Drilling in 2012: Production Up; Fewer Leases

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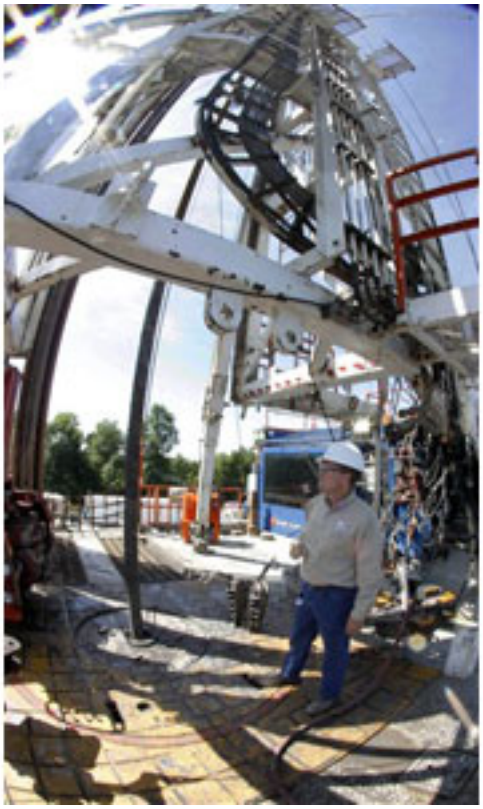

PITTSBURGH (AP) — Marcellus Shale natural gas production is expected to keep rising in 2012, yet landowners may find that signing lease deals isn't as easy as in years past.

Though still in its early stages, industry experts say that the business of Marcellus Shale gas drilling is starting to change, as new forces emerge.

Among them: lawmakers putting regulations in place that will create more drilling opportunities in shale states other than Pennsylvania; Shell's coming decision on where to build a massive processing plant; and the great unknown, the market prices for natural gas.

Drillers have swarmed in recent years to the lucrative Marcellus Shale region primarily beneath Pennsylvania, New York, West Virginia and Ohio. Pennsylvania is the center of activity, with more than 3,000 wells drilled in the past three years and thousands more planned. Critics say a drilling method known as hydraulic fracturing, or fracking, could poison water supplies, while the natural-gas industry says it's been used safely for decades.

2012 could lessen the spotlight on Pennsylvania. Other states are moving toward updating laws to regulate drilling, and the industry is starting to explore a new gas resource — the Utica shale, which lies under the Marcellus formation.

"New York will see a regulatory package; I think West Virginia will probably be in a

situation where there's more certainty," said Kathryn Klaber, president of the Marcellus Shale Coalition, an industry group based in Pennsylvania.

There's one variable that impacts the industry everywhere it operates, Klaber said.

The biggest unpredictable for 2012 is wholesale natural gas prices, she said. They've stayed low for a few years, and that's helped boost demand from some areas, such as gas-fired electric power plants. But with more and more gas entering the market, no one knows just where the balance of supply and demand will lead.

If prices drop further, drilling could slow. But if they rise, the boom could speed up even more.

Klaber said it will become clearer next year just how economically viable the Utica Shale is. Some companies have reported promising results from wells in western Pennsylvania and eastern Ohio.

"The wells drilled to date have made a lot of folks optimistic. But I think it's still too early to tell how the Utica will play out," she said.

Officials from three of the shale states — Pennsylvania, Ohio and West Virginia — are all competing to land the a huge new multibillion-dollar Shell Oil Co. petrochemical processing plant. Known as cracker plants in the industry, such plants take a liquid form of natural gas and turn it into other commercial compounds, such as plastics.

Shell expects to choose a location for the plant soon and announce the decision early in January, spokeswoman Kelly op de Weegh told The Associated Press.

Another coming change will be in leases for land to drill on, experts said.

The past few years saw what seemed at times to be a mad rush by the industry to persuade property owners to sign deals. But now many of the big drilling companies have tens of thousands of acres under lease, said Brian Pitell, a representative for the National Association of Royalty Owners in northwestern Pennsylvania.

"The land grab, like the gold rush, is kind of over. You don't have two, three or four different companies" all competing to offer leases in the same region, he said.

That means landowners have fewer options, and less power to demand certain lease terms.

"There's a muting, to some degree, of competition," Pitell said. Sometimes it's the fine print that changes, he said, noting that one recent lease from a big company removed the landowner's right to audit royalty statement payments.

And if a landowner doesn't like that?

"If you think you're just going to hold out, that may not work out all that well for

you," Pitell said.

That's because when many surrounding landowners have already signed leases with one company, others will have little use for the remaining isolated parcels.

But Pennsylvania still has some significant advantages in the marketplace, Pitell added. While it's true that companies could move some drilling operations to New York, West Virginia or Ohio, they'd have to build up infrastructure there to do so.

Pennsylvania has significant infrastructure in place now, in terms of well pads and a growing network of pipelines and processing stations.

"Once they have that infrastructure in place, they want to feed that infrastructure," Pitell said of drilling companies, noting that to justify moving a drilling rig "the geology is going to have to prove that it makes sense for them to potentially abandon development in a given area, and move to New York" or some other state.

Klaber agreed that the growth of pipeline networks and mergers in that industry will create more ways to deliver gas to customers. But she noted that some widely discussed possibilities, such as the Shell plant, will take years to permit and build.

But there's no question the quantity of gas produced from the Marcellus is increasing rapidly. In 2010, the industry estimated Marcellus production to be the equivalent of 1.3 billion cubic feet per day. By the end of 2012 it is projected to be more than 6 billion cubic feet per day.

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