HB
815

COMMITTEE REPORT

SENATE

FURTHER: None

5/10/78

Date: 5/30/78

Mr. President:

The Committee on RESOURCES has had CSHB 815 (Fin) oil and gas conservation

under consideration and (a majority of the committee) (the committee reports it back as follows)

( ) recommends it do pass ( ) recommends it do not pass

( ) recommends it do pass with attached amendment(s)

(X) recommends it be replaced with CS for CS HB 815

and ______ ( ) new title ( ) same title

( ) AND attaches a Letter of Intent ( ) New Fiscal Note

(X) reports it back without recommendation

( ) and recommends it be referred to the ______ Committee

MEMBERS SIGNING DO PASS: OTHER RECOMMENDATIONS:

[signatures] DO PASS WITH ... AMENDMENT

AGO 085864

R. Poland

Chairman

S 60 (rev. 6/77)

Testimony Before
Alaska Senate Resources Committee
on
CSHB 815

My name is Thomas H. Krueger. I am an attorney for Exxon Company, U.S.A. and am located in Los Angeles. I appreciate the opportunity to appear before this Committee and present testimony for Exxon.

CSHB 815 operates to amend various chapters in Titles 31 (Oil and Gas) and 38 (Public Lands) of the Alaska statutes. Much of the Bill deals with unitization and unitized operation of oil and gas pools. Exxon is and has long been a strong supporter of unitized operations designed to enhance recovery, promote resource conservation, prevent waste, eliminate unnecessary operations and safeguard correlative rights of the parties involved. Thus, we are interested greatly in presenting our views on this Bill to the Committee.

Several portions of CSHB 815 appear to be proper and acceptable revisions of the State's oil and gas law, and we will not take up your time discussing these provisions. There are, however, three areas in the Bill that are of considerable concern to us.

Section 7 of the Bill, which amends the unitization provisions of A.S. 31.05.110(b), deletes one of the findings of the Department of Natural Resources ("DNR") essential to a DNR order of unitization. Under current law, the DNR must find, among other things, that unitization and the adoption of a unitized method(s) are "for the common good and will result in the general advantage of the owners of the oil and gas rights within the pool or portion of it directly affected." The Bill proposes to eliminate the finding of resultant general advantage to the affected property owners, leaving only the finding that unitization and adoption of one or more unitized methods of operations are for the "common good". Significantly, "common good" is not defined.

In Exxon's view, unitization should result to the general advantage of the owners of the oil and gas rights, including the royalty owners directly affected, as well as to the "common good". If it does not, it should not be ordered by the State. The current provision is fair and should not be changed.

Under the Bill, the DNR could make the requisite finding that unitization, etc. are for the "common good" in a context where it would not result in

the general advantage of the owners of the oil and gas rights directly affected thereby. If DNR-ordered unitization were approved in such a context, serious constitutional questions could arise as applied to property owners who, in fact, were not benefited by and did not approve unitization, etc. of their interests. These questions could take the form of deprivations of liberty and property without due process of law.

(2) Underlifting and overlifting

Section 10 of the Bill, which would apply to all units created after June 30, 1978, allows underlifting and overlifting of unit production only when it does not create waste; and, regardless of waste, underlifting and overlifting may be permitted by the commissioner for temporary periods when there are extraordinary disruptions to the owner's production disposal systems. Further, this section restricts the recovery of underlifted oil to a daily rate not to exceed 10 percent of a working or royalty interest owner's share of daily production at the time of underlift recovery.

Exxon strongly supports the prevention of waste, but does not consider the first portion of this section to be necessary. Waste is already prohibited by the statutes and the Department of Natural Resources is fully empowered to carry out the purposes of AS 31.05.

As to the part of this section which limits the rate of recovery of underlifted oil, we see no need for the restriction that is imposed or for the state to intervene in this area. The details of underlifting and overlifting are matters that can best be worked out satisfactorily by the oil and gas resource owners. By imposing this restriction, which produces no apparent benefit to anyone, unforeseen future problems may be created.

3. Sections 11 and 16 of the Bill would remove the requirement that state-ordered unitization be acceptable to 62.5% of the lessees and 62.5% of the royalty owners within the unit area (with certain exclusions). Under these provisions, the State, without working or royalty owner concurrence, could mandate unitization, including the details of unit participation, unitized management of further development and operation of the unit area, cost and expense apportionment, financing, etc.

(3)

Exxon believes that unitized operations are best accomplished through voluntary agreement between the persons whose property interests would be affected. In this way, interested persons are consulted and mutual agreement reached in a manner satisfactory to those concerned. This promotes harmony and contributes to the achievement of

unit operations. Under present law, compulsory unitization must be acceptable to working and royalty interest owners of at least 62.5 percent of the unit area, thereby insuring comfortable majority support and satisfaction. This provides some degree of assurance both that only meritorious unit projects are considered and approved and that the State will not be forced to act on applications for unitization which are lacking in merit and reasonable support.

Exxon Company, U.S.A. is presently participating in more than 370 reservoir-wide and field-wide unitization projects throughout the United States, all of which have been formed voluntarily or with majority consent of both royalty and working interests. We have found that when a project has merit, its benefit will be recognized by the resource holders and it will be implemented. In our experience, we have seen no need for government-dictated unitization; however, we do support the concept of state-ordered unitization where majority, but not total, agreement is reached for unitization amongst the participants.

We question that enactment of Sections 11 and 16 would serve to benefit all interest owners in a pool since the sections eliminate the necessity for working and royalty interest approval for State unitization as provided under current Alaska law. There is no

need for this legislation since (a) to Exxon's knowledge, no unitization project which was needed in the State of Alaska has failed to materialize as a result of failure to reach sufficient agreement among the persons affected, and (b) present conservation laws contain sufficient authority for unitization and conservation of oil and gas resources. If the Bill is enacted, the only way that a dissatisfied person could object to State-ordered unitization affecting him would be to resort to litigation.

Finally, if the State were to undertake unitization by unilateral action, it would be put in the position of addressing many complex technical, operating, financial and legal issues normally handled by the operators. This would require a large expansion of its staff, and could delay the unitization process. Many of these issues that the State would set itself up to resolve would impact only upon the working interest owners and not upon the State.

In summary, Exxon believes that there is no need to change existing law on this subject and supports retention of voluntary and majority consent unitization as presently provided for in the statutes.

In summary, Exxon opposes that portion of Section 7 of the Bill which removes the required finding that unitization and adoption of unitized method(s) will result in the general advantage of the owners of the oil and gas rights. Present law on this subject is reasonable and fair and should not be changed. In addition, Exxon is opposed to Section 10 of the Bill since the provisions it adds concerning underlift and overlift appear to be unnecessary. The restriction on the rate of recovery of underlifted oil could cause problems in the future. Finally, we are strongly opposed to Sections 11 and 16 which allow for unitization by unilateral state action.

STATE OF ALASKA
THE LEGISLATURE

POUCH Y - STATE CAPITOL
JUNEAU ALASKA 99811
907-465-3800

LEGISLATIVE AFFAIRS AGENCY

March 1, 1978

MEMORANDUM

SUBJECT: HB 815 (W.O. #12/R)

TO: The Honorable Al Osterback, Chairman
House Resources Committee

FROM: Richard G. Haggar
Research Analyst

This memorandum is in response to your request that we prepare a summary analysis of HB 815, relating to oil and gas conservation.

Section 1

Amends AS 31.05.030(d) and allows the Department of Natural Resources to require oil or gas well operators to measure and monitor pressures within oil or gas pools. Such pressure monitoring would provide an additional source of information for state conservation authorities in terms of seeing that state conservation objectives are met.

Section 2

Amends AS 31.05.030(e) and allows the Department of Natural Resources to regulate the production rate of oil and gas from a well or property for purposes of meeting state conservation objectives.

Section 3

Amends AS 31.05.030(a)(1) and allows the Department of Natural Resources to require that oil or gas well operators make, and file the results of, flow test information from wells drilled for oil or natural gas. Such flow test information would be covered under the confidentiality provisions of AS 31.05.035(c).

Section 4

Amends AS 31.05.035(c) and provides that only operators of oil and natural gas wells may require confidential treatment of data submitted to the Department of Natural Resources in relation to state conservation requirements. The current statute does not specify which parties may require confidential treatment of data.

Section 5

Amends AS 31.05.060 by adding a new subsection (b) which requires that any action by the Department of Natural Resources under AS 31.05 that has state-wide or general application will be performed in accordance with the Administrative Procedure Act (AS 44.62), except that any action by the Department under AS 31.05 with respect to a single well or field will be performed in accordance with regulations of the department designed to afford persons affected by the action notice and an opportunity to be heard.

Section 6

Amends AS 31.05.110(b) by removing the requirement that a unitization agreement, if promulgated, "...will result in the general advantage of the owners of the oil and gas rights within the pool or portion of it directly affected..."

Section 7

Amends AS 31.05.110(c) in the following manner:

1. Makes discretionary the Department of Natural Resources' authority to determine the size and area of operating units.

2. Revises the terms by which the department determines the area of an operating unit from "...the area of a pool or portion of it..." to "...the boundary of the area...".

3. Makes discretionary the department's authority to limit unitization agreements to single pools or portions of single pools.

4. Removes the requirement that unitization agreements can cover only those areas of a pool or pools which have been defined and determined to be productive of oil and gas by actual drilling operations.

Section 8

Amends AS 31.05.110(h) by deleting references to "one-eigth" landowner royalty shares. The amendatory language would take into account circumstances where the landowners royalty share was other than one-eighth (12.5%).

Section 9

Amends AS 31.05.110(i) by forbidding either underlifting or overlifting of an "aliquot" (a fraction) of unit production unless an emergency order for such under- or overlifting is approved by the department. "Emergency order" is not, however, defined either in HB 815 or the current statute.

Section 10

Amends AS 31.05.170(11) by defining the drilling of unnecessary wells to carry out the general conservation purposes of AS 31.05 as "waste".

Section 11

Amends AS 31.05.170(12) by clarifying the definition of a "cubic foot of natural gas" and by changing the pressure measurement base for defining a "cubic foot of natural gas" from 14.65 pounds per square inch absolute to 14.73 pounds per square inch absolute (conforming Alaska's law to both federal standards and those of the Interstate Oil Compact).

Section 12

Amends AS 38.05.180 relating to the leasing of public lands, by adding the requirement that no lease under section 180 may be issued without inclusion of the language of AS 31.05.110(h) (providing for the assessment of unitization costs) as part of the lease. Section 12 also provides that leases issued in violation of this requirement shall be construed as containing the language of AS 31.05.110(h).

Section 13

Amends AS 43.55.140(2) relating to Alaska's oil and gas severance tax, by changing the pressure measurement base for defining "one cubic foot of gas" from 14.65 pounds per square inch absolute to 14.73 pounds per square inch absolute (again, conforming Alaska's law to the federal and Interstate Oil Compact standard).

Section 14

Provides that the Act will take effect July 1, 1978.

324A S. Willoughby
Juneau, Alaska 99801

May 15, 1978

SENATOR ROLAND

Senator Chancy Croft
Alaska State Senate
Pouch V
Juneau, Alaska 99811

Dear Senator Croft:

As the sponsor of Senate Bill 503, relating to the establishment of an Oil and Gas Conservation Commission, you already know that the House has passed House Bills 815 and 830 on much the same subject.

There is, however, a small technical change which could be made to your bill or to the appropriate House bill, which change would have a potential benefit to the State of Alaska in excess of $135 million.

The details of the cost savings to the State are related in the accompanying letters to Representatives Chatterton and Malone and to Secretary Schlesinger.

Put simply, the suggested change would give the state the option of keeping its "excess" or "surplus" oil in the ground until markets can be found which have low transportation costs & consequent high royalty income levels--or until the Federal government can be persuaded to compensate Alaska for continued production on behalf of the East Coast even at low royalty rates for Alaska.

The change involves giving the Commission the right to set prorationing rates for "conservation or marketing purposes". (The underlined words need to be added to either the House bill or to your bill to make the Commission's rights explicit rather than implicit.)

The other change to reach this desirable end is in the definition section: the definition of "waste" should include "the production of oil or gas at a rate greater than economic market demand."

As the letter to Representative Buchholdt points out, "economic market demand" is purposely left vague to allow the Commission to decide whether to maximize production or revenue, whether or not to leave oil excess to West Coast demand in the ground or to produce oil to satisfy East Coast demand.

Since legislators are used to arguments from self-interest, I suggest 10% of the savings come to me; these small changes will in any case benefit Alaska--and the oil companies--greatly by reducing high

transportation costs on the "excess" oil. Or--and this may be ultimately the more likely possibility--the fact that Alaska has given itself this power may mean that the Federal government will either be willing to compensate Alaska for excess production on behalf of East Coast consumer states or will be willing to aid Alaska in realizing the Japanese barrel-for-barrel swap.

In short, this is a change which benefits Alaska: please do what is possible to add these suggested words.

Sincerely and cordially,

Dr. Joe Sonneman
Five Star Consulting and Research

P.S.: There is one oversight: as production is scheduled to rise to 2 million barrels a day, the actual potential cost to the State of Alaska from continuing production of the "excess" oil will be substantially more than $135 million over the three year period; the potential savings will also be more, therefore, if the change in SB503 or HB815 is effected.

cc: Senator Poland
Senator Sackett
Senate President Rader
Senator Ray
Senator Hohman
Senator Sumner
Senator Huber
Senator Rodey

Title 31 - Chapter 05 - The States Oil and Gas Conservation Act was adopted in 1955 by the Territorial Legislature. The Act is virtually the Interstate Oil Compact Commission's Model Act. No substantive changes have been made to the Act since adaption, 23 years ago. The Model Act was drafted primarily for the purpose of providing States with the authority to protect correlative rights of private mineral land owners and prohibit waste.

HB 815 except for Section 15 deals solely with amendments to the Oil and Gas Conservation Statute 31-05. The intent of the bill is to improve Statute for application to Alaska which is primarily a public lands state rather than a private lands state typified by the uplands of oil producing south 48 states.

HB 815 incorporates in addition to the sponsors proposals amendments to Statute requested by the Department of Natural Resources and amendments to Statute requested by the industry. Several sections of the bill address requirements for the Industry, additional data deemed necessary to insure Alaska protection of correlative rights and prevention of waste. Other sections address housekeeping amendments to facilitate better administration of the Act.

The most substantive change to existing statute is provided by Section 16 of the bill. This is a policy question.

Current law 31.05.110(d) in addition to permitting voluntary unitization of many oil and gas leases in to one cooperative reservoir management unit, provides the State with the authority to mandate unitization providing that 62.5% or more of the lessees approve and 62.5% or more of the lessors approve.

Section 16 of the bill repeals the proviso for 62.5% or more approval; thus providing the State with the power to mandate unitization of Oil and Gas leases when deemed necessary to protect correlative rights and prevent waste.

You may ask why this power is needed. Oil and Gas reservoirs almost always have a habit of occuring beneath leases having different owership interests. Unless the entire reservoir is managed as one unit "waste" as defined by Statute will generally occur and in fact waste as defined by Statute will most often be necessary to protect correlative rights. We have a show window example of such waste existing on State lands today. We need the statutory hammer to force unitization. After all, because of our severance tax law we have a vested interest in maximizing the ultimate recovery of oil and gas from all lands within the State regardless of ownership.

Of lesser significance are Sections 10 and 15 of the bill. Section 10 permits underlifting/overlifting of unit production only when it will not create waste excepting for temporary periods where the Commission finds extraordinary conditions have occurred.

Section 15 requires that all future oil and gas lease forms include the language set forth within the quotation marks. We would not be in the court today if such language had been adopted in earlier years.

AMENDMENT

OFFERED IN THE ~~HOUSE:~~ Senate Resources BY: Chatterton

TO: Senator Poland HOUSE BILL No. CSHB 815 (Finance)

SENATE BILL No. _____

PAGE: 7 and 9 LINE: Pg. 7 - Lines 20 & 23
Pg. 9 - Lines 3,4 & 6

Page 7, Line 20

(a) Delete - (the unit) immediately preceding the word Production.

(b) Add - or lease immediately following the word tract.

Page 7, Line 23

Add - or lease immediately following the word unit.

Page 9, Line 3 & 4

(a) Delete - (the unit) immediately preceding the word Production.

(b) Line 4 - Add - or lease immediately following the word tract.

Page 9, Line 6

Add - or lease immediately following the word unit.