

STATE OF MONTANA
DEPARTMENT OF NATURAL RESOURCES AND CONSERVATION
MINUTES OF THE
BOARD OF OIL AND GAS CONSERVATION MEETING AND PUBLIC HEARING
December 14 & 15, 2016

CALL TO ORDER

The regular business meeting of the Montana Board of Oil and Gas Conservation was called to order by Chairman Linda Nelson at 2:00 p.m., Wednesday, December 14, 2016, at its office at 2535 St. Johns Avenue in Billings, Montana. Board members present were Chairman Linda Nelson, Steven Durrett, Ronald S. Efta, Paul Gatzemeier, Peggy Ames-Nerud, Wayne Smith, and Corey Welter. Staff present was John Gizicki, Jim Halvorson, George Hudak, Ben Jones, Jennifer Rath, and Rob Stutz.

APPROVAL OF MINUTES

A motion was made by Mr. Gatzemeier, seconded by Mr. Durrett, and unanimously passed, to approve the minutes of the October 26, 2016, business meeting.

PUBLIC COMMENT ON AGENDA AND NON-AGENDA ITEMS

Susann Beug, member of Northern Plains Resource Council and Carbon County Resource Council, thanked the Board for their efforts in putting together the drilling notification rule. This rule defends Montana's constitutional rights to a clean environment. The Board has the authority to protect the environment with rulemaking. Ms. Beug stated the Board has the expertise and knowledge, compared to the Legislature, to adopt this rule. Ms. Beug urged the Board to adopt the rule today.

Northern Plains was live streaming the drilling notification proceedings to their online viewers.

Lana Sangmeister from Nye, Montana, urged the Board to vote for the drilling notification rule, for the rule is within the Board's jurisdiction. Otherwise, the rule will be back at the Legislature.

Charles Sangmeister from Nye, Montana, is concerned about property rights and other things that will spoil communities if the drilling notification rule is not adopted. The Board understands the rule and should adopt the rule. Mr. Sangmeister did not want this issue back at the Legislature.

James Hawkins, president of Robert Hawkins, Inc. (Hawkins), and Judd Jensen, attorney, appeared on behalf of Hawkins. Hawkins and Montana Oil Field Acquisitions I, LLC (MOFA) have submitted signed change of operator forms for Hawkins to take over 31 MOFA wells. This transfer of wells is due to a legal agreement. The wells are located in Pondera, Teton, and Toole Counties, Montana.

In June 2016, MOFA was brought to the Board for spill violations. MOFA did not achieve compliance within the agreed 45 days and a daily fine of \$250 was instated until compliance was achieved for all three wells. MOFA has not achieved compliance. As of today, the total fine amounts to \$34,000. MOFA is now out of compliance with production reporting and must submit delinquent production reports.

Mr. Hawkins requested that MOFA's \$34,000 fine not be transferred to Hawkins.

MOFA is responsible to pay the \$34,000 fine. If MOFA does not pay the fine, the Board could pursue legal action.

Mr. Jensen stated Hawkins would clean up the wells and resume production reporting. He asked for Board approval on the change of operator requests even though there are outstanding compliance issues.

Mr. Halvorson made the recommendation to allow staff to process the change of operator forms, stop the \$250 daily fine (as of 12/14/16), and schedule MOFA for show cause, if any it has, why additional penalties should not be assessed for failure to pay the \$34,000 fine.

Motion: Mr. Welter made the motion to approve the recommendations made by staff. Mr. Efta seconded and the motion passed unanimously.

Mr. Alan Olson, Executive Director of Montana Petroleum Association, opposed the adoption of the rule. He stated the rule is outside the Board's authority to notice owners of occupied structures. To resolve the authority issue, the upcoming legislative session will have drilling notification legislation sponsored by Tom Richmond.

Tom Richmond, Senator for Montana Senate District 28 and former Board of Oil and Gas Administrator, plans to carry the drilling notification bill, LC0421.01, and Mr. Duane Ankney will introduce the bill. The bill draft is attached as Exhibit 1. This bill specifies notification to owners of occupied dwellings within 660' of a wellbore surface location.

Shawna Bonini is concerned about the wellbore definition and would like it clarified.

Julie Holzer of Red Lodge encouraged the Board to take action and vote for the drilling notification. The Board has authorization and jurisdiction.

PROPOSED ADOPTION OF NEW RULE I PERTAINING TO NOTIFICATION OF APPLICATION FOR PERMIT TO DRILL

The Board discussed the drilling notification. Attached, as Exhibit 2, is the draft notice of adoption.

Ms. Ames-Nerud wanted to take action on the rule today and modify the rule to include the wellbore clarification.

Mr. Halvorson noted the wellbore clarification would require a new draft of the rule and public comment on that draft.

Mr. Stutz discussed the statutes that give the Board the authority to adopt a rule and the statutes that give the Board the authority to implement a rule. If the Legislature approves the drilling notification bill, that statute would supersede the Board's rule.

Ms. Ames-Nerud wanted to adopt the drilling notification in case the Legislature does not pass the bill.

Mr. Jones reviewed the statistics pertaining to the draft rule. Over the last six years, there were 1,520 drilling permits issued; of those permits, only 79 were within ¼ mile of a house. Of those instances, 44 of the homes owners also owned the land surface where the well was located and already received notice a well would be drilled. That leaves only 35 cases that would be affected by a new drilling notification rule, or only 2.3% of permits during that six year period.

Mr. Efta wanted to review North Dakota and Wyoming drilling notification rules.

Mr. Jones stated that Wyoming has a drilling notification to owners of occupied dwellings within 1,000 ft of the proposed well and North Dakota is 1,320 ft. These states do not have a protest period where the protestor can come before the Board.

Mr. Stutz clarified Mr. Welter's concern that any future requests to increase the notification distance is at the Board's discretion, but any change to the rule would require rulemaking.

Mr. Smith supported the drilling notification, but he was concerned that adopting the rule prior to the Legislature is to prove a point.

Mr. Gatzemeier opposed a setback rule but supported the notification rule. This rule will help the people affected by drilling. He wanted to adopt the rule today.

Mr. Durrett supported the concept, but is not in favor of the rule as it is currently drafted. He wanted this issue deferred to the Legislature.

Mr. Welter agreed with Mr. Durrett. Should the Legislature not pass the drilling notification bill, the Board will still have time to pass the rule.

Chairman Nelson supported the rule, for the Legislature may not pass the drilling notification bill. Chairman Nelson did not believe it is the owner's responsibility to monitor the legal ads for drilling activity. It is the owner's right to know.

Motion: Ms. Ames-Nerud made the motion to adopt the drilling notification. Mr. Gatzemeier seconded and the motion passed. The motion passed with four members voting yes and three members voting no. The members voting yes were Ms. Ames-Nerud, Mr. Efta, Mr. Gatzemeier, and Chairman Nelson. The members voting no were Mr. Welter, Mr. Durrett, and Mr. Smith.

COALRIDGE DISPOSAL & PETROLEUM, INC.

Robert Spoklie appeared at the October 26, 2016, business meeting to address his concern about the Spoklie 1-24 well located on his property in the SESW of Section 1, T34N, R57E, Sheridan County, Montana. At that meeting, Mr. Spoklie stated Coalridge Disposal & Petroleum, Inc. (Coalridge) did not have the oil and gas lease for the well and requested the Board to direct Coalridge to plug and abandon the well and reclaim the well site.

Board staff followed up with this issue and found out Mr. Spoklie has a restraining order against Coalridge. Mr. Spoklie did not respond to the Board's letter regarding the restraining order against Coalridge, attached as Exhibit 3.

Mr. Halvorson requested permission to disregard Mr. Spoklie's request since the court order prohibited Coalridge from plugging the Spoklie 1-24 well.

Motion: Mr. Smith made the motion to approve the recommendation made by staff. Mr. Durrett seconded and the motion passed unanimously.

Mr. Welter requested staff conduct an inventory of the wellsite.

LONGEVITY & SERVICE AWARDS

Chairman Nelson presented certificates and a longevity pin or gift card to the following employees for their years of service to the state:

John Gizicki, 5 years
Jim Halvorson, 25 years
Kris Goll, 35 years

FINANCIAL REPORT

Ms. Rath discussed the financial statement, attached as Exhibit 4.

Mr. Halvorson provided the Board a privilege and license tax update, attached as Exhibit 5. The Governor's upcoming budget for the biennium used the wrong tax rate of 0.09% instead of the correct, recently updated rate of 0.30%. With the incorrect tax rate, the Board projected a negative balance at the end of FY2019. The correct tax rate and the oil and gas revenue forecast included in the budget predict a positive balance in the special revenue account at the end of FY2019.

Mr. Halvorson noted that there is a new proposal to remove \$600,000 from the special revenue account for a Bureau of Mines project. This expenditure, along with continued funding of the sage grouse program, will impact the budget and delay any planned reduction in the privilege and license tax.

A reserve balance of \$1.5 – 2 million would help prevent the Board from projecting a negative balance in the future. The Board recommended that staff draft a letter to the Legislature requesting a reserve balance.

BOND SUMMARY & INCIDENT REPORT

Mr. Halvorson presented the bond report and the incident report, attached as Exhibits 6 and 7.

DOCKET SUMMARY

Mr. Halvorson presented the docket summary, attached as Exhibit 8.

The Augusta Exploration, LLC (Augusta) docket will be continued. Prior to proceeding with bond forfeiture, the federal receiver needs to confirm that Augusta has no remaining assets to plug and abandon the well. No confirmation has been received.

GAS FLARING EXCEPTIONS

Mr. Jones did not have any flaring exception requests at this time. However, Whiting Oil and Gas Corporation (Whiting) had wells flaring over the 100 MCFG per day limit without an exception. According to the policy, Whiting was assessed its second \$250 delinquent flaring penalty.

Due to a possible pipeline disruption, a few operators flared over 100 MCFG only for the month of

October.

Staff monitors gas flaring and wants operators to be more responsive to flaring, especially once economic conditions improve.

PLUGGING AND RECLAMATION PROGRAM AND UPDATE

Mr. Halvorson reviewed Mr. Popp's plugging project summary and plugging cost spreadsheet, attached as Exhibit 9. The plugging and reclamation program has plugged or reclaimed three wells with a cost that exceeded \$300,000.

The next candidate well to be plugged is the Beery 22-24 well, located in McCone County, formerly operated by Native American Energy Group (Native American). The issue with this well is that equipment remains on the wellsite. With no existing tax liens, the Board cannot move the equipment.

Mr. Stutz is looking into the legality of putting a lien on Native American and taking over the equipment. The Board gave Mr. Stutz permission to investigate potential solutions for this and other related matters.

STAFF REPORTS

Staff did not have any significant developments to report to the Board.

OTHER BUSINESS

No other business was discussed.

EXEMPT STAFF PERFORMANCE EVALUATIONS

Exempt staff performance evaluations were done in a closed session meeting.

PUBLIC HEARING

The Board reconvened on Thursday, December 15, 2016, at 8:00 a.m. at the Board's hearing room at its office at 2535 St. Johns Avenue in Billings, Montana, to hear the matters docketed for public hearing. As a result of the discussion, testimony, technical data, and other evidence placed before the Board, the following action was taken in each matter.

Docket No. 57-2016 – A motion was made by Mr. Efta, seconded by Mr. Gatzemeier and passed, to approve the application of Kraken Oil & Gas LLC as set forth in Board Order 50-2016. Mr. Welter recused himself and took no part in this matter.

Docket No. 58-2016 – The application of Azure Sky was continued to the February 2017 hearing.

Docket No. 46-2016 – Board staff placed this application on the Default Docket for approval without hearing if no protests or requests for hearing were received by 9:00 a.m. on the day of the hearing. None were received. The application of Legacy Reserves Operating LP was approved as set forth in Board Order 51-2016.

Docket No. 59-2016 – A motion was made by Mr. Gatzemeier, seconded by Ms. Ames-Nerud and unanimously passed, to assess Mountain Pacific General Inc. a \$1,000 fine for not appearing at the December 15, 2016, public hearing. Mountain Pacific General Inc. was ordered to immediately increase its plugging and reclamation bond to \$250,000 and pay the \$1,000 penalty for failure to appear at the December hearing. Mountain Pacific General Inc. is to appear at the February 2, 2017, public hearing. This is set forth in Board Order 52-2016

Docket No. 60-2016 – A motion was made by Ms. Ames-Nerud, seconded by Mr. Gatzemeier and unanimously passed, to assess Seymour, James G. a \$1,000 fine for failure to appear at the December 15, 2016, public hearing. Seymour, James G. is to appear at the February 2, 2017, public hearing and show-cause, if any it has, why additional penalties should not be assessed for failure to pay the penalty assessed for delinquent reporting and to appear at the December 15, 2016, public hearing. This is set forth in Board Order 53-2016.

Docket No. 61-2016 – A motion was made by Ms. Ames-Nerud, seconded by Mr. Gatzemeier and unanimously passed, to assess Seymour, James and Lorraine a \$1,000 fine for failure to appear at the December 15, 2016, public hearing. Seymour, James and Lorraine is to appear at the February 2, 2017, public hearing and show-cause, if any it has, why additional penalties should not be assessed for failure to pay the penalty assessed for delinquent reporting and to appear at the December 15, 2016, public hearing. This is set forth in Board Order 54-2016.

Docket No. 62-2016 – A motion was made by Mr. Gatzemeier, seconded by Mr. Efta and unanimously passed, to forfeit Stratex Oil & Gas, Inc. plugging and reclamation bond. This is set forth in Board Order 55-2016.

Docket No. 63-2016 – A motion was made by Mr. Durrett, seconded by Mr. Welter and unanimously passed, to assess McMinn Operating Company a \$1,000 fine for failure to appear at the December 15, 2016, public hearing and to forfeit McMinn Operating Company plugging and reclamation.

A second motion was made by Ms. Ames-Nerud, seconded by Mr. Efta and unanimously passed, to remove the \$1,000 fine, since it was previously assessed. This is set forth in Board Order 56-2016.

Docket No. 97-2015 – No Board action took place in the August Exploration, LLC docket.

Docket No. 48-2016 – A motion was made by Mr. Gatzemeier, seconded by Mr. Welter and unanimously passed, to continue Docket 48-2016, Shadwell Resources Group, LLC, until the April 6, 2017, public hearing. Shadwell Resources Group, LLC was fined \$2,000 for failure to plug the Ft. Gilbert 3 SWD located in the SW¹/₄NE¹/₄ of Section 32, T24N-R59E, Richland County, Montana, prior to the October 27, 2016, public hearing. Shadwell Resources Group, LLC needs to plug the Ft. Gilbert 3 SWD prior to the April 6, 2017, public hearing. This is set forth in Board Order 57-2016.

Docket No. 49-2016 – A motion was made by Mr. Durrett, seconded by Mr. Gatzemeier and unanimously passed, to continue Docket 49-2016, Storm Cat Energy (USA) Operating Corporation, until the February 2, 2017, public hearing. This is set forth in Board Order 58-2016.

NEXT MEETINGS

The next business meeting of the Board will be Wednesday, February 1, 2017, at 2:00 p.m. at the Board's hearing room at its office at 2535 St. Johns Avenue in Billings, Montana. The next regular public hearing will be Thursday, February 2, 2017, beginning at 8:00 a.m. at the Board's hearing room at its office at the 2535 St. Johns Avenue in Billings, Montana. The filing deadline for the February 2, 2017, public hearing is January 5, 2017.

BOARD OF OIL AND GAS CONSERVATION OF THE STATE OF MONTANA

Linda Nelson, Chairman
Steven Durrett, Board Member
Ronald S. Efta, Board Member
Paul Gatzemeier, Board Member
Peggy Ames-Nerud, Board Member
Corey Welter, Board Member
Wayne Smith, Board Member

ATTEST:

Jennifer Rath, Program Specialist