that would depend to some degree on the work that was done on a particular lease. For example, if the company had obtained a lease and done exploratory work that showed there was value to that lease, using eminent domain, a willing buyer would probably pay a premium for that lease. On the other hand, it could be that the work has shown there was no value in the lease. It could really go in either direction.

CHAIR OGAN assumed that value would be pretty subjective if no exploration had been done. He thanked everyone for their patience and testimony on this issue. There being no further business to come before the committee, he adjourned the meeting at 5:22 p.m.
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