

RECOMMENDATIONS FOR 2000

**STUDY OF THE REGULATION
OF OIL AND GAS PRODUCTION**

**Report to the
Colorado General Assembly**

**Research Publication No. 463
November 1999**

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November 1999

To Members of the Sixty-second General Assembly:

Submitted herewith is the final report of the Study of the Regulation of Oil and Gas Production in Colorado. The interim committee was created pursuant to House Joint Resolution 99-1018.

At its meeting on November 15, 1999 the Legislative Council reviewed the report of this committee. A motion to forward this report and the bills therein for consideration in the 2000 session was approved.

Respectfully submitted,

/s/ Senator Ray Powers
Chairman
Legislative Council

RP/DB/cs

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STUDY OF THE REGULATION OF OIL AND GAS PRODUCTION

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EXECUTIVE SUMMARY

Committee Charge

The Interim Committee on the Regulation of Oil and Gas Production in Colorado was created pursuant to House Joint Resolution 99-1018 and charged with studying the regulation of oil and gas operations, mineral development, and surface impacts. Specifically, the committee considered: the regulation of the oil and gas industry and what may assist the Colorado Oil and Gas Conservation Commission (COGCC) in meeting its statutory mandates; the impacts of oil and gas activities on affected citizens and their property, health, safety, and welfare; the impacts of oil and gas activities on other natural resources; and, the economic benefits of mineral rights development. The committee also toured and held public hearings in locations that are affected by oil and gas operations.

Committee Activities

The committee held six meetings and visited four regions of the state that have experienced problems with increased residential development and oil and gas well development and production. For example, the committee visited subdivisions in La Plata and Garfield counties where gas wells are being drilled near homes because the COGCC approved denser well development, called infilling, in that area. In Trinidad, the committee visited gas wells that are depleting groundwater supplies for nearby homes. The committee also visited a housing development that is encroaching on oil and gas wells in Weld County. A public meeting was held on the first day of each tour and the committee visited oil and gas operations on the following day.

The committee received testimony from the COGCC regarding the regulation of oil and gas activities. The commission provided technical data and explained the technological and regulatory challenges associated with the development of mineral resources in each of the four areas toured by the committee. Surface landowners testified about the impacts to people and wildlife from oil and gas development including noise, truck traffic, and groundwater depletions. They also described the results of their efforts to have the commission address these impacts. Oil and gas operators described their efforts to minimize impacts to surface landowners from oil and gas operations. They also described the economic benefits of oil and gas production. County commissioners and other local government officials described their policies and programs to address impacts from oil and gas activity. Legal experts in oil and gas issues described mineral owner and surface landowner property rights. The United States Bureau of Land Management explained its regulation of impacts from oil and gas development on federal lands. The committee also received memoranda from legislative staff concerning property rights of land and mineral owners, the laws regulating the production of oil and gas, and the role of local governments in the regulation of oil and gas.

Committee Recommendations

As a result of committee discussion and deliberation, the committee recommends three bills for consideration in the 2000 legislative session.

Bill A — Oil & Gas Conservation Commission Personnel. This bill eliminates the requirement that commission membership be based on congressional districts and requires that one commission member be from west of the continental divide. The bill also allows each member to receive \$50 per diem for meetings or hearings.

Bill B — Colorado Oil and Gas Conservation Commissions Authority to Consider Wildlife. Bill B allows the commission to regulate oil and gas operations to prevent or mitigate impacts to wildlife to the extent necessary to protect public health, safety, and welfare. Such regulations must also consider cost effectiveness and technical feasibility

Bill C — Document to Surface Landowners. This bill requires oil and gas operators to provide information to a surface owner prior to commencement of operations. This information includes information about the COGCC's regulation pertaining to notification, the name and address of the well developer and persons who regulate oil and gas operations, the surface owners right to seek legal counsel, and other information that the COGCC determines would be useful for a surface owner.

STATUTORY AUTHORITY AND RESPONSIBILITIES

Pursuant to HJR 99-1018, the Interim Committee to Study the Regulation of Oil and Gas Production in Colorado was created to study the current regulatory framework of the oil and gas industry in light of the seemingly irreconcilable goals of surface landowners, oil and gas developers, state regulators, and local governments. The committee was composed of six members (three from the House and three from the Senate). The resolution allowed the committee to tour at least four areas of the state that are affected by oil and gas operations including areas that are experiencing significant amounts of development and in-filling of oil and gas wells. The committee was also allowed to consider but was not limited to the following issues:

- scope of existing regulation of the oil and gas industry and methods for assisting the Colorado Oil and Gas Conservation Commission to meet its statutory mandates;
- effectiveness of the rulemaking procedures of the Colorado Oil and Gas Conservation Commission;
- impacts that the production of oil and gas have on affected citizens and their property, health, safety, and welfare;
- relationships that the production of oil and gas have with Colorado's other natural resources; and
- mineral rights development and the attributable economic development benefits.

COMMITTEE ACTIVITIES

Economic Benefits from Oil and Gas Operations

Overview. The committee learned that Colorado is one of the nation's major oil and gas producing states and heard testimony about the importance of the oil and gas industry to state and local economies. In 1998, the oil and gas extraction industry employed 7,900 Coloradans who earned an average salary of \$58,000. The industry also contributed \$141 million in state and local tax revenue.

Oil and gas production in Colorado. Colorado is the seventh largest producer of gas and the tenth largest producer of crude oil in the United States. According to the COGCC, in 1998 the total production value for oil, gas, and carbon dioxide in Colorado was \$1.69 billion. During that year, Colorado produced 705 billion cubic feet of natural gas, up from 212 billion cubic feet in 1988, and 22 million barrels of oil, down from 33 million barrels in 1988. Currently, there are approximately 20,000 active oil and gas wells in the state. The committee heard testimony about the growing importance of cleaner burning natural gas to the nation, and the need for domestic oil production and the risk of the country's growing reliance on foreign sources of oil.

Tax revenue from oil and gas. According to the Division of Local Government, state and local tax revenues from oil and gas production in 1998 provided \$76.8 million in local property taxes, \$23.6 million in State Severance Tax, and \$19.6 million from the state's share of federal mineral royalties, for a total of \$141.4 million in tax revenue. State revenue from oil and gas supports the entire COGCC budget and portions of the State School Fund, the Colorado Water Conservation Board's Construction Fund, and the Department of Local Affairs. Between 1990 and 1998, the state provided approximately \$133 million to local governments to address the impacts of mineral development. Oil and gas operations also provide some counties with substantial portions of their total tax revenue. For example, in 1998 La Plata County obtained nearly 50 percent of its total property tax revenue from oil and gas operations. See Table A for a comparison of total property tax revenue and the oil and gas property taxes for Colorado's top producing counties.

Wages and employment benefits from the oil and gas industry. According to the Department of Labor and Employment, nearly 8,000 persons were directly employed in 1998 by the oil and gas extraction industry, down from over 12,000 in 1989. The average wage for oil and gas employees in 1998 was \$58,000 which is significantly above the statewide average of \$33,884. Other testimony described the importance of oil and gas wages to regional economies.

TABLE A - Oil and Gas Property Taxes vs. Total Property Taxes for Colorado's Top Producing Counties – 1999 Tax Revenues

County	General County Revenues			Public Schools		
	Oil and Gas Property Taxes	Total Property Taxes	Oil and Gas as Percent of Total	Oil and Gas Property Taxes	Total Property Taxes	Oil and Gas as Percent of Total
Adams	\$2,805,536	\$200,444,464	1.4%	\$1,815,700	\$129,277,191	1.4%
Baca	\$540,299	\$3,141,101	17.2%	\$317,931	\$1,829,274	17.4%
Cheyenne	\$2,339,089	\$3,695,642	63.3%	\$1,323,045	\$2,009,803	65.8%
Garfield	\$3,601,935	\$25,739,682	14.0%	\$2,430,643	\$18,164,597	13.4%
Kiowa	\$547,080	\$6,344,877	8.6%	\$258,958	\$1,248,152	20.7%
La Plata	\$17,690,026	\$36,554,666	48.4%	\$12,914,925	\$26,448,925	48.8%
Las Animas	\$1,224,468	\$6,749,228	18.1%	\$593,313	\$3,625,310	16.4%
Logan	\$380,351	\$10,610,518	3.6%	\$226,451	\$5,647,998	4.0%
Mesa	\$588,791	\$50,243,885	1.2%	\$368,019	\$31,360,312	1.2%
Moffat	\$2,668,395	\$19,234,769	13.9%	\$1,701,892	\$11,830,555	14.4%
Montezuma	\$3,872,760	\$12,261,849	31.6%	\$2,864,740	\$8,907,445	32.2%
Rio Blanco	\$4,320,237	\$7,090,257	60.9%	\$2,669,905	\$4,452,408	60.0%
Washington	\$1,151,094	\$5,213,273	22.1%	\$648,813	\$2,745,862	23.6%
Weld	\$22,119,199	\$114,152,234	19.4%	\$14,334,277	\$70,210,996	20.4%
Yuma	\$2,711,032	\$9,742,700	27.8%	\$1,866,877	\$6,284,118	29.7%

Note: General County Revenues include property taxes for the county, school districts, and cities.
Source: Legislative Council Staff compilation from the 1998 Annual Report of the Division of Property Taxation.

Impacts from Oil and Gas Operations

Scope of the issue. Colorado's growing population is moving into oil and gas producing regions. Often, these new residents are limited in their ability to prevent or control drilling on or near their land because they do not own the rights to the underlying minerals. Also, new production methods and technologies are enabling the development of new wells throughout the state. Consequently, more persons and wildlife are experiencing the impacts from oil and gas development and production. To better understand these impacts, the committee visited oil and gas operations including well drilling rigs, recently drilled well sites, reclaimed well sites, pipeline construction projects, gas compressor stations, and well production enhancement projects.

Severed mineral rights and oil and gas conflicts. Part of the conflict between surface landowners and oil and gas developers can be attributed to severed mineral rights. This means that surface land and the underlying minerals are owned or leased by different parties. Persons who do not own the minerals under their land are limited in their ability to prevent or control drilling on their land. According to Colorado law, the mineral owner has the right to use as much of the surface land as necessary to develop the mineral. Also, mineral owners are not required to compensate the surface owner for use of his or her land. While most mineral developers attempt to secure a surface use agreement with a landowner prior to drilling, a mineral developer may drill without obtaining the landowner's permission. Consequently, some landowners become quite concerned upon learning that a well will be drilled on their land and that the law limits their ability to prevent or control the drilling operation.

Prior to receiving notice that a well is planned for their property, some landowners do not know that the mineral rights have been severed from their land or that a mineral developer has the right to use surface lands to obtain the mineral. In an attempt to address this problem, the Colorado Real Estate Commission may require that a residential sales contract include title advisory language pertaining to mineral estates. The proposed language would state in bold and capital letters that the surface and mineral estate may be owned separately and that the owner of the mineral estate has the right to enter and use the property. The Real Estate Commission will decide whether to add the title advisory language at its December 1999 meeting.

Recommendation. The committee recommends Bill C. Current law requires that an oil or gas developer provide a surface owner with advance notice of a drilling project. The bill requires that additional information be provided at the time of notification including the phone number and address for the COGCC.

Residential growth, well development, and oil and gas conflicts. Coloradans continue to move into rural areas that overlie substantial oil and gas reserves. Also, denser well development, called in-filling, is occurring in some areas of the state because the commission has determined that more wells are needed to efficiently drain an oil or gas resource. The committee visited a rural subdivision in La Plata County that is threatened by well in-filling. Residents of this subdivision expressed concern that there are too many

homes in the area to safely accommodate additional wells. The committee also visited a subdivision that is encroaching on existing oil and gas wells in Adams County. The developer of this project wants the state to order the wells to be plugged and abandoned so that he may build houses on the well sites. He said that the wells are not economically productive and should not be allowed to occupy land in the housing development. The COGCC testified that it would only order a well to be plugged and abandoned if it is a risk to public health, safety and welfare and not for economic reasons.

Recommendations. The committee did not recommend a bill that would restrict in-filling of oil and gas wells or require that economically nonproductive wells be plugged and abandoned.

Noise and traffic impacts from oil and gas development. The life of a well may extend more than 20 years. During its life, a well may undergo regular maintenance and occasional large-scale production enhancements. Some of the most significant impacts from oil and gas operations occur during well development when access roads are constructed, drilling pads are created, pipelines are buried, and wells are drilled and enhanced. Generally, such projects are short term operations that produce loud noises and involve large amounts of equipment and workers. For example, well drilling may last up to two weeks with operations continuing 24 hours a day. State regulation allows wells to be located as close as 150 feet from occupied buildings and public roads. Some homeowners testified that their quality of life had been disrupted by well activity near their home. Some landowners recommended that the committee impose additional restrictions on noise from oil and gas operations. A county official recommended that counties be granted greater authority to regulate noise caused by oil and gas operations.

Recommendations. The committee makes no recommendation to impose greater restrictions on noise or expand the authority of local governments to regulate the impacts from oil and gas operations.

Methane contamination and impacts from groundwater removal. The committee heard testimony in La Plata County that gas production by some wells may be causing methane gas to contaminate area homes and residential wells. Methane is flammable and contamination may result in fires or explosions if not properly vented. In Las Animas County, the committee heard from persons who want to use the groundwater that is being pumped by gas wells for agricultural and domestic purposes. Under current law, this water, called produced water, may not be discharged into a stream or used beneficially. However, unlike most other areas of the state, this produced water is clean enough to be used to irrigate crops and water stock. The committee heard suggestions that regulations be changed to allow for the beneficial use of produced water because water in the area is scarce and quite valuable. Homeowners also expressed concern that the gas wells are depleting the groundwater on which they rely for their domestic water.

The COGCC said that it is monitoring methane gas seepage and that it will order all wells that are causing methane contamination to be repaired or plugged and abandoned. The State Engineer, COGCC, and the Division of Water Quality testified that they are

determining whether high quality produced water may be used under current law or whether regulatory changes are needed. Officials from Las Animas County and the Department of Local Affairs explained that they are seeking alternative residential water supplies for homeowners concerned about the impact from gas well development.

Recommendations. The committee makes no recommendation to address problems associated with the removal of groundwater by gas wells.

Impacts to wildlife from oil and gas development. Each oil and gas well site and its access road impacts approximately two acres of land. In addition to the loss of terrestrial habitat, access roads and drill pads may cause erosion and sedimentation that could affect aquatic ecosystems. Well activity and truck traffic may also disturb wildlife. Dense well development may be detrimental to wildlife if it occurs in riparian areas and winter ranges that are important for wildlife survival and reproduction. The committee heard testimony in La Plata County about wells that have been constructed in the middle of a narrow valley that may block the migration of wildlife to important habitat.

Recommendations. The committee recommends Bill B to allow the COGCC to regulate oil and gas operations to prevent and mitigate impacts to wildlife. The commission must consider the effect of such measures on public health, safety, and welfare, as well as cost effectiveness and technical feasibility.

Colorado Oil and Gas Conservation Commission and the Regulation of Oil and Gas Operations

Scope of the issue. The mission of the COGCC has changed from its original charge under the Oil and Gas Conservation Act of 1951. It must now balance environmental and public health concerns with the prevention of resource waste and protection of mineral rights. Rules that once focused primarily on minimizing resource waste and promoting production now also reflect the COGCC's charge to mitigate environmental impacts and protect the public from potential harm to their health, safety, or welfare caused by oil and gas operations. The committee examined regulations and activities that allow the commission to balance its charge, and considered whether additions to COGCC's authority would reduce conflicts between surface and mineral owner.

Senate Bill 94-177. In 1994, the General Assembly broadened the power of the COGCC to require production in a manner that prevents and mitigates significant adverse environmental impacts on any air, water, soil or biological resource, taking into consideration cost-effectiveness and technical feasibility. The committee toured sites that served as examples of COGCC's effort to protect the public and the environment. Examples include well setback regulations, environmental monitoring, and special operational considerations, such as requiring that a well be directionally drilled. The committee also heard testimony regarding the COGCC's membership requirements that were changed in 1994.

Well setback regulations. The commission's well setback requirements establish a safe distance from a well pad to an occupied building. In La Plata County, the committee viewed a well located across the street from a school. The well's location was determined not only by the operator's ability to access the resource, but also by the COGCC's setback requirement that established a safe distance from the well pad to the school. The committee toured a residential neighborhood in Weld County and learned that wells are much denser in Weld County than in other parts of the state. Still, wells must comply with the setback requirement.

Monitoring threats to the public and environment. To protect the public and environment, the COGCC investigates and monitors activities that threaten to cause significant adverse impacts. For example, the director of the COGCC testified that methane gas is seeping from the ground in parts of La Plata County. Some residents in the county expressed concern about the impact to public health and the environment. The COGCC is monitoring, mapping and modeling the gas seeps to determine if they are related to gas production in the area.

Noise from oil and gas operations may negatively affect nearby residences. The COGCC's field inspectors are equipped with sound meters to monitor noise levels and enforce the commission's noise regulations. During tours, the committee compared sound meter measurements at construction, well production and compressor station sites. They found that decibel readings were within the COGCC's standards.

Special operational requirements. The COGCC reviews applications to drill wells and sometimes requires that certain considerations be made. For example, the committee learned that oil and gas wells cannot always be drilled in places that are the most convenient for the operators. If the drilling of a well poses an environmental threat, the COGCC may require the operator to relocate the well site. The committee toured directionally drilled wells sites in Trinidad County. Typically, a well is drilled directly above the resource. A directionally drilled well uses angled drilling to reach the resource. In Trinidad, a well was constructed on a mesa rather than in the narrow valley below. The COGCC would not permit the well to be drilled in the valley because of proximity to a stream. They determined that the probability of flooding, which could harm the well and stream, was too great.

Commission membership requirements. The commission has seven members. One member is from each congressional district, one is at-large, and one is from west of the continental divide. Senate Bill 94-177 changed COGCC membership by requiring that five of the members have substantial experience in the oil and gas industry and two members not be employed by industry and have expertise in agriculture, land reclamation, environmental protection or soil remediation.

The committee heard substantial testimony urging that the commission's make-up be changed. Proponents of changing COGCC membership stated that the current composition creates a conflict of interest for members with an industry background who are also regulating the industry. Supporters of current membership requirements stated that it is necessary to have members who understand the complexity of oil and gas development

and production. Also, the commission requires members to remove themselves from discussions that could affect a company in which they have direct financial interest.

Recommendation. The committee recommends Bill A. This bill changes commission membership requirements and provides a per diem.

Colorado Oil and Gas Conservation Commission's Rulemaking Process and Local Participation

Scope of the issue. The commission's rulemaking process allows stakeholder groups, such as industry representatives, farmers, and local government officials to help develop rules. For example, prior to holding well spacing hearings, the COGCC encourages public input on public health and environmental issues associated with the well spacing change. Well spacing is determined by the COGCC on a regional basis and is established by the number of wells per acre that can efficiently drain a reserve. Local public forums provide an opportunity for dialogue on these and other issues. At these meetings, conflicts of interest between surface owners and mineral owners can be discussed and possibly resolved with the commission's help. The committee heard testimony from citizens and the commission on the effectiveness of the rulemaking process.

Local government designee. The commission's local government designee program enables counties and municipalities to stay up to date on COGCC activities in their area. A designee is appointed as the local government's primary contact for the COGCC. They receive notification of commission hearings, well drilling activity, and applications to change well spacing or increase well density. La Plata County's local government designee testified about the difficulties county planners experience when trying to make land uses decisions for a growing residential population. They do not always know where the commission intends to allow future well drilling activities or if it will affect land use plans.

Local public forum. The commission implemented the local public forum process to address complaints that the public has been excluded from the commission's hearing and review process. The forum allows elected officials, local government personnel, and citizens to raise questions or express concerns regarding potential impacts from proposed well drilling applications. The committee learned that oil and gas developer's applications to establish or change drilling and spacing units can be discussed in a local public forum.

Recommendations. The committee did not recommend changes to the COGCC's rulemaking or local participation processes.

SUMMARY OF RECOMMENDATIONS

As a result of the committee's activities, the following three bills are recommended to the Colorado General Assembly.

Bill A — Oil & Gas Conservation Commission Personnel

The committee learned that over fifty percent of the state's oil and gas production occurs in Colorado's third congressional district. This district primarily covers the western slope. Due to current membership requirements for the Colorado Oil and Gas Conservation Commission, the district is represented by one commissioner. This bill eliminates the requirement that at least one commission member be appointed from each congressional district, thereby allowing areas of the state with high production levels to have greater representation on the commission. The bill increases the number of members from the west slope from one to two and also provides each commission member a \$50 per diem for meetings or hearings they attend.

The bill has a state fiscal impact because it will require a General Fund appropriation of \$16,492 to pay for the commissioner's per diem.

Bill B — Colorado Oil and Gas Conservation Commissions Authority to Consider Wildlife

Each oil and gas well site and its access road impacts approximately two acres of land. In addition to the loss of terrestrial habitat, access roads and drill pads may cause erosion and sedimentation that could affect aquatic ecosystems. Dense well development may be detrimental to wildlife if it occurs in riparian areas and winter ranges that are important for wildlife survival and reproduction. This bill allows the commission to develop regulations that prevent and mitigate significant adverse impacts on wildlife during oil and gas operations. For example, the commission may require that operations do not disrupt a wildlife migration route. However, the regulations cannot be more stringent than those already in place to protect public health, safety, and welfare. Likewise, cost-effectiveness and technical feasibility must be taken into consideration.

Bill B does not have a fiscal impact because it does not affect state or local government revenue or expenditures.

Bill C — Documents to Surface Landowner

Some landowners are unaware of oil and gas policies and that minerals have been severed from their land. They become quite concerned when they receive notice that an oil or gas well is planned for their land. The committee considered the COGCC's process of notifying surface landowners and determined that certain relevant information is not being

provided by the mineral developer to the surface landowner. This bill requires the oil and gas operator to provide specific documentation to surface owners during the notification process including:

- copies of the commission's rules related to notices of oil and gas operations and consultations with surface owners;
- the name, address and telephone number of the commission's regional representative and local government designee;
- the commission's main office address and toll-free telephone number;
- the name of the oil and gas operator or operator's agent and their address and telephone number;
- information that the surface owner has the right to seek the opinion of an attorney; and
- any other information the commission determines may assist the surface owner prior to oil and gas activity on his or her land.

Bill C does not have a fiscal impact because it does not affect state or local government revenue or expenditures.

RESOURCE MATERIALS

The resource materials listed below were provided to the committee or developed by legislative staff during the course of meetings. The summaries of meetings and attachments are available at the Division of Archives, 1313 Sherman Street, Denver. For a limited time, the meeting summaries and materials developed by legislative staff are available on our web site at:

http://www.state.co.us/gov_dir/leg_dir/lcsstaff/1999/99interim.htm.

Meeting Summaries	Topics Discussed
August 3 & 4, 1999	Regulation of oil and gas development, mineral rights law, panel discussion on oil and gas issues, public testimony, and tour of Adams and Weld counties' oil and gas operations.
September 8 & 9, 1999	Impacts and benefits of oil and gas development in La Plata County, overview of gas production on private and tribal lands, public testimony, and tour of oil and gas operations in La Plata County.
September 20 & 21, 1999	Overview of oil and gas development on federal lands and private lands in Garfield County, environmental concerns and economic benefits of oil and gas operations, public testimony, and tour of gas operations in Garfield County.
October 5 & 6, 1999	Groundwater depletion from gas production, overview of gas and CO2 production in Las Animas County, impacts and benefits from gas production, and tour of gas operations in Las Animas County.
October 19, 1999	Overview of Energy and Mineral Impact Fund, surface damage negotiations, and treatment of oil and gas disputes by the courts.
October 20, 1999	Public testimony and committee action on proposed legislation.

Memoranda and Reports

Memoranda from Office of Legislative Council Staff

Statutory Authority of the Colorado Oil and Gas Conservation Commission, Allison Pasternak, July 27, 1999

Well Spacing and Well Siting, Allison Pasternak, July 27, 1999

State and Local Government Land-Use and Planning Authority Pertaining to Oil and Gas Development and Production Facilities, David Beaujon, July 30, 1999

Oil and Gas Legislation, David Beaujon, August 19, 1999

Proposed Title Advisory Language in Residential Real Estate Sales Contracts, David Beaujon, August 31, 1999

Conflict of Interest Requirements for the Public Utilities Commission, David Beaujon, October 4, 1999

Memorandum from Office of Legislative Legal Services staff

Overview of Surface Damages Acts in Other States, Robert Neill, August 30, 1999

Reports Provided to the Committee

Executive Summary of State Engineer's Presentation About Groundwater from Coal Bed Methane Wells in Las Animas County, Division of Water Resources, September 29, 1999

Role and Purpose of the Energy and Mineral Development Impact Grant Program, Department of Local Affairs, October 19, 1999