IN THE SUPERIOR COURT FOR THE STATE OF ALASKA
THIRD JUDICIAL DISTRICT AT ANCHORAGE

DENALI CITIZENS COUNCIL,	)	
	)	
Appellant,	)	
	)	
v.	)	
	)	
STATE OF ALASKA, DEPARTMENT OF NATURAL RESOURCES, and USIBELLI COAL MINE, INC.,	)	
	)	
Appellees.	)	
	)	Case No. 3AN-10-12552 CI

ORDER ON ADMINISTRATIVE APPEAL

This is an administrative appeal arising from the Department of Natural Resources' (DNR) final decision to grant Usibelli Coal Mine, Inc. (Usibelli) a gas-only exploration license covering 208,630 acres in the Healy basin area.[1] Denali Citizens Council (DCC) appeals DNR's final finding that granting the license was in the best interests of the state. DCC's main arguments are (1) DNR's finding that a smaller license area is economically unfeasible is arbitrary, and (2) DNR's approach to mitigation measures is not supported by law.

I. Facts and Proceedings

On April 18, 2003, Usibelli submitted eight shallow-gas lease applications totaling 46,080 acres east of the Nenana River in the Healy area. [Exc. 2-47] On March 25, 2004, Usibelli submitted seven shallow-gas lease applications totaling 38,400 acres in roughly the same areas. [Exc. 54-90] Around this time, the Alaska State Legislature was considering H.B. 531, 23rd Ak. State Leg. (Ak. 2004). H.B.

[1] The Court has jurisdiction pursuant to AS 30.05.035(l).

531 would replace the leasing program under which Usibelli filed the lease applications with a new gas-only exploration licensing program. The intent of exploration licensing is to encourage exploration in areas outside of known oil and gas provinces. [Exc. 138] Because there is a higher investment risk to explore in areas with relatively low or unknown potential, the exploration licensing program incentivizes an interested party by giving that party the exclusive right to conduct exploration without initial expense. *Id.*

In anticipation of H.B. 531, Usibelli submitted a gas-only exploration license proposal on April 23, 2004. [Exc. 91-93] The proposal covered 208,630 acres in the Healy area, encompassing land included in the original lease applications and expanding west of the Nenana River. [Exc. 93] H.B. 531 was signed into law and Usibelli let the original 2003 and 2004 applications lapse.

On November 9, 2004, DNR provided notice of its intent to evaluate the proposal. [Exc. 122] DNR requested competing proposals, but did not receive any. *Id.* On January 11, 2005, DNR requested comments from agencies and the public within 60 days regarding the proposed license. *Id.*

DCC responded, objecting to expansion into residential areas, *e.g.* the Wolf Township, and wildlife and recreation rich areas because it created significant conflicts between gas activities, residents, and wildlife. [Exc. 123-28] DCC commented that DNR should address facility siting, spacing and noise mitigation in the findings. *Id.*

On August 31, 2005, DNR issued a preliminary "best interest" finding (hereafter "preliminary finding"). [Exc. 131-312] The preliminary finding dedicated one chapter to mitigation measures. [Exc. 250-61] DNR imposed several measures to "mitigate the potential adverse social and environmental effects of specific license related activities[.]" [Exc. 251] For example, DNR prohibited Usibelli from constructing drill pads within 500 feet of any residential structure and compressor stations within 1,500 feet. [Exc. 255] Additionally, Usibelli could not "construct drill pads or compressor stations in any residential subdivision in

which more than half of the land is divided into lots sized at five acres or less, without the consent of all surface property owners within that subdivision." [Exc. 255] DNR also imposed measures to mitigate potential noise impacts associated with facilities and compressor stations, requiring a plan of operations to include a noise monitoring plan. [Exc. 253] DNR established maximum ambient noise levels for day and night hours. [Exc. 253-54] Some measures to mitigate noise impacts included: venting exhaust away from residences, using quiet design mufflers, limiting the hours of noise-generating operation to daytime hours, using sound insulating enclosures, and siting facilities and compressor stations in locations that use geographic features to buffer noise. [Exc. 254] The preliminary finding provided that DNR may grant exceptions to mitigation measures, but only "upon a showing by the licensee that compliance with the mitigation measure is not feasible or prudent, or that the licensee will undertake an equal or better alternative to satisfy the intent of the mitigation measure." [Exc. 251] DNR concluded that issuance of the license was in the best interests of the state. [Exc. 268]

On August 31, 2005, DNR provided public notice of the preliminary finding and invited the public to comment. [Exc. 129-30] DCC submitted comments on the preliminary finding, again objecting to the size of the license area. [Exc. 313-30] Usibelli also submitted comments, stating, in part, that "the operation practicalities and economic would be significantly affected if DNR were to impose any more onerous mitigating measures" than the ones in the preliminary finding. [Exc. 337]

On June 28, 2010, DNR issued a final "best interest" finding, entitled "Healy Basin Gas Only Exploration License Final Finding of the Director" (hereafter "final finding"). [Exc. 348-594] DNR concluded that granting Usibelli's

license proposal was in the best interests of the state.[2] The final finding did not remove acreage from the license proposal. In response to commenters' position that the area west of the Nenana River should be removed from the license area, DNR explained:

> Removing the area west of the Nenana River from the license area may make the project economically unfeasible. The imposition of mitigation measures to avoid, minimize, or mitigate potential impacts is preferable to removing a large acreage from the license area. As specific projects are proposed, additional mitigation measures may be imposed. Given these measures, licensee advisories, and existing laws and regulations, removing the area west of the Nenana River from the license area is unnecessary. ...

[Exc. 515][3] Additionally, DNR addressed concerns regarding the Denali National Park and Preserve and the Wolf Townships:

> Mitigation measures and licensee advisories are designed to protect diverse aspects of habitats, species local uses, and other uses and values. Each of these measures, in turn, will help protect recreational values, fish and wildlife populations and habitats, scenic views, and adjacent landowners such as [the National Park Service].

[Exc. 515-16] Also, DNR modified the provision regarding exceptions to mitigation measures. DNR replaced the language "not feasible or prudent" with "not practicable," allowing an exception to mitigation measures "upon a showing by the licensee that compliance with the mitigation measure is not practicable." [Exc. 500]

DNR also modified specific mitigation measures. For example, DNR rewrote the noise standards, removing the noise monitoring plan requirement and the maximum ambient noise levels. In lieu of these measures, DNR decided that

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[2] "[T]he director has concluded that the potential benefits of issuing the Healy exploration license outweigh the possible negative effects, and that issuing the Healy exploration license will best serve the interests of the state of Alaska." [Exc. 373; *see also* Exc. 359, 364-65.]

[3] In Appendix A to the final finding, DNR provided a summary of agency and public comments received and DNR's responses to those comments. [Exc. 511-56] Although the Court does not

noise impacts would be "considered on a site-specific basis." [Exc. 502] DNR also removed the requirement that Usibelli obtain approval from all surface property owners within a subdivision.

DCC appeals DNR's final finding, arguing that DNR erred by failing to remove acreage from the license area and modifying the mitigation measures.

II. Applicable Law

The Alaska Constitution provides that the state's policy is "to encourage...the development of its resources by making them available for maximum use consistent with the public interest" and that the "legislature shall provide for the utilization, development, and conservation of all natural resources belonging to the State...for the maximum benefit of its people. Alaska Constitution, article VIII, § 1 and 2.

AS 38.05.035(e) permits the state to approve contracts for the sale, lease, or other disposal of available land or resources based on a single written finding that disposal would be in the state's best interests. The commissioner may issue exploration licenses pursuant to AS 38.05.132 to "encourage exploration for oil and gas on state land[.]" AS 38.05.132(a). AS 38.05.132(c)(2) provides that an exploration license may cover "an area of not less than 10,000 acres and not more than 500,000 acres, that must be reasonably compact and contiguous[.]"

AS 38.05.133 establishes the procedure for issuing an exploration license, which begins with the submission of a proposal. After considering the proposal and any solicited comments, DNR issues a written finding addressing whether approving a license would be in the state's best interests under AS 38.05.035(e) and (g). DNR may impose mitigation measures in addition to conditions and limitations already imposed by law. AS 38.05.035(e).

AS 38.05.035(e)(1)(C) allows DNR to "limit the scope of an administrative review and finding for the proposed disposal to the applicable statutes and

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interpret DNR's responses to comments as findings, the responses are helpful in evaluating whether DNR's findings were reasonable and not arbitrary.

regulations, facts and issues...that pertain solely to the disposal phase of the project[.]" Here, DNR limited this Court's scope of review to the disposal phase. [Exc. 375; *see also* Exc. 373.]

III. Standard of Review

"'(I)n cases concerning administrative expertise as to either complex subject matter or fundamental policy formulations,' an administrative agency's decision will be reviewed by the court only to the extent necessary to ascertain whether the decision has a 'reasonable basis.'" *Hammond v. North Slope Borough*, 645 P.2d 750, 758 (Alaska 1982) (quoting *Kelly v. Zamarello*, 486 P.2d 906, 917 (Alaska 1971). The Alaska Supreme Court has specifically held that DNR's best interests determination is "subject to a deferential reasonable basis review." *Kachemak Bay Conservation Soc. v. State, Dept. of Natural Resources*, 6 P.3d 270, 275 (Alaska 2000). In reviewing DNR's decision, the Court does not "undertake an elaborate reconsideration of the substantive merits of the Director's decision at some later date." *Moore v. State*, 553 P.2d 8, 36 n.20 (Alaska 1976). The Court "has neither the authority nor competence to decide whether the public interest is 'best served' by a proposed disposition of land. Nonetheless, a limited review of the Director's decision would be available simply to ensure that it was not arbitrary, capricious, or prompted by corruption." *Id.* Although this standard of review is deferential, the Court's duty is to ensure that DNR has taken a "hard look at the salient problems and has genuinely engaged in reasoned decision making." *Kachemak Bay*, 6 P.3d at 275 (citation omitted).

IV. Analysis

A. DNR had a reasonable basis to grant Usibelli the exploration license without limiting acreage.

DCC argues that DNR arbitrarily relied on the possibility that excluding acreage may make the project economically unfeasible for Usibelli. For support, DCC relies on Usibelli's 2003 and 2004 lease applications, covering approximately 40,000 acres each, to argue that an exploration license area smaller

than 208,000 acres would have been economically feasible for Usibelli. In response, DNR argues it did not find that limiting acreage would make the project economically unfeasible, only that it may do so. Additionally, DNR's statement regarding economic unfeasibility was made in response to comments, is part of the appendix to the final finding and is not a finding itself. DNR also argues that granting the license served the state's best interests. DNR argues that eliminating acreage is not consistent with encouraging oil and gas assessment or minimizing adverse impacts of exploration and development. At oral argument, Usibelli commented that leases differ from licenses and, therefore, DCC's comparison of the exploration license to the 2003 and 2004 lease applications is misplaced.

The Court concludes that DNR's decision to grant Usibelli the exploration license without limiting the amount of acreage was reasonable. DNR's decision was not arbitrary for several reasons. First, the license area is within the parameters established by AS 38.05.132(c)(2), which provides that an exploration license may cover "an area of not less than 10,000 acres and not more than 500,000 acres, that must be reasonably compact and contiguous[.]" The license covers an area of 208,630 acres—less than half of the maximum allowed--and is reasonably compact and contiguous.

Second, the license area is consistent with the intent of exploration licensing, which is to encourage exploration in areas with low or unknown potential. DNR considered this factor in its final decision, stating that "[v]ery little subsurface geological information is available within the Healy Basin exploration license area, and there is no documentation available quantifying the occurrence of hydrocarbons, either gas or oil, within the license area…It is not known whether the gas is of sufficient quantity to be commercially developable." Exc. 430.

Third, it is reasonable for DNR to conclude that a larger license area is more consistent with the best interests of the state than a smaller license area. AS 38.05.180(a)(2) provides that "it is in the best interests of the state (A) to encourage an assessment of its oil and gas resources and to allow the maximum

flexibility in the methods of issuing leases to...minimize the adverse impact of exploration, development, production, and transportation activity...and (B) to offer acreage for oil and gas leases or for gas only leases[.]" Therefore, DNR's decision to impose mitigation measures instead of limiting the license area is reasonable and consistent with the best interests of the state to offer acreage and encourage assessment while minimizing adverse impacts.

DCC draws a comparison of the acreage in Usibelli's lease applications to the much larger acreage in Usibelli's license in order to suggest the license is excessive. The comparison is unpersuasive. As DNR discussed in the final finding, there are "significant differences between the leasing and licensing programs." [Exc. 369-70] For example, prospective lessees submit a bonus bid based on dollars per acre, whereas a prospective licensee proposes direct exploration expenditures for a specific area. [Exc. 369] Also, lease rentals begin at $1 per acre, increasing annual to a maximum of $3 per acre. Licensees, on the other hand, pay a one-time, $1 per acre licensing fee. [Exc. 370]

In light of these considerations, the Court concludes that DNR's decision to grant the license without limiting the license area was reasonable, not arbitrary, and consistent with the best interests of the state.

B. DNR's final finding on mitigation measures is not arbitrary.

DCC argues that DNR's decision is arbitrary because the final finding imposes mitigation measures with standards lower than those set forth in the preliminary finding. Citing *Trustees for Alaska v. State, Department of Natural Resources*, 851 P.2d 1340 (Alaska 1993) (*Camden Bay II*), DNR argues that DCC's challenge to mitigation measures is premature and their adequacy should not be assessed until DNR reviews a plan of operation. Notwithstanding this point, DNR argues the measures are sufficient and not arbitrary. DNR's final finding devoted an entire chapter to mitigation measures, detailing measures that applied to all plans of operation, exploration, or development and other permits. [Exc. 499-508]

In *Camden Bay II,* Trustees challenged the adequacy of DNR's mitigation measures at the lease sale stage. *Id.* at 1346-47. DNR argued that mitigation measures were not required at that stage. *Id.* The supreme court agreed with DNR, explaining:

> DNR's mitigation measures provide sensible guidelines to minimize the harmful effects of oil and gas development. Most importantly, the lessees cannot develop their leases until they submit detailed plans, which must satisfy the ACMP regulations. If the plans do not satisfy the ACMP regulations, DNR can impose additional mitigation measures that assure that the regulations are complied with. Thus we reject Trustees' argument to the extent that it would tie the reasonableness of DNR's consistency determination to its developing and assessing detailed mitigation measures even before knowing which activities it needs to mitigate.

Id. The court rejected the requirement that DNR "evaluate the effectiveness of mitigating measures before even receiving detailed development proposals." *Id.* The supreme court reaffirmed this position in *Ninilchik Traditional Council v. Noah*, 928 P.2d 1206 (Alaska 1996), which held that it was reasonable for DNR to prescribe general mitigation measures at the lease sale stage. *Id.* at 1210-12. The court reasoned that DNR prescribed more than twenty general mitigation measures that provided "sensible guidelines" to minimize effects of development. *Id.* at 1211.

Under the precedents established by our supreme court, at this time it is premature to consider the adequacy of DNR's mitigation measures. This conclusion is reinforced by DNR's final finding, which provided that "[a]dditional [mitigation] measures will likely be imposed when licensees submit a proposed plan of operations." [Exc. 500] No plan of operations has been submitted yet.

Although it is premature to evaluate mitigation measures in this case, the Court does not find the measures DNR has adopted thus far to be arbitrary. DCC's main challenge is that when DNR issued it final finding it revised the measures stated in the preliminary finding and did so, according to DCC, arbitrarily. After

reviewing the measures, however, the Court concludes that the changes had a reasonable basis.

For example, in response to the noise measures set forth in the preliminary finding, Usibelli submitted comments to DNR that: "the noise standards appear arbitrary and possibly unreasonable because no discussion or citations were provided in the preliminary finding relating to the source and justification for the specific attainment standards; also, there is no discussion about what portions of the license area, or type of activities would require a monitoring plan." [Exc. 540] DNR responded: "[t]he noise standards have been rewritten for the final finding. Specific noise criteria and methods to meet those criteria will vary depending on location and will be determined on a case-by-case basis during the permitting process." *Id.*

DNR also addressed removing the requirement that Usibelli obtain the consent of subdivision residents. Usibelli commented that the requirement to obtain approval from all surface property owners within a subdivision to operate on any lot in the subdivision goes beyond reasonable regulation. Usibelli commented that this type of measure is not necessary on top of the additional setbacks and other protective measures that are included. DNR agreed, responding that the requirement for obtaining consent of all surface property owners within a subdivision has been removed from mitigation measures in the final finding. [Exc. 540]

DCC argues DNR arbitrarily lowered the standard in determining whether to grant an exception to mitigation measures, disagreeing with DNR's decision to replace the language "not feasible or prudent" with "not practicable." In response to a comment made by Usibelli, DNR explained the reason for the modification:

> Exceptions may be granted if it is not practicable to comply with the standard. The final finding uses the term practicable instead of "feasible or prudent." Practicable means feasible in light of overall project purposes after considering cost,

existing technology, and logistics of compliance with the mitigation measure.

[Exc. 540] Merriam-Webster defines "practicable" as "capable of being put into practice or of being done or accomplished." "Feasible" is defined as "capable of being done or carried out." "Prudent" means wise or judicious, but may also refer to frugality. It is difficult to discern any meaningful difference in the terms "practicable," on one hand, and "feasible or prudent," on the other. In the context of this case, both expressions embody a consideration of multiple factors such as available technology, costs and benefits. Contrary to DCC's suggestion, the Court does not perceive the change in language establishes a lower standard in the final finding than in the preliminary finding.

V. Conclusion

Given DNR's detailed and comprehensive findings, the Court must reject DCC's contention that DNR's decision to grant Usibelli the exploration license was arbitrary. DNR's decision to impose mitigation measures to minimize adverse impacts of development rather than exclude acreage from the license is consistent with the best interests of the state. The Court, therefore, AFFIRMS DNR's decision.

ORDERED this 29th day of August, 2012, at Anchorage, Alaska.

Andrew Guidi

ANDREW GUIDI
Superior Court Judge

I certify that on 8/30/12
a copy of the above was mailed to
each of the following at their
addresses of record: A Do - Kruse
K. Parker
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BBrown
for Jackie Kapper, Judicial Assistant