

STATE OF MONTANA
DEPARTMENT OF NATURAL RESOURCES AND CONSERVATION
MINUTES OF THE
BOARD OF OIL AND GAS CONSERVATION MEETING AND PUBLIC HEARING
February 10 & 11, 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 1:00 p.m., Wednesday, February 10, 2016, at its office at 2535 St. Johns Avenue in Billings, Montana. Board members present were Chairman Linda Nelson, Steven Durrett, Ronald S. Efta, John Evans, Paul Gatzemeier, Peggy Ames-Nerud, and Wayne Smith. Staff present was John Gizicki, Jim Halvorson, George Hudak, Ben Jones, Jennifer Rath, Erin Ricci, and Rob Stutz.

APPROVAL OF MINUTES

A motion was made by Mr. Gatzemeier, seconded by Mr. Efta and unanimously passed, to approve the minutes of the December 9, 2015, business meeting.

SAGE GROUSE PROGRAM OVERVIEW

Carolyn Sime, program manager, presented a slideshow on sage grouse. Attached as Exhibit 1 are handouts from the presentation.

Ms. Sime reviewed the governor's strategy for sage grouse that included a map of sage grouse affected by the order. The sage grouse map is based on a lek's location, which is a known breeding area that can extend up to four miles from breeding ground to nest. The sage grouse core area makes up about 75% of the sage grouse population.

The goal of the order is to minimize habitat disturbances. There will be a marketplace habit exchange/conservation bank where credits will be earned with habitat conservation and debits created with habitat disturbances. An operator will also be able to purchase credits.

If an operator has an upcoming project in sage grouse habitat, the operator needs to visit the sage grouse website <https://sagegrouse.mt.gov> and provide information on the activity, location, and agency the operator is working with. The sage grouse team will review the information and send a letter to the operator of any conditions that will be required of the permitted activity. Permitted activity is activity that requires a permit from the state or federal agency. This does not include maintenance activity. The sage grouse team is reviewing discretionary maintenance and talking with Wyoming's program staff to see what might be sent in on a sundry notice that increases surface disturbance.

Mr. Alan Olson, Executive Director of Montana Petroleum Association, expressed concern that day-to-day work on a well will require a sundry notice and that a sundry notice will be interpreted as a permit. Additionally, he is worried about the length of time it will take to get activity approval from the sage grouse team.

SURVEY OF NATIVE PROPPANT RESOURCES FINAL REPORT

The Board of Oil and Gas Conservation funded a three-year survey of Montana natural sands that have

the potential use as proppant applicable to hydraulic fracturing of oil and gas wells. Montana Tech (Tech) conducted the survey and Mr. John Getty, Tech instructor, Ms. Alicia Kastelitz and Mr. Jonathan Rice, Tech students, presented the slideshow of the survey. Attached, as Exhibit 2, is the final report.

There were 348 samples collected from 10 formations. The targeted formations were of high-energy marine deposits and marginal marine sand dune. The most promising formation was the Tyler Formation. Many sands are possible for proppant, but it is unknown if the formations are big enough for mining. More research would be required. The mine around Dillion that mines proppant sand from the Quadrant Formation has not been too active because it is a low strength material.

This survey has generated interest in proppant sources and other states are conducting similar research.

The Bureau of Mines and Geology will maintain the database of samples. The database website is <http://data.mbg.mtech.edu/proppant/Data.asp>.

PUBLIC COMMENT

Mr. Dennis Trudell, member of the Northeast Montana Land and Mineral Owners Association, wanted to know when an oil company declares bankruptcy, what happens to the mineral owner. In addition, what happens to a mineral owner when the mineral owner stops receiving payments from an operator and the well is still producing.

The Board does not have authority in these matters, but an operator is required by statute to pay a mineral owner interest on its delinquent royalty checks. It was recommended for concerned royalty owners to talk with an attorney.

Mr. Trudell asked Mr. Stutz if a mineral owner is protected in a bankruptcy case. Mr. Stutz was unsure.

Mr. Durrett commented that bankruptcy creditors try to protect the operator's assets, because the lease is what holds value to the creditors. If there is not a lease payment, it is grounds for cancelling a lease.

Alan Olson, the executive director of Montana Petroleum Association, introduced himself to the Board.

Becky Gray thanked the Board for the previous two presentations, as both were informative.

CUSTOM CARBON PROCESSING, INC. REQUEST FOR REHEARING OF DOCKET 160-2015

The Board denied the rehearing request of Docket 160-2015, due to Custom Carbon Processing, Inc.'s failure to appear.

DRILLING NOTIFICATION DRAFT RULE PROPOSAL

Mr. Jones read the drilling notification draft rule that was based off of the subcommittee's recommendation to amend the permit process and require notification to owners of occupied residences within a ¼ mile of the proposed drilling location. Attached, as Exhibit 3, is the draft.

The word 'occupied structure' generated many issues with the Board. Mr. Stutz clarified it could be interpreted as a seasonal or a permanent resident, but it was kept broad. The Board can revise this draft.

Mr. Durrett thought the Board needed to address how rental property owners need to notify its tenants of a possible well.

Another issue was if email should be included in the rule. The Board has an email address to receive comment. However, if the interested party provides an email address, there is no proof the email response was read. Certified mail maybe the better way, because you have a signed return receipt.

It was suggested that the draft be updated to say 'lived in once per year.' Chairman Nelson requested the draft be revised to reflect this. Board member comments can be emailed back to Mr. Halvorson. The Board will review the revised draft at the next meeting.

FINANCIAL REPORT

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

Mr. Halvorson gave an update of the privilege and license tax, attached as Exhibit 5. The timeline indicates the Board needs to consider immediately a rate increase of the privilege and license, due to the Legislature's expenditures/transfers of \$1.56 million to non-board related duties.

In order for the rate to be effective by October 1, 2016, rulemaking needs to start prior to April 1, 2016. Mr. Halvorson recommended a telephone conference to approve Mr. Halvorson as the authority to begin rule making by April 1, 2016.

If the Board plans to raise the rate to the max, cities and counties will no longer receive a share of revenue.

Mr. Efta was in support of the rate increase.

Mr. Stutz noted the drafted rule has to be at the Secretary of State's office by the next filing deadline, February 22, 2016.

Motion: Mr. Efta made the motion to increase the privilege and license tax rate to the maximum allowable rate. Mr. Smith seconded and the motion passed unanimously.

There will be a special meeting on February 17, 2016 at 9:00 for the proposed notice of amendment to the privilege and license tax, 36.22.1242. This meeting is open to the public.

BOND SUMMARY & INCIDENT REPORT

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

DOCKET SUMMARY

Due to the lack of dockets, no docket summary was presented.

GAS FLARING EXCEPTIONS

Mr. Jones discussed the gas flaring report, attached as Exhibit 8.

There are twenty-three wells flaring in excess of 100 mcf/day. Of these twenty-three wells, there are nineteen flaring exception requests at this time. One exception involves an operator who is unable to obtain a pipeline right-of-way agreement with the surface owner and the rest of the exceptions are due to pipeline/gas plant capacity issues.

Mr. Jones recommended a six-month flaring exception for the nineteen wells.

Motion: Mr. Smith made the motion to approve the recommendations. Mr. Gatzemeier seconded and the motion passed unanimously.

STAFF REPORTS

George Hudak

The annual UIC injection fee of \$200 was due January 1, 2016. Due to Bensun Energy, LLC (Bensun) recent bond increase due to non-compliance with Board rules, Mr. Hudak noted Bensun was one of the operators who have not paid the annual injection fee.

Rob Stutz

Mr. Stutz gave a brief litigation update. The Anne Ostby case is dormant. The Omimex case is close to settling and the Board is not required to participate in the settlement. The Hekkel settlement agreement fell apart, but both parties agree that the issued board order is enforceable and that the Board does not have to be a part of the settlement. The Malsam case and the process the Board followed is similar to the case Mr. Stutz handed out, attached as Exhibit 9. A scheduling conference is coming up. CCRC appealed the district court decision related to the ECA well to the Montana Supreme Court. A response from the Board is due before the next meeting. Lastly, The Board has not received permission from the receiver in the Augusta Exploration federal court case to forfeit Augusta's bond.

The Board met in a closed executive session to discuss litigation strategy after the public hearing on February 11, 2016.

Jim Halvorson

Mr. Halvorson brought up Custom Carbon Processing, Inc. (Custom) and the fine the Board assessed at \$250/day starting July 1, 2015 that has accumulated to over \$50,000. Since Custom's bond was forfeited, Custom no longer exists. One option would be to take action in district court to recover the fine owed. The board directed that staff investigate other remedies that could be applied in situations similar to that of Custom Carbon Processing.

Mr. Halvorson recommended delaying the bonding discussion.

There is one vacant position we are currently taking applications online.

Attached as Exhibit 10 is Mr. Dave Popp's plugging project summary on the Kopp #1 well and upcoming inspector training for field inspectors.

OTHER BUSINESS

No other business was discussed.

PUBLIC HEARING

The Board reconvened on Thursday, February 11, 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. 1-2016 – A motion was made by Mr. Efta, seconded by Ms. Ames Nerud and unanimously passed, to forfeit Miocene Oil Company plugging and reclamation bond. This is set forth in Board Order 1-2016.

Docket No. 2-2016 – A motion was made by Mr. Gatzemeier, seconded by Mr. Efta and unanimously passed, to forfeit Kelly Oil and Gas plugging and reclamation bonds. This is set forth in Board Order 2-2016.

Docket No. 3-2016 – A motion was made by Mr. Durrett, seconded by Mr. Evans and unanimously passed, to have Stealth Energy USA, Inc. appear at the April 7, 2016, public hearing and show-cause, if any it has, why it should not provide a plan and timeline for the plugging and abandonment of its wells. This is set forth in Board Order 3-2016.

NEXT MEETING

The next business meeting of the Board will be Wednesday, April 6, 2016, 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, April 7, 2016, 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 April 7, 2016, public hearing is March 3, 2016.

BOARD OF OIL AND GAS CONSERVATION OF THE STATE OF MONTANA

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

ATTEST:

Jennifer Rath, Program Specialist