Committee on Resources

Witness Testimony

**STATEMENT OF GEORGE H. FANCHER, JR.
TO THE SUBCOMMITTEE ON ENERGY AND MINERAL RESOURCES
OF THE U. S. HOUSE OF REPRESENTATIVES
COMMITTEE ON RESOURCES
JUNE 30, 1997**

Thank you Madam Chairman for the privilege to appear before you and the subcommittee on Energy and Mineral Resources. It is time we examine the issues which are adversely affecting our industry. You are to be complimented on your interest in listening to some of the problems that producers in the Rocky Mountain Region are having with governmental agencies such as the BLM. The goal of the government should be to encourage and help private industry to be more efficient and to economically develop and produce the domestic oil and gas reserves that are available in the United States.

My name is George Fancher and I am the owner of Fancher Oil Company, a small independent producer located in Denver, Colorado. I have been active in the Rocky Mountain area since 1969. I am a member of the Independent Petroleum Association of Mountain States (IPAMS), the Wyoming Independent Producers Association (WIPA), and the Independent Petroleum Association of America (IPAA). From 1991 through 1996, I served as Chairman of IPAMS Crude Oil Committee and last year I was a member of Governor Geringer's State and Industry Negotiating Committee for the Express Pipeline Project State Land's Right-of-Way issue.

However, today, I am not representing any organization and my comments reflect only my concern about the procedures used by the BLM in approving the Environmental Impact Statement (FEIS) for the Express Pipeline Project which is projected to deliver 172,000 BPD of Canadian crude oil from Hardisty, Alberta to Casper, Wyoming. As a result of my experience with the Express Project, I am concerned about the lack of a comprehensive process to evaluate the need for and impact of an international pipeline on local and state economies and to the domestic oil and gas industry.

The Express Pipeline has been in operation for only a few months and its impact upon crude oil prices has already been felt. Prices for crude oil have fallen by approximately $2.50 a barrel and have virtually wiped out the premiums (bonus) over posted price which Wyoming crude oil producers were receiving. I expect that by the end of the year the premiums will no longer exist. This is due to the fact that by the end of the year Express Pipeline will be shipping approximately 172,000 barrels of crude oil per day from Hardisty, Alberta to its connection with the Platte Pipeline at Casper, Wyoming. I anticipate that substantial quantities of crude oil being shipped on Express Pipeline will be used to compete with oil produced by Rocky Mountain oil producers in markets which include Wyoming, Colorado, and Utah. The balance of Express' crude will be shipped eastward on the Platte Pipeline to its terminus at Wood River, Illinois.

Initial studies commissioned by the BLM of the socio-economic impact of the pipeline predicted the effect which is now being felt. The initial studies concluded that there would be a price reduction of approximately $2.50 per barrel for all types of Wyoming crude as a result of the pipeline. The initial

report by the BLM's consultants concluded that the potential total cumulative loss of income to Wyoming producers resulting from foregone production (accelerated decline) and lower prices through 2005 would be as much as $2.1 billion. The initial report also found the total impact on Wyoming state and local tax revenues would be about $23.3 million in 1997. These initial reports directly contradicted conclusions reached by the BLM in the Draft Environmental Impact Statement for Express Pipeline ("DEIS") stating that the pipeline would not directly affect oil production in Wyoming and Montana. The initial report described above confirmed comments made by producers which were received by the BLM after the DEIS was published, that there would be a substantial impact on crude oil production in Wyoming.

In my view, the BLM did an inadequate job in evaluating the impact of this pipeline. In fact, the BLM capitulated to Express after Express' attorneys objected to the consultants analysis which resulted in dramatic changes to their revised report.

While the initial report concluded that there would be a price reduction of $2.50 per barrel for all types of Wyoming crude as a result of the Pipeline, the revised report concluded that there would be a price reduction of only $1.00 per barrel for just Wyoming sweet crude, and that since "sweet crude only comprises 35 percent of Wyoming's total production, the overall income and tax revenue effects would be similar to a $0.35 per barrel decline for all Wyoming production." The initial report stated that "the total impact on Wyoming State and local tax revenues would be about 23.3 million in 1997." Ten days after receiving criticisms from Express' attorney, however, the BLM consultant revised its report and concluded that "[t]he total impact on Wyoming State and local tax revenues would amount to $3.4 million in 1997."

Also, the initial report concluded that "[t]he potential total cumulative loss of income to Wyoming producers resulting from foregone production (accelerated decline) and lower prices through 2005 could be as much as $2.1 billion." Ten days later, BLM's consultant concluded that the Pipeline "is not expected to accelerate the overall rate of decline in production of Wyoming oil," and that "[b]ased on the projected annual rate of decline of 4.0 percent for the next ten years, the potential loss of income resulting from the $1.00 per barrel reduction in sweet crude through 2005 could be as much as $195.8 million." In the span of ten days, the BLM's consultant changed its evaluation of the cumulative impact to local producers from 2.1 billion dollars through 2005 to 195.8 million through 2005 (a change of over 1.9 billion dollars).

The Final EIS incorporated the conclusions of the revised report issued ten days after Express's attorney criticized the initial report.

The final EIS report recognized that the premiums or bonus being paid at that time for sweet crude were in the range of $2.25 per bbl and up to $4.50 per bbl for general sour crude. With refineries in the region operating at capacity, the impact of an additional 100,000 BPD of crude via Express was only expected to reduce the price of sweet crude by $1.00 per bbl and would have no effect on Wyoming general sour crude.

The final report contains numerous flaws including, but not limited to 1) the use of the same production decline rate to forecast what would happen without the Pipeline and what would happen with the Pipeline; 2) the failure to adequately support its conclusion that even though a bonus in the range of $2.25 to $4.50 per barrel is being paid for Wyoming crude oil because of purported shortages of oil, and even though the consultants assumed that the Pipeline would more than adequately meet

local demand for crude oil, that somehow the Pipeline would effectively reduce the price of Wyoming crude by only $.35 per barrel; 3) the failure to specifically identify the sources upon which the consultants relied for material assumptions; 4) inconsistent assumptions concerning transportation costs; and 5) an inadequately supported assumption that Canadian crude will not displace Rocky Mountain oil production; 6) failure of the WSO to include information based on regional historical retail gasoline prices and, whether or not a crude oil oversupply has ever resulted in lower gasoline prices at the pump.

Because of the radical changes between these two reports, the Wyoming State Office of the BLM (WSO) should have been very concerned about this shift and sought independent review. The WSO never independently challenged or even questioned this dramatic $1.9 billion dollar change and the consultant's reversal of its initial conclusion. The WSO never disclosed the presence of the two radically different socio-economic analyzes and never disclosed why it rejected the initial Report and accepted the revised Report. The WSO made no attempt to quantify the loss of non-renewable natural resources which will result from the construction and operation of the Pipeline. Thus, the WSO breached its obligations under NEPA to independently review and analyze the consultant's work on socio-economic impacts and failed to ensure the professional integrity of the analysis contained in the consultant's Final Report. The first time the public had an opportunity to review the analysis performed by the reports was when the FEIS was issued.

The WSO refused to extend the FEIS comment period to allow the Governor of Wyoming an opportunity to address the final report which was disclosed to the public for the first time in the FEIS. The WSO failed to adequately address and consider relevant information submitted to it during the commenting process on the FEIS which put into question the validity of key assumptions upon which the final report was based, including the transcript of a March 20, 1996 hearing held before the Wyoming State Senate Select Committee on Mineral Transportation which was submitted to the WSO, and other information concerning domestic oil production and related socio-economic impacts this Pipeline would cause. The WSO should have treated the final report as new information not previously disclosed in the DEIS and afforded the public the same commenting opportunity which was provided on other areas originally covered in the DEIS.

On June 13, 1996, I learned that the consultant had new information which would have caused them to reach different conclusions from those in the final report. On or about June 20, 1996, I spoke to Mr. Ogaard of the WSO about the consultant's new information. Mr. Ogaard informed me that he did not really care if there was new information or if the consultant's opinion may have changed, that he had to draw the line somewhere and the WSO was not about to re-open the case to consider the impact the pipeline would have on domestic crude oil production and related socio-economic impacts.

It was and is reasonably foreseeable that the inundation of large volumes of Canadian crude oil in the Rocky Mountain region would cause the price of oil in Wyoming to fall and wells to be shut-in, resulting in a loss of otherwise recoverable domestic natural resources which violates one of the fundamental purposes of NEPA which is the prevention of waste of non-renewable natural resources. The WSO was obligated to evaluate and disclose "any irreversible and irretrievable commitments of resources which would be involved in the proposed action should it be implemented" including the loss to domestic oil reserves resulting from the project.

"In order to encourage the greatest recovery of oil and in the interest of conservation," the BLM announced new regulations reducing the rate of federal royalties for heavy grades of crude oil. 61 Fed.

Reg. 4748 (February 8, 1996). These new rules were designed to "provide an economic incentive to implement enhanced oil recovery projects, and delay the plugging of [marginal] wells until the maximum amount of economically recoverable oil can be obtained from the reservoir or field." 61 Fed. Reg. at 4748. The BLM explained why it felt royalty relief was needed:

As many as two-thirds of all marginal properties (including non-heavy oil properties) could be lost during a period of sustained low oil prices (Marginal Wells, a Report of the National Petroleum Council, 1994, p.3). The danger in losing the marginal wells is that, although production from individual wells may be small, their collective production is significant, accounting for one-third of all onshore domestic production excluding Alaska.

Nowhere in the analysis of the socio-economic impact of the Pipeline did the WSO address the impact of these regulations which were promulgated by its own agency. Neither the DEIS nor the FEIS contained any analysis of the economic limits of domestic oil production or any quantification of the domestic oil reserves which will be lost as a result of the proposed Pipeline.

The failure of the BLM to adequately assess the impact of Express on local prices violates NEPA which provides that it is the responsibility of the Federal Government to "enhance the quality of renewable resources and approach the maximum attainable recycling of depletable resources. Crude oil is a natural resource, but it is depletable. If fields or wells have to be abandoned before the resource has been produced to its maximum attainable limit, then waste will occur. The prevention of waste of natural resources is a fundamental purpose of NEPA. The broad aim of NEPA is well established.

The National Environmental Policy Act contains no exhaustive list of so-called "environmental considerations" but without question its aims extend beyond sewage and garbage and even beyond water and air pollution. The act must be construed to include protection of the quality of life...(citations omitted).

When economic and environmental effects are interrelated, the EIS must discuss all of the effects of the proposal on the human environment, including social and economic. The scope of effects to be considered under NEPA is expansive. Under NEPA, the term "effects" includes:

Indirect effects, which are caused by the action and are later in time or farther removed in distance, but are still reasonably foreseeable. Effects and impacts as used in these regulations are synonymous...Effects includes...economic, social, or health, whether direct, indirect or cumulative. Effects may also include those resulting from actions which may have both beneficial and detrimental effects, even if on balance the agency believes that the effect will be beneficial.

A cumulative impact is defined in NEPA regulations as:

[T]he impact on the environment which results from the incremental impact of the action when added to other past, present, and reasonably foreseeable future actions regardless of what agency (Federal or non-Federal) or person undertakes such other actions. Cumulative impacts can result from individually minor but collectively significant actions taking place over a period of time.

Here economic and environmental effects are clearly interrelated. It is "reasonably foreseeable" that the Pipeline will cause a substantial number of domestic oil wells to be shut in, resulting in the loss of

otherwise recoverable domestic natural resources.

In summary, the process must ensure that the socio-economic aspects of the NEPA process receive more comprehensive treatment than was done with the Express Pipeline project. The failure to disclose the radical shift in the analysis of the socio-economic impact of this pipeline to the public must be prevented in the future, especially where the lack of a truly independent analysis may lead to the waste of natural resources.

In the future, our industry will be faced with similar situations involving foreign oil and gas projects that will directly impact the domestic energy industry. The Express Pipeline Project illustrates the fact that no state or federal governmental agency has the final or overall authority to evaluate the need for and the impact of an international pipeline on local and state economies and the domestic energy industry in general.

Because of the many questions that the Express pipeline has raised, I recommend that the government, in conjunction with industry, develop a comprehensive approval process for foreign pipelines transporting foreign crude oil, natural gas and/or refined products into this country which will evaluate the viability and effect of the project on all concerned.

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