

**NOTICE OF FINAL RULEMAKING
DEPARTMENT OF ENVIRONMENTAL PROTECTION
ENVIRONMENTAL QUALITY BOARD
[25 PA CODE CH. 78]
OIL AND GAS WELL FEE AMENDMENTS**

The Environmental Quality Board (Board) by this order amends §§ 78.1 and 78.19 (relating to definitions; and permit application fee schedule) to read as set forth in Annex A. These amendments satisfy the obligation of the Department of Environmental Protection (Department), as specified in § 78.19(f), to provide the Board with an evaluation of the Chapter 78 fees and recommend regulatory changes to address any disparity between Oil and Gas Program (Program) income generated by the fees and the Department's cost of administering the Program. These amendments include several changes to the structure of oil and gas well permit fees, including establishing increased flat fees for unconventional well permits.

This final-form rulemaking was adopted by the Board at its meeting of January 21, 2014.

A. Effective Date

These amendments will go into effect upon publication in the *Pennsylvania Bulletin* as final rulemaking.

B. Contact Persons

For further information, contact Kurt Klapkowski, Director, Bureau of Oil and Gas Planning and Program Management, Rachel Carson State Office Building, 15th Floor, 400 Market Street, P. O. Box 8765, Harrisburg, PA 17105-8765, (717) 772-2199; or Trisha Salvia, Assistant Counsel, Bureau of Regulatory Counsel, P.O. Box 8464, Rachel Carson State Office Building, Harrisburg, PA 17105-8464, (717) 787-7060. Persons with a disability may use the AT&T Relay Service, (800) 654-5984 (TDD users) or (800) 654-5988 (voice users). This final-form rulemaking is available electronically on the Department of Environmental Protection's (Department) web site at www.dep.state.pa.us (DEP Search/Keyword: Public Participation).

C. Statutory Authority

The final-form rulemaking is being made under the authority of 58 Pa.C.S. § 3274 (relating to regulations) which directs the Board to adopt regulations necessary to implement 58 Pa.C.S. Chapter 32 (relating to development), 58 Pa.C.S. § 3211(d) (relating to well permits), which authorizes the Board to establish permit fees that bear a reasonable relationship to the cost of administering 58 Pa.C.S. Chapter 32, and section 1920-A of The Administrative Code of 1929 (71 P. S. § 510-20), which authorizes the Board to promulgate regulations of the Department.

D. Background of the Amendments.

Applicants for permits to drill oil and gas wells in this Commonwealth shall pay the permit fee established by the Board. These permits fees fund the entire operation of the Department's Office of Oil and Gas Management (Oil and Gas Program), which is responsible for Statewide oil and gas conservation and environmental programs to facilitate the safe exploration, development and

recovery of Pennsylvania's oil and gas reservoirs in a manner that will protect this Commonwealth's natural resources, the environment and public health, safety and welfare. The permit fees are placed in the Well Plugging Fund.

The Department prepared and presented to the Board a 3-Year Regulatory Fee and Program Cost Analysis Report (Report) as part of this rulemaking. A copy of the Report is available from the persons listed in Section B. The conclusions of the Report are outlined below.

The Well Plugging Fund balance is declining as the Department's expenses to operate the Program have exceeded permit fee revenues for the past several fiscal years. Fiscal Year (FY) 2011-12 revenues totaled \$13.5 million and expenditures exceeded \$16.6 million. The Program is projected to have increasing expenditures with declining revenues in future fiscal years, which will continue to deplete the existing fund reserves. At current permit fee and expenditure levels, with projected permitting levels, the Well Plugging Fund will be insufficient to maintain the operations of the program through FY 2015-16.

In addition to declining Well Plugging Fund balances, the Program is facing increasing operational expenditures due to increased activity in the area of oil and gas exploration associated with previously unexplored unconventional gas formations, as well as the development of natural gas infrastructure throughout this Commonwealth. These expenditures are only expected to increase as exploration of other unconventional formations and infrastructure development expands.

These amendments increase the well permit fee to provide adequate revenue to support the ongoing operations of the Program as well as to meet future Program needs, including permitting, inspection, enforcement and information technology needs. Compounding the problem of declining funds due to increasing expenditures is the decrease of well permit applications. Since 2010, the Department has experienced a year-over-year decrease in the number of unconventional well permit applications received. The decline in permit applications is met with declining revenues but with the passage of the act of February 2, 2012 (P. L. 67, No. 9) and the act of February 14, 2012 (P. L. 87, No. 13), the overall responsibility of the Program has increased. It is imperative that the Department has the resources and technology necessary to ensure industry compliance and environmental protection as Office of Oil and Gas Management responsibilities in this area continue to expand.

This increase in workload coupled with declining permit revenues creates a situation where the incoming permit revenue is insufficient to cover the current operational costs of the Program, not allowing any room for flexibility in terms of future staff and resource needs. As the oil and gas industry continues to expand in this Commonwealth, additional Department staff and technology will be critical to ensure the Department's proper oversight of the industry.

Two areas where this increased workload and expenditures make this permit fee increase critical are streamlined electronic review and staffing.

Streamlined Electronic Review

The Department will allocate a substantial portion of the increased fee revenue to Information Technology projects for the Program, such as electronic permitting, mobile digital inspections, upgrades to existing reporting systems and modernization of forms and databases. This investment in technology will yield efficiencies for both the Department and the regulated community in terms of more predictable and timely permit issuance, more effective site inspections, increased availability of staff for compliance assistance, and more streamlined reporting to and communication with the Department. It will also make the Department's work more transparent to the public as electronic documents can be easily made available on the Internet. The two key initiatives on the forefront of information technology priorities for the Department are the ePermitting initiative and enabling staff with devices and the capability to conduct mobile digital inspections.

The ePermitting system will provide the ability to process applications for oil and gas permits online. The new system will replace the manual process that requires applicants to complete paper forms and deliver multiple copies of documentation to a Department district office. This change should reduce data transcription errors from entering data on paper forms into the Department's databases. The new ePermitting system is designed to increase review efficiency through electronic workflow and to significantly decrease the time from initial application submission to permit issuance. It will enable applicants to submit online payment and provide for permit review transparency as an applicant will be able to closely follow a permit through the approval process and receive automatic notifications as it completes the outlined benchmarks. Upon approval, the system will deliver the permit electronically to the applicant, thereby eliminating the lag time from permit issuance to receipt by the applicant.

Electronic receipt and storage of the permitting documents will also result in significant savings in terms of storage and of staff time and costs associated with related Right-to-Know requests. The Department is second in the Commonwealth in terms of Right-to-Know requests, much of which is attributed to the Program. The public will enjoy greater access to timely data as the Department receives it.

Creation and deployment of a mobile digital inspection platform and mobile devices will create marked improvement and efficiencies in terms of how the organization conducts site inspections. Current paper based inspection forms necessitate staff spending at least 1 day a week in the office to manually enter data from paper inspection reports and mail the resulting inspection report and findings to operators. Mobile digital inspections will allow entry of data into the system while onsite, eliminate the need to return to the office for data entry and enable employees to spend their time where they are needed, on location for inspections and compliance assistance.

Staffing Needs

Currently, there are 202 full time equivalents (FTE) assigned to the Office of Oil and Gas Management. The Program has grown considerably; in 2004 the Program had 64 FTEs. Approximately 80% of the current staff is assigned to engineering, scientific or

permit/inspection-related work, as oil and gas inspectors or oil and gas inspector supervisors. Another 20% are assigned to clerical, administrative or legal work to support the Program.

The Department is proposing that additional positions are needed within the Office of Oil and Gas Management to implement the additional responsibilities required under 58 Pa.C.S. Chapter 32 to review well pad and pipeline development permit applications in an efficient and timely manner and to support the Bureau of Oil and Gas Planning and Program Management.

Chapter 32 of 58 Pa.C.S. comprehensively amended the Oil and Gas Act of 1984 and established a number of new responsibilities on the oil and gas industry as well as the Department. Under 58 Pa.C.S. Chapter 32, the Department must inspect well sites before drilling can begin and well drillers must now notify the Department prior to cementing all strings of casing and before hydraulic fracturing operations begin. These new requirements have stretched thin the current staff and therefore necessitate additional inspectors to fulfill the increased inspection requirements and expectations of 58 Pa.C.S. Chapter 32. Absent additional inspection staff, well sites will not be inspected at the frequency envisioned by 58 Pa.C.S. Chapter 32.

In addition to responding to new requirements, additional staff is needed to timely review the increase in permits received by the Department due to substantial natural gas infrastructure development throughout this Commonwealth. Failure to review permit applications within a reasonable time period can result in substantial cost increases for these projects and ultimately prevents natural gas from reaching consumers, thus increasing commodity costs.

Finally, as a result of the Department's 2011 reorganization, the Office of Oil and Gas Management was created to unify the planning and program management staff with the permitting, inspection and enforcement staff under a common Deputate. As a result of this reorganization, additional staff is necessary to support the Office of Oil and Gas Management's Bureau of Oil and Gas Planning and Program Management. These additional staff will enable the Office of Oil and Gas Management to better develop new regulations, policies and technical guidance documents pertaining to well construction and surface activities on a timely basis. Failure to promptly develop these rules and policies can lead to uncertainty and inconsistent application of 58 Pa.C.S. Chapter 32. Additional staff will better serve the public as well as the industry by making more transparent how the Department interprets and implements 58 Pa.C.S. Chapter 32.

Without additional revenue provided by a regulatory fee package, additional staff complement will not be possible, which will jeopardize the Department's ability to provide high quality compliance assistance, ensure timely permitting, ensure adequate inspection and enforcement operations, and leverage existing technology to streamline inspection and permitting activities.

The Department consulted with the Oil and Gas Technical Advisory Board (TAB) in the development of the proposed rulemaking. The Department presented the draft proposed rulemaking to TAB at its April 23, 2013, meeting. Because the proposed rulemaking did not address technical issues relating to oil and gas, TAB did not take a formal action relative to the proposed rulemaking.

E. Summary of Regulatory Requirements

Current Fee Structure

The current permit fee structure is outlined in § 78.19 and establishes three classes of wells. Two are based on the type of wellbore that will be used to produce oil or natural gas—vertical or nonvertical (deviated or horizontal) and the third is based on the Marcellus Shale being the target formation. Permit fees for an individual well are determined by use of a sliding scale based on the total well bore length in feet. The sliding scales for the nonvertical and Marcellus wells are identical and are roughly two to three times the fee paid for a vertical well of the same total well bore length. As an example, an applicant requesting a permit for a 5,000-foot vertical well pays a fee of \$550, while an applicant for a nonvertical or Marcellus Shale well of the same well bore length would pay \$1,600. The current average nonvertical unconventional well permit fee is approximately \$3,200 and the current average vertical unconventional well permit fee is \$2,900.

Amended Fee Structure

The final-form rulemaking amends § 78.19 to create two classes of wells for permit fee purposes. These classes are “conventional wells” and “unconventional wells.” These amendments follow the general structure of 58 Pa.C.S. Chapter 32, which established the “conventional vs. unconventional well” distinction in a number of different areas. For example, 58 Pa.C.S. § 3215 (relating to well location restrictions) establishes differing setback requirements for the two classes of wells and 58 Pa.C.S. § 3218 (relating to protection of water supplies) establishes differing presumptions of liability for the two classes of wells.

It is important to be clear that the final-form rulemaking does not include any changes to the current permit fee structure for applicants for permits to drill “conventional” oil and gas wells. Although “conventional” wells and formations are not defined in 58 Pa.C.S. § 3203 (relating to definitions), the amendments to § 78.1 define those terms with reference to definitions in 58 Pa.C.S. § 3203 of “unconventional well” and “unconventional formation.”

By reviewing the “unconventional” definitions, “conventional wells” include: (1) any wells drilled to produce oil; (2) wells drilled to produce natural gas from formations other than shale formations; (3) wells drilled to produce natural gas from shale formations located above the base of the Elk Group or its stratigraphic equivalent; and (4) wells drilled to produce natural gas from shale formations located below the base of the Elk Group where natural gas can be produced at economic flow rates or in economic volumes without the use of vertical or nonvertical well bores stimulated by hydraulic fracture treatments or by using multilateral well bores or other techniques to expose more of the formation to the well bore. For permit applicants to drill these wells, these amendments do not have any impact.

Permit applicants for conventional wells will not see an impact from these amendments because the rulemaking retains the current “vertical well” fee structure as the new “conventional well” fee structure. Typically, “conventional wells,” as defined in this final-form rulemaking, would pay the “vertical well” fee if permitted prior to these amendments taking effect.

For “unconventional nonvertical wells” and “unconventional vertical wells,” these amendments establish flat permit fees of \$5,000 and \$4,200, respectively, regardless of the total well bore

length of the well. The Department determined that this increase will enable the Department to operate the Program in the manner contemplated by the current rules and regulations, as well as undertake the initiatives previously described.

F. Summary of Comments and Responses on the Proposed Rulemaking and Changes to the Proposed Rulemaking

The Board received comments from six commentators and the Independent Regulatory Review Commission (IRRC) during the 30-day public comment period. Four commentators, including the Pennsylvania Independent Oil and Gas Association and IRRC, suggested adding more detail to the proposed definition of “conventional well.” This suggestion was accepted and this final-form rulemaking contains the additional detail in section 78.1.

Two commentators explicitly supported the concept of fee increases, with one requesting that the fee be doubled above what was proposed. One commentator was opposed to fee increases to support staffing increases until such time as the Department’s electronic permitting initiative is in place and the efficiencies gained from that development can be assessed. This comment fails to acknowledge the additional responsibilities placed on the Department by Acts 9 and 13 of 2012 as well as the expanding universe of regulated oil and gas wells (more wells are permitted and drilled each year than are plugged so the regulated universe continues to expand), as well as the infrastructure development oversight carried out by the Office of Oil and Gas Management. As noted above, the Department has conducted a thorough analysis of the program’s current resources and expenditures, as well as future requirements necessary to carry out the Program’s responsibilities under the statutes of the Commonwealth and believes that the fee and staff increases are adequate given the program’s needs.

G. Benefits, Costs and Compliance

Benefits

The increased oil and gas permit fee revenue would be used to adequately fund the Department's Office of Oil and Gas Management. Revenue to the Department from the fee increase would be used solely to operate the regulatory program overseeing the responsible development of this Commonwealth's oil and natural gas resources. In addition, the Department will be able to pursue streamlined electronic review initiatives and increase the Office of Oil and Gas Management staffing levels to meet the challenges of increased responsibilities and timely oversight, responsiveness and transparency. Finally, these amendments reduce the burden on the regulated community and the Department because the sliding scale permit fees, which require proper calculation and review, are replaced with flat fees that are easy to understand and implement.

Compliance Costs

Nonvertical Unconventional Wells:

The average permit fee paid for a nonvertical unconventional well or Marcellus Shale well during 2012 was approximately \$3,200 per well. The amendments establish a fixed \$5,000 fee for each nonvertical unconventional well which is an increase of \$1,800 per well. The

Department projects that approximately 2,600 well permit applications will be received annually following the effective date of this rulemaking. This would result in an additional annual incremental permit cost of \$4.68 million to the regulated community.

Vertical Unconventional Wells:

The amendments establish a fixed \$4,200 fee for each vertical unconventional well. The Department projects that approximately 80 well permit applications for vertical unconventional wells will be received annually following the effective date of this rulemaking. This would result in an additional annual incremental permit cost of \$104,000 to the regulated community.

No new legal, accounting or consulting procedures would be required.

Compliance Assistance Plan

The Department plans to educate and assist the public and regulated community in understanding these amendments and how to comply with them. This outreach initiative will be accomplished through the Department's ongoing compliance assistance program. Permit application forms and instructions have been amended to reflect the new permit fee structure.

Paperwork Requirements

There are no additional paperwork requirements associated with these amendments with which the industry would need to comply.

H. Pollution Prevention

The Pollution Prevention Act of 1990 (42 U.S.C.A. §§ 13101—13109) established a National policy that promotes pollution prevention as the preferred means for achieving state environmental protection goals. The Department encourages pollution prevention, which is the reduction or elimination of pollution at its source, through the substitution of environmentally friendly materials, more efficient use of raw materials and the incorporation of energy efficiency strategies. Pollution prevention practices can provide greater environmental protection with greater efficiency because they can result in significant cost savings to facilities that permanently achieve or move beyond compliance. The anticipated increased revenues would allow the Department to continue providing adequate oversight of the oil and gas industry in this Commonwealth, ensuring continued protection of the environment and the public health and welfare of the citizens of this Commonwealth.

I. Sunset Review

These regulations will be reviewed in accordance with the sunset review schedule published by the Department to determine whether the regulations effectively fulfill the goals for which they were intended. In addition, in accordance with § 78.19(f), the Department will evaluate these fees and recommend regulatory changes to the Board to address any disparity between the Program income generated by the fees and the Department's cost of administering the Program with the objective of ensuring fees meet all Program costs and programs are self-sustaining. This

report and any proposed regulatory changes will be presented to the Board no later than 3 years after the effective date of this final-form rulemaking.

J. Regulatory Review

Under section 5(a) of the Regulatory Review Act (71 P.S. § 745.5(a)), on _____, 2013, the Department submitted a copy of the notice of proposed rulemaking, published at 43 Pa.B. 5457, to the Independent Regulatory Review Commission (IRRC) and the Chairpersons of the House and Senate Environmental Resources and Energy Committees for review and comment.

Under section 5(c) of the Regulatory Review Act, IRRC and the Committees were provided with copies of the comments received during the public comment period, as well as other documents when requested. In preparing these final-form regulations, the Department has considered all comments from IRRC, the Committees and the public.

Under section 5.1(j.2) of the Regulatory Review Act, on _____, 2014, these final-form regulations were deemed approved by the House and Senate Committees. Under section 5.1(e) of the Regulatory Review Act, IRRC met on _____, 2014, and approved the final-form regulations.

K. Findings of the Board

The Board finds that:

(1) Public notice of proposed rulemaking was given under sections 201 and 202 of the act of July 31, 1968 (P.L. 769, No. 240) (45 P.S. §§ 1201 and 1202) and regulations promulgated thereunder at *1 Pennsylvania Code* §§ 7.1 and 7.2.

(2) A public comment period was provided as required by law, and all comments were considered.

(3) These regulations do not enlarge the purpose of the proposal published at 43 *Pennsylvania Bulletin* 5457 (Saturday, September 14, 2013).

(4) These regulations are necessary and appropriate for administration and enforcement of the authorizing acts identified in Section C of this order.

L. Order of the Board

The Board, acting under the authorizing statutes, orders that:

(a) The regulations of the Department of Environmental Protection, 25 Pennsylvania Code, Chapter 78, are amended to read as set forth in Annex A.

(b) The Chairperson of the Board shall submit this order and Annex A to the Office of General Counsel and the Office of Attorney General for review and approval as to legality and form, as required by law.

(c) The Chairperson of the Board shall submit this order and Annex A to the Independent Regulatory Review Commission and the Senate and House Environmental Resources and Energy Committees as required by the Regulatory Review Act.

(d) The Chairperson of the Board shall certify this order and Annex A and deposit them with the Legislative Reference Bureau, as required by law.

(e) This order shall take effect immediately.

E. CHRISTOPHER ABRUZZO
Chairman
Environmental Quality Board