



September 27, 2016

Alaska Oil and Gas Conservation Commission
333 West Seventh Avenue
Anchorage, AK 99501

RE: Proposed Changes to 20 AAC 25.022 through 20 AAC 25.990

Dear Commissioners:

Cook Inlet Region, Inc. (“CIRI”), an Alaska Native Corporation, appreciates the opportunity to provide comments on the proposed changes to the Alaska Oil and Gas Conservation Commission’s (“AOGCC” or “Commission”) regulations in Title 20, Chapter 25 of the Alaska Administrative Code.

I. Introduction

As a landowner in Cook Inlet and as an oil and gas lessor, CIRI is interested in ensuring AOGCC’s regulations provide clear and fair direction for parties interested in oil and gas development and that those regulations are consistent with the AOGCC’s statutory mandates to prevent waste, protect correlative rights, and enhance production. As such, the AOGCC’s intent to update and clarify its regulatory requirements, improve understanding, and streamline the implementation of its regulations is laudable. Although the AOGCC is proposing many changes, CIRI has comments only on the three regulations discussed below.

II. CIRI encourages AOGCC to reconsider and/or revise some of its proposed changes to the regulations.

- A. The AOGCC should not adopt the proposed changes to 20 AAC 25.055(a) that are contrary to the AOGCC’s statutory obligations in AS 31.05.100(a), do not sufficiently protect correlative rights and prevent waste, and create an undue administrative burden.

The proposed changes to 20 AAC 25.055 alter from mandatory to permissive the AOGCC’s obligation to establish drilling units, and delete the existing rules for creating drilling units and well spacing in the absence of an AOGCC order regarding the same. CIRI objects to this proposed change for three reasons.

First, the introductory sentence to 20 AAC 25.055(a) that changes the AOGCC’s obligation to establish drilling units from mandatory to permissive by removing “will, in its

discretion”¹ and replacing it with “may” suggests that the AOGCC need not establish drilling units to govern well spacing or prescribe other spacing patterns for pools. Such a result would be contrary to AS 31.05.100(a), which provides, in pertinent part, that “the commission shall, after a hearing, establish a drilling unit or units for each pool.” (Emphasis added). The proposed change also would contravene the language in 20 AAC 25.520, which provides that the AOGCC “will,” upon request or its own motion after the discovery of oil or gas in a field or pool, hold a hearing and “will” prescribe “rules to govern the proposed development and operation of the pool.”

Second, the proposed changes in 20 AAC 25.055(a)(3) and (4) that delete the existing rules establishing drilling units in the absence of an AOGCC order regarding the same should not be adopted² because they are contrary to AOGCC obligations under AS 31.05.100(a). Current rules set a governmental quarter section as the statewide drilling unit for oil wells and a governmental section for gas wells, which rules are clear and understandable for all stakeholders. The proposed regulations eliminate that clarity and do not address the drilling unit size if the AOGCC has not yet issued an order regarding that particular pool.³ The minimum property-line-spacing distances do not fill this regulatory gap because they do not establish drilling units. Adopting these changes would result in the AOGCC disregarding its statutory mandate in AS 31.05.100(a) to establish drilling rules for “each pool,” unless the AOGCC holds individual hearings for each well drilled after the discovery of oil or gas and sets individual pool rules.⁴ CIRI believes the requirement to hold an individual hearing for each discovered pool would strain the AOGCC’s resources, those of oil and gas companies seeking to develop a pool, affected landowners, and other stakeholders. The proposed regulation would require an AOGCC hearing be held for the first development well to be drilled in a pool, even if the well was the only one within the drilling unit that would otherwise have been established by the AOGCC’s statewide rules. Without the existing provisions which provide certainty and clarity, oil and gas companies and landowners would have to spend time and money to ensure that appropriate drilling unit sizes were established via the Commission’s hearing process, even in cases where the statewide rules would have led to the same result. The AOGCC should reconsider its

¹ It is CIRI’s understanding that the phrase “in its discretion” does not modify the verb “will” given the AOGCC’s enabling statutes, but instead reflects the AOGCC’s discretion in determining the appropriate drilling unit and spacing pattern.

² It is not clear whether the AOGCC intended to delete the statewide drilling and spacing unit provisions discussed here, as the substance of these changes were not reflected in the Commission’s first or second public notice related to the proposal.

³ To the extent the proposed changes to 20 AAC 25.556 are adopted, it appears that all of the AOGCC’s prior orders establishing drilling unit and spacing rules that are more than five years old as of the regulation’s effective date will have to be revisited.

⁴ CIRI assumes the existing regulation satisfies the AOGCC’s obligation under AS 31.05.100(a) if it was adopted after a hearing. *See also* AS 31.05.100, which provides that drilling units for each pool should be established “[f]or the prevention of waste, to protect and enforce the correlative rights of lessees in a pool, and to avoid the augmenting or accumulation of risks arising from the drilling of an excessive number of wells.”

proposal to eliminate the clear and useful rules setting drilling units in the absence of a commission order establishing specific pool rules.

Third, CIRI objects to the proposed changes in 20 AAC 25.055(a)(3) and (4) that delete the existing rules establishing statewide well spacing requirements, including the spacing distances between wells,⁵ as to adopt them would violate the AOGCC's statutory and policy duties to protect correlative rights, avoid waste, and ensure efficient recovery.⁶ It is well-established that "[a] typical oil and gas conservation statute consists of a series of provisions that seek to balance public interest and private rights. The most important of those provisions are well-spacing rules. ... [A]n important step toward controlling the problem[s of over-drilling and protection from drainage] is to require that wells be located far enough from boundary lines and from one another so that excessive drainage will not occur."⁷ The current regulation satisfies these obligations by establishing statewide spacing rules that rationally develop pools while allowing each landowner to extract his share of the oil or gas.⁸ If those statewide rules are eliminated, spacing rules will have to be established for each pool. Spacing rules are necessary not only to protect correlative rights, but also to maximize recovery.⁹ For the same reasons described above in relation to establishing individual drilling units, having to set spacing rules for each discovered pool creates an undue administrative burden on the AOGCC, oil and gas companies, landowners, and other stakeholders.¹⁰ CIRI encourages AOGCC to consider the

⁵ It is not clear if the Commission intended to delete this rule, since its proposed language regarding applications for exceptions retain the 1000 feet and 3000 feet references to the statewide well spacing rules.

⁶ AS 31.05.095 ("The waste of oil and gas in the state is prohibited"); AS 31.05.030(b) ("the commission shall investigate if waste exists or is imminent"); AS 31.05.030(d)(9) (the AOGCC may require plans for a pool "to prevent waste, ensure a greater ultimate recovery of oil and gas, and protect the correlative rights of persons owning interests in the tracts of land affected").

⁷ See Lowe, John S., *Oil and Gas Law in a Nutshell*, 6th Edition, 23 (2014) (emphasis added).

⁸ *Id.*

⁹ Lowe at 23. The short-term overproduction that comes from wells being drilled too close together is likely to result in lower borehole pressure leading to inefficient and lower ultimate recovery from the reservoir. Lower ultimate recovery is a form of waste. See Lowe at 20. "[R]ational development prevents waste because it maximizes ultimate recovery." Drainage is a product of the rule of capture and greed, resulting in too many wells drilled too closely together. Lowe at 23.

¹⁰ Alaska Statute 31.05.100(b) provides that each well shall be drilled "in accordance with the spacing pattern as the commission prescribes for the pool." Without the statewide spacing pattern that currently exists, the AOGCC will have to hold a hearing for the first development well drilled in each pool.

administrative inefficiency and burden created by the proposed revisions to 20 AAC 25.055 and instead reinstate the proposed deletions to 20 AAC 25.055(a)(3) and (4).

CIRI agrees that the AOGCC's proposed changes to 20 AAC 25.055(a)(1) and (2) for new and recompleted wells, when different owners or landowners¹¹ are on either side of the property line, should be adopted. The prior language allowed owners to begin drilling a well that could not be tested or produced without permission from the AOGCC. Addressing such issues, which directly impact correlative rights, before drilling rather than after it has been completed, is a sound decision. The AOGCC's proposed clarification that the rule is applicable if "any portion of the well" is within the specified area is a logical interpretation and provides the AOGCC with the best information to make decisions. It should be adopted, as should the AOGCC's proposed addition of having recompleted wells expressly subject to the same rule, as is proposed in (a)(3) and (a)(4). CIRI believes, however, that the language regarding recompleted wells should be moved to (a)(1) and (2), and the deleted language from (a)(3) and (a)(4) restored as discussed above.

- B. The proposed deletion of 20 AAC 25.055(b) and (c) is inconsistent with the AOGCC's statutory obligations to protect correlative rights.

The language of 20 AAC 25.055(b) protects correlative rights by precluding production from wells unless the interests of all persons owning the drilling rights and rights to share in the production have been pooled. This provision is a safeguard and ensures that oil and gas development companies are acting in a prudent and responsible manner by coming to an agreement with those parties who should share the proceeds of production before that production begins. While the provision may benefit from clarification, it cannot be deleted if the AOGCC is to fulfill its obligations to land and royalty owners. The importance of this provision was recently demonstrated, as it and other AOGCC precedent were the basis of the relief the AOGCC granted which stopped Buccaneer Alaska LLC's illegal drainage from CIRI and State of Alaska lands in the Kenai Loop unit. In its Order directing Buccaneer to escrow proceeds from Kenai Loop production pending the parties' agreement on allocation, the AOGCC noted, "in order to protect correlative rights a production allocation agreement must be established[.]"

Rather than delete subsection (b), CIRI suggests the Commission instead adopt the following modifications to 25.055(b). First rather than referring to the quarter section and section set forth in the statewide drilling unit provisions, these terms could be replaced by the term "drilling unit." That would clarify that the appropriate area is the proposed drilling unit, whether established in the statewide rules or in an AOGCC order. Second, in addition to a pooling agreement under AS 31.05.100, the acceptable agreements should be expanded to include a voluntary unit agreement with allocation provisions, an agreement under AS 31.05.110, an agreement specifying how production is to be allocated, or if the parties are unable to reach consensus, an agreement to escrow production proceeds subject to AOGCC approval. Similarly, subsection (c) should be reinstated and modified to require one of these forms of allocation

¹¹ An "owner" is the person holding the right to drill and produce from a pool; a "landowner" is the person who holds title to the subsurface estate of the affected tract. AS 31.05.170(7), (10).

agreements to be filed with the Commission before regular production begins. For these reasons, CIRC requests that the language in 20 AAC 25.055(b) and (c) either remain the same, or be modified as set forth above.

- C. The proposed additions to be codified at 20 AAC 25.055(b) should be adopted, with one change.

CIRC agrees that the proposed changes to the information that must be submitted to the AOGCC to receive an exception to the rules set forth in 20 AAC 25.055 protect correlative rights by adding clarity and ensuring that applicants properly notify all stakeholders. CIRC does believe that a subsection should be added to ensure all stakeholders within the applicable drilling unit are also notified of the application and given a copy of it. This addition will further protect correlative rights and ensure all impacted stakeholders have been properly notified.

- D. The additions to 20 AAC 25.110 that protect landowner rights when an operator proposes to suspend a well or seeks to renew a suspension approval should be adopted.

CIRC agrees that the AOGCC's proposed changes to 20 AAC 25.110 should be implemented. By requiring the operator to prove that its leases are valid and that it properly obtained drilling rights related to that land, the AOGCC is protecting correlative rights. These changes also give the AOGCC valuable information regarding the landowners who are directly impacted by the AOGCC's decision whether to suspend a well, renew a suspension, complete the well, or require the operator to plug and abandon the well. The requirements of landowner information for all portions of the well and notice to the AOGCC when the lease status changes, eliminate ambiguity and provide clear information for the AOGCC in its efforts to protect correlative rights. CIRC encourages AOGCC to adopt the proposed changes to 20 AAC 25.110.

- E. The AOGCC should consider modifying its proposed changes to 20 AAC 25.556 to reduce the administrative burden on the Commission, oil and gas companies, and other interested stakeholders.

The proposed changes to 20 AAC 25.556 would cause certain AOGCC orders to expire after a particular time has passed or after a designated event. With respect to the provisions automatically terminating certain orders five years after they were issued, the regulation is not, on its face, limited to orders issued after the regulation's effective date. If the AOGCC intends for the regulation to apply to all of its conservation, enhanced recovery, area, storage, and disposal orders, this would cause all such orders that were issued more than five years before the regulation's effective date to automatically expire. This result would cause a tremendous administrative burden for the AOGCC and also would create uncertainty for operators, landowners, and other stakeholders. Indeed, the expiration of all prior orders that were more than five years old as of the regulation's effective date would cause many operators to be in immediate violation of AOGCC's existing statutes and regulations, as well as the proposed new regulation at 20 AAC 25.556(d) that applications for reauthorization of orders "must be timely filed" to allow a hearing under 20 AAC 25.540, if necessary, and an AOGCC decision before the

order expires.”¹² If this was not the AOGCC’s intent, it should consider revising the proposed regulation to clarify that 20 AAC 25.556(b) and (c) will only apply to orders adopted after the regulation’s effective date, provide a reasonable period of time after the effective date to allow operators to comply, or reauthorize all such orders the day the regulation becomes effective. Regardless of the AOGCC’s intent, it appears that the automatic expiration of a conservation, enhanced recovery, area, storage, and disposal order five years after the order is issued will create an unnecessary administrative burden for the AOGCC, oil and gas companies and other stakeholders.

As an alternative to the five year rule, and in addition to the proposed rule requiring review when the operator changes, CIRC respectfully suggests that the AOGCC consider re-evaluating orders when a unit contracts, expands or terminates, or when production terminates. This would allow the Commission to evaluate whether changes to prior orders are necessary and also terminate any outdated orders that should no longer be in effect. This would also diminish the risk that a conservation order impacting correlative rights or otherwise restricting an operator’s actions might be allowed to expire rather than be renewed since, as drafted, the operator is the only person who can file such an application.¹³

Thank you for the opportunity to comment. If you have any questions or I can provide additional information, please contact me at eschutt@ciri.com or 907-274-8638.

Sincerely,

COOK INLET REGION, INC.



Ethan G. Schutt
Senior Vice President, Land and Energy Development

¹² See proposed 20 AAC 25.556(d).

¹³ The AOGCC may also do so on its own motion, but no other person is authorized to do so. Thus, the AOGCC may want to consider allowing applications for reauthorization to be filed by parties other than the operator.