



Energy and Telecommunications Interim Committee

60th Montana Legislature

SENATE MEMBERS

GREG LIND--Vice Chair
JERRY BLACK
VERDELL JACKSON
DON RYAN

HOUSE MEMBERS

HARRY KLOCK--Chair
DUANE ANKNEY
ROBYN DRISCOLL
BRADY WISEMAN

COMMITTEE STAFF

SONJA NOWAKOWSKI, Lead Staff
TODD EVERTS, Staff Attorney
DAWN FIELD, Secretary

MINUTES

September 4, 2008

Room 172, State Capitol
Helena, MT

Please note: These minutes provide abbreviated information about committee discussion, public testimony, action taken, and other activities. The minutes are accompanied by an audio recording. For each action listed, the minutes indicate the approximate amount of time in hours, minutes, and seconds that has elapsed since the start of the meeting. This time may be used to locate the activity on the audio recording.

An electronic copy of these minutes and the audio recording may be accessed from the Legislative Branch home page at <http://leg.mt.gov>. On the left-side column of the home page, select *Committees*, then *Interim*, and then the appropriate committee.

To view the minutes, locate the meeting date and click on minutes. To hear the audio recording, click on the Real Player icon. Note: You must have Real Player to listen to the audio recording.

COMMITTEE MEMBERS PRESENT

REP. HARRY KLOCK, Chair
SEN. GREG LIND, Vice Chair
SEN. JERRY BLACK
SEN. VERDELL JACKSON
SEN. DON RYAN
REP. DUANE ANKNEY
REP. ROBYN DRISCOLL
REP. BRADY WISEMAN

STAFF PRESENT

SONJA NOWAKOWSKI, Lead Staff
TODD EVERTS, Staff Attorney
DAWN FIELD, Secretary

AGENDA & VISITORS' LIST

Agenda, Attachment #1.
Visitors' list, Attachment #2.

COMMITTEE ACTION

The Energy and Telecommunications Interim Committee:

- approved the May 1 & 2, 2008, meeting minutes, as written;

- did not approve LC4003 - study resolution for additional study of carbon sequestration; and
- approved LC4001 - eliminate the USB termination date;.
- approved the revised carbon sequestration report; and
- approved the revised public power report.

CALL TO ORDER AND ROLL CALL

00:00:02 REP. KLOCK called the meeting to order at 9:00 a.m. The Secretary noted the roll, SEN. BLACK, SEN. LIND, and SEN. RYAN were excused (Attachment #3).

PUBLIC POWER STUDY

00:01:25 **Sonja Nowakowski, Research Analyst, Legislative Services Division (LSD)**, reviewed the revisions made to the public power draft report (EXHIBIT #1), as requested by Committee members at the July 16, 2008, meeting.

Public Comment

00:03:45 No public comment was given.

Committee discussion and executive action

00:03:52 REP. WISEMAN thanked the ETIC members for agreeing to investigate public power in Montana. He said the work done produced good information that will be a good resource for future work. REP. WISEMAN **moved** to accept the report, as revised. The **motion passed** on a unanimous voice vote.

CARBON SEQUESTRATION STUDY

00:04:50 Ms. Nowakowski reviewed changes made to the draft carbon sequestration report (EXHIBIT #2), as requested by Committee members at the July 16, 2008, meeting. She also reviewed the accompanying bill draft, LC4003 (EXHIBIT #3).

Public Comment

00:11:11 No public comment was given.

Committee discussion and executive action

00:11:24 REP. ANKNEY **moved** to accept the revised draft report. The **motion passed** on a unanimous voice vote.

00:11:59 Ms. Nowakowski discussed LC4003 (EXHIBIT #3) and said that the ETIC must approve the draft in order to move it on to the 2009 Legislature for consideration.

Public Comment

00:12:24 No public comment was given on LC4003 (EXHIBIT #3).

Committee discussion

00:13:33 The ETIC members held a brief discussion about the intended purpose of the bill draft. A **motion was made to approve** LC4003 for introduction into the 2009 Legislature. The **motion failed** on a 5-1 roll call vote, with REP. DRISCOLL voting yes and SEN. BLACK (Klock proxy), SEN. JACKSON, REP. ANKNEY, REP. WISEMAN, and REP. KLOCK voting no (Attachment #4).

ADMINISTRATIVE MATTERS

Approval of May 1 & 2, 2008, Meeting Minutes

00:16:52 REP. DRISCOLL **moved to approve** the May 1 and 2, 2008, meeting minutes, as written. The **motion passed** on a unanimous voice vote.

Budget Review

00:17:32 Ms. Nowakowski said that the ETIC will have approximately \$3100 as an ending balance after paying for the final meeting.

Interim Wrap Up, Staff Evaluation

00:18:38 REP. WISEMAN said that, in his opinion, the ETIC dealt with extremely complicated subjects and that a great deal of research was done, including informative speakers and panelists. He said he would like to commend Ms. Nowakowski for her exemplary work.

BREAK

OIL PRICING AND PRODUCTION PANEL

00:33:03 REP. WISEMAN thanked the panelists for agreeing to discuss with the ETIC what is happening in the oil and gas industry in Montana. He asked the panelists to answer specific questions:

1. how many rigs are active in Montana in gas and oil and what is the future trend for rig counts in Montana;
2. is it true that rigs are leaving the state and, if so, why;
3. what is the impact of North Dakota tax rates on Montana production;
4. what other factors should be considered in reviewing oil and gas pricing and production;
5. how many people are employed in oil and gas production and related services;
6. what is the relation between prices paid to producers and to the prices consumers are paying;
7. will prices in Montana decrease if there is a massive increase in production and if not, why;
8. is there a relationship between supply and demand and prices in Montana;
9. is there a relationship between different types of wells;
10. what are the specific impacts of oil and gas tax holidays on Montana revenues; and
11. what are specific production profiles for holiday periods versus given post-holiday periods.

● PRODUCTION

00:37:11 **Tom Richmond, Board of Oil and Gas Conservation Administrator (BOG)**, discussed Montana oil production and consumption using a PowerPoint presentation (EXHIBIT #4) which included production summaries for oil and gas. Mr. Richmond's presentation also included information on the Bakken Formation.

00:53:33 REP. WISEMAN asked several questions relating to oil production and if it is declining. Mr. Richmond said that overall, production has been declining since a production high in 2006.

- 01:03:44 REP. WISEMAN asked what "fracture" means in "fracture stimulation" drilling method. Mr. Richmond explained that it is a treatment and stimulation process to increase production.
- 01:10:06 REP. WISEMAN asked Mr. Richmond, as the chief regulator of the oil and gas industry in Montana, if production is moving to North Dakota and if so, why. Mr. Richmond said some parts of the industry naturally ebb and flow, so it would be difficult to say definitively. He said that North Dakota did pass a tax incentive for one year, which just expired, and that it likely did cause rigs to move in order to take advantage of the tax break. He said that shorter leases have also affected movement of rigs. Mr. Richmond noted that his presentation did not include information on enhanced oil recovery (EOR), which, he said, could have a significant impact on Montana oil production.
- 01:13:43 REP. WISEMAN said it appeared to him that price, rather than a tax holiday, has had a more significant impact on drilling in Montana. Mr. Richmond said it is difficult to distinguish the cause and effect of tax holidays but that tax breaks are a part of the decision making process for oil companies considering doing business in Montana. He said that even with the tax holiday in North Dakota, Montana's tax rate is competitive.
- 01:18:51 In response to several questions from REP. WISEMAN regarding how oil is actually taxed under Montana tax code, Mr. Richmond explained that the royalty owner does not get the tax break and pays a higher tax rate; and that the life of the well and the use of EOR also affect how the tax holiday is applied. REP. WISEMAN said that the policy question is, does that incentive mean anything? He said that Montana is giving up a huge amount of money and that he wants to know what Montana is getting in return. Mr. Richmond said that the BOG deals in volume, not value. He said that the concept of the tax holiday is that a well with a 20-year life span, for instance, will produce about 85% of its total production in the first 18 months, which falls under the tax holiday.
- 01:28:42 SEN. JACKSON asked if Montana tax code is competitive with Canada tax code. Mr. Richmond said that most of Canada's oil and gas resources are owned by the Canadian government, so it is an "apples and oranges" comparison and would be difficult to say.
- 01:29:52 SEN. JACKSON said that REP. WISEMAN brought up good point regarding the actual benefit of a tax holiday. He asked how more information could be gathered. Mr. Richmond said that all he could really say with certainty is that the tax holiday is a part of the decision making process of oil companies wanting to do business in Montana.
- BREAK**
01:37:10 **Beth Claude, Manager, State Government Affairs, Enbridge Pipelines Inc.,** discussed pipeline infrastructure and its role in oil economics (EXHIBIT #5). Ms. Claude also discussed a map of major crude oil pipelines serving the upper Midwest region of the United States (EXHIBIT #6).

01:57:51 REP. WISEMAN asked if most of the Bakken Formation oil is being shipped to Minnesota and not to Billings. Ms. Claude said that most of the Enbridge Bakken oil is shipped to Minnesota, but is dispersed multiple ways from there.

● **PRICING AND TAXATION**

02:00:39 **John Felmy, Chief Economist, American Petroleum Institute (API)**, gave an overview of pricing and taxation using a handout titled, "*The Truth About Oil and Gasoline: An API Primer*" (EXHIBIT #7). Mr. Felmy said that a great deal more information is available at the API's website: www.api.org.

02:18:27 REP. WISEMAN asked why prices remain high at the pump, considering the surge in Montana oil production. Mr. Felmy said that production is tied to world, not local markets; and that other factors, such as transportation costs and the quality of the crude also affect the price.

02:20:19 REP. WISEMAN asked what assurances Mr. Felmy could give regarding decreasing prices, if Montana continues to do its part in increasing production. Mr. Felmy said he could give no assurance that prices will go down because of the larger impact of world markets.

02:24:00 SEN. JACKSON asked how or if dividends are taxed. Mr. Felmy said he was not a tax expert but that he did not think oil companies are taxed on the dividends paid out.

02:25:25 **Terry Johnson, Principal Fiscal Analyst, Legislative Fiscal Division (LFD)**, discussed Montana severance tax, including oil and gas production taxes, tax rates, distribution, and collections (EXHIBIT #8).

02:38:15 REP. WISEMAN asked how local governments receive their share of tax revenues. Mr. Johnson said that he would get that information for REP. WISEMAN.

02:39:15 **Eric Dale, Associate Revenue Analyst, Office of Budget and Program Planning (OBPP), Governor's Office**, discussed price differentials using a table comparing West Texas Intermediate (WTI) and Montana prices (page 6 - EXHIBIT #9). He also distributed copies of an analysis of oil and natural gas tax production incentives for production in calendar years 2003 through 2007, and the effect on state funds (EXHIBIT #10). Mr. Dale said that production remained relatively constant until the first quarter of 2006. He said that it dropped back down a little in early 2007 but that the differential is growing again, probably due to increased production in North Dakota. He predicted that the differential would not shrink in the short term.

02:43:11 REP. WISEMAN asked Mr. Dale if the OBPP has done a study of the differential in production taxes between North Dakota, Canada, and Montana. Mr. Dale said that a comparison has been done with North Dakota only and that the analysis shows that North Dakota is similar to Montana.

- 02:44:17 SEN. JACKSON asked for Mr. Dale's perspective on the recent drop in oil prices. Mr. Dale said that it would be tough to pin point the exact reasons why prices have dropped but that he has heard that Mexico has locked in production prices and that factors in other regions may also have affected prices.
- 02:45:43 **Bob Decker, Executive Director, The Policy Institute**, discussed the Montana consumer's interests, mainly that of purchasing gas. He said that basically, Montana consumers are not "price makers", but "price takers" and that the focus needs to be on conservation and on decreasing energy consumption. He said that if the recommendations put forth in the Governor's report on climate control were put into effect, a savings of \$725 million dollars would be realized over the next 12 years.
- 02:51:59 Mr. Decker discussed his perspective of Montana's tax holiday for oil companies and said the data presented by Mr. Dale in EXHIBIT #10 raises the question of whether the incentives are working the way they were intended to.
- 03:02:02 Mr. Decker offered one critical observation about the new oil and gas tax holiday rates, saying that one needs to remember that the base production rate is not constant. He asked that the ETIC consider the fairness of the current tax structure and base production rate history and suggested that it may benefit the citizens of Montana to return to the old tax rates.
- 03:04:22 REP. WISEMAN asked, regarding the recommendations put forth by the Governor's report on climate change, if implementing the recommendations would require a public investment. Mr. Decker said he would get the information.

● **ECONOMIC IMPACT**

- 03:06:09 **Scott Rickard, Director, Center for Applied Economic Research, Montana State University - Billings**, used a PowerPoint presentation to discuss the economic impact of oil production in Montana (EXHIBIT #11). He said it is a major industry in Montana that extends well beyond the oil fields and refineries and that dollars are at risk when changes are made to the industry structure.
- 03:26:18 REP. WISEMAN asked for the actual number of workers engaged directly in production. Dr. Rickard said it would be very difficult to say because of the limited amount of income tax data available. He guessed, based on his information, that the total number would be about 3,500 workers.
- 03:28:36 **Pat Barkey, Director, Bureau of Business and Economic Research, University of Montana - Missoula**, presented a PowerPoint presentation (EXHIBIT #12) that provided information and data on the amount of money being spent on fuels by Montana families.

Public Comment

- 03:37:59 **Dave Galt, Executive Director, Montana Petroleum Association**, said that his association has production tax history information available and that he would provide it to the ETIC. Regarding previous comments made about the impact of tax incentives and capital decisions, Mr. Galt said it must be considered what the

scenario could have been without the incentives, which, he said, were definite factors in the investment decision. Mr. Galt also commented on domestic production and said that it is important to consider the impact on prices in the event no new drilling is allowed.

Lunch recess until 1:45 p.m.

PICK SLOAN PROJECT USE POWER

- 00:00:02 **Michael Ryan, Regional Director, Great Plains Region, Bureau of Reclamation (BOR)**, responded to three questions prepared by the ETIC (EXHIBIT #13) and asked by REP. ANKNEY:
1. We fully understand the current difficulties with the funding available to the Bureau for water development. Is the Bureau open to exploring ways that the State could design and construct with oversight by the Bureau as well as delivery of PMSBP project pumping power to the main and relift pumps? Mr. Ryan said it definitely could be taken under consideration but that any proposal would require congressional approval.
- 00:02:11 *It seem like the focus of the State of Montana is looking for ways to get off foreign oil and encourages economic development. We are wondering how we can work with the Bureau of Reclamation to develop a joint development package that would include renewable resources such as wind and bio-fuels plants that could be integrated into an irrigation program.* Mr. Ryan said he thought the Bureau would be interested in such projects because of the increasing demand for those types of energy, particularly for irrigation projects.
- 00:04:54 *In addition to wanting to get off of foreign oil there is also a big push to increase our food production in this country. It appears that we need to look at a different approach to the economics to move the irrigation program forward that was envisioned in the 1944 Flood Control Act. Do you have some thoughts on what we can do to improve this process.* Mr. Ryan said that currently, money available for investment by the federal government is very limited. He said he is working with several different states on economic development projects that will use a combination of federal, state, and local government funds, so opportunities do exist. He said that on a national level, conversations are taking place regarding green and renewable energy projects, so there is development potential there also.

Public Comment

00:07:49 No public comment was given.

RULE REVIEW

00:07:51 Mr. Everts reported that there were no proposed rules for review.

WHOLESALE ENERGY TRANSACTION TAX

00:08:11 Ms. Nowakowski explained the background and rationale for the wholesale energy transaction tax. She reported that following deregulation in 1997, legislation was passed that established the tax on transmission services providers. Ms. Nowakowski said that the revenue generated by the tax is deposited into the general fund and has varied from a low of \$2.9 million in 2002

to \$3.8 million in 2006. She explained how the tax is collected and from whom. She said she could provide additional information, if the Committee desired.

00:13:57 REP. WISEMAN asked if the tax is passed through to Montana rate payers. Ms. Nowakowski said NWE for example, does include the wholesale energy transaction tax amount in its rate base.

DISCUSSION OF 2009 COMMITTEE LEGISLATION

00:15:20 Mr. Everts reviewed LC4001 - an act to eliminate the Universal System Benefits termination date (EXHIBIT #14).

Public Comment

00:16:16 No public comment was given.

00:16:23 REP. WISEMAN **moved to approve** LC4001 for drafting. The **motion passed** on a unanimous voice vote.

MONTANA PUBLIC SERVICE COMMISSION UPDATE

00:17:45 **Greg Jergeson, Chairman, Public Service Commission (PSC)**, discussed potential legislation, saying that Commissioner Mood has asked the Commission to develop potential alternate legislation for deregulation of motor carriers.

Administrative Report

00:20:28 Chairman Jergeson provided an administrative update, saying that there are a number of big things going on:

- two hearings will be held in September regarding Colstrip 4, one that will decide whether to allow Northwestern Energy (NWE) to put Colstrip 4 into its rate base and another to investigate NWE's acquisition of ownership interest in Colstrip 4 as an investment in an unregulated enterprise;
- NWE has filed an application with the PSC to get preapproval of the Mill Creek gas-fired plant near Anaconda;
- several telecommunications hearings will be held in November to deal with Qwest issues and its proposal to move to an alternative form of regulation;
- the PSC has responsibility for rate regulation of private investor-owned water utilities and a hearing will be held on October 2, 2008, in Bozeman regarding *Utility Solutions*, a Gallatin Valley company;
- the PSC continues its ongoing efforts to encourage the public to adopt conservation measures, particularly regarding natural gas, due to the dramatic increases occurring in that market; and
- the PSC has taken steps to encourage the public to implement conservation measures now and to not wait until the cold hits, including engaging the media to help get the word out on programs that are available to help the public.

00:39:43 SEN. JACKSON asked about the statewide electrical supply, specifically if Chairman Jergeson was predicting brownouts. Chairman Jergeson said he did not think brownouts would occur because Montana is an exporter state and that overall, the utilities are in good shape.

00:43:49 SEN. JACKSON asked for additional information about NWE's proposal to construct a new gas-fired generator. He wondered about NWE moving from a cheaper source to a more expensive source of electricity. Chairman Jergeson said he could not comment about the Commission's decision that will be rendered. He said that the final outcome could affect two different electricity markets, depending on what NWE decides to do in response to the PSC's upcoming decision.

MONTANA'S ENERGY POLICY

00:48:25 SEN. JACKSON said that Montana has no long-term energy supply plan and that because he believes it is of great importance, he personally took the initiative to prepare a proposed energy policy, including a goals statement and a policy development process. He said he tried to structure his proposal to fit into what is already existing law and commented that it frightens him that America is so dependent on foreign oil. He reviewed his proposed energy policy statement (EXHIBIT #14).

01:11:59 REP. DRISCOLL, SEN. JACKSON, and REP. KLOCK discussed several recycling concerns, as addressed in SEN. JACKSON's report.

Public Comment

01:15:55 No public comment was given.

1:16:06 SEN. JACKSON asked that his report be made available to the next ETIC as a beginning of an energy supply plan for the state. REP. KLOCK agreed. Ms. Nowakowski said she will post the report on ETIC website and that she would also provide copies of it to the Department of Environmental Quality and the Environmental Quality Council. REP. KLOCK said it could be made available for the 2009 Legislature's Energy Committee also.

01:18:31 REP. KLOCK said that the ETIC had received outstanding information all through out the interim. SEN. JACKSON agreed, and said that the meeting presenters were of very high quality and that he enjoyed serving on the ETIC. REP. DRISCOLL said that she appreciated the cooperation among committee members and that they worked in a non partisan manner.

ADJOURNMENT

01:20:13 SEN. JACKSON moved to adjourn to Energy and Telecommunication Interim Committee. The meeting was adjourned.

CI0429 9174dfxa.