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FISCAL IMPACT REPORT

ORIGINAL DATE 02/03/10
 LAST UPDATED 02/06/10 HB 192

SPONSOR Taylor

SHORT TITLE Rescind Oil & Gas Pit Rules SB _____

ANALYST Pava

APPROPRIATION (dollars in thousands)

Appropriation		Recurring or Non-Rec	Fund Affected
FY10	FY11		
	NFI	Recurring	General Fund

(Parenthesis () Indicate Expenditure Decreases)

SOURCES OF INFORMATION

LFC Files

Responses Received From

Dept. of Finance & Administration (DFA)
 Energy, Materials, Natural Resources Dept. (EMNRD) – Oil Conservation Division (OCD)
 Attorney General Office (AGO)
 NM Environment Dept. (NMED)

Response Not Received From

NM Oil & Gas Association

SUMMARY

Bill Synopsis:

HB 192 proposes to rescind the rules adopted by the Oil Conservation Division of the Energy, Minerals and Natural Resources Department, compiled at 19.15.2 NMAC, commonly known as the revised "pit rules". It declares an emergency for rescission of these rules to replenish state revenue reserves.

FISCAL IMPLICATIONS

There is no appropriation.

HB 192 attests that the “pit rules” have cost the state approximately \$140 million in tax revenue thus far. Further more, the rules compiled under 19.15.2 NMAC are no longer effective and an emergency should be declared for public peace, health and safety making it possible for this act to take effect immediately.

EMNRD indicates: HB 192 and the pit rules do not have the fiscal implication claimed of \$140 million lost in tax revenues. If every cubic foot of decline in NM natural gas production in 2008-9, compared to 2007, was attributed to the pit rules the production tax decline would amount to only \$70 million.

NM declines in natural gas production can be explained by price declines and the absence of new finds comparable to those in other states. Natural gas prices peaked twice in 2005 and 2008 at approximately \$13 per mcf, then fell below \$3 in 11/08. The average price in 2009 was approximately \$3.47, and the low below \$2. Oil production has not declined materially since 2005. If the pit rules were a significant cause of production declines, one would expect larger declines in oil production than in natural gas. Production trends for oil and gas correlate with price movements not pollution control costs. The price of crude oil fluctuates, but today it remains at a higher price than prior to the “bubble” in 2008.

Another reason for declining natural gas production in NM is the inevitable and natural occurring depletion of the reserve. The principal NM gas-producing basins have been active since the early 1950s. In the event 2001 was the peak year for NM natural gas production, it has declined in every year since then except for a very small increase in 2004 compared to 2003. The NE Colfax Basin began in 1999, is a small resource, and has increased steadily but is only 1% of statewide production.

Price movements have had a much more significant effect on the State’s revenues from production taxes than have production declines. The declines in production of natural gas have been small, - 4.46% in ‘08 and approximately - 4% in ‘09. The average price of natural gas declined more than 50% in ‘09 compared to ‘08.

SIGNIFICANT ISSUES

EMNRD indicates: Effect of Rescinding the Pit Rules - 19.15.17 NMAC, instead of 19.15.2 NMAC, would eliminate all rules concerning pits and below-grad tanks, leaving operators free to dispose of drilling waste in any way they choose, including unlined pits or surface dumping. The OCC’s ability to formulate new rules to prevent practices most obviously detrimental to the environment would be undermined by the Legislature’s irregular procedure of rescinding a rule.

Question of Citation & Oversight Entity- House Bill 192 attempts to repeal the pit rules adopted by the OCD as 19.15.2 NMAC. However, the rules governing oil and gas pits were not adopted by OCD, but were instead adopted by the Oil Conservation Commission (OCC), and are not compiled at 19.15.2 NMAC. The pit rules are codified at 19.15.17 NMAC. Thus it is questionable if the Legislature has the authority to rescind an executive branch rule, or whether this bill would rescind anything. There are some definitions in 19.15.2.7 that the OCC adopted at the same time it adopted the pit rule amendments, and which pertain to the pit rules. The bill may repeal only those new definitions.

However, Section 1.B of the bill purports to rescind “the rules compiled at 19.15.2 NMAC.” That would repeal all definitions applicable to all of the OCC’s rules, and would also repeal general rules providing for the operations of district offices and the issuance of emergency orders. Repeal of these definitions would leave enormous questions concerning the

application of OCC and OCD rules.

EMNRD presumes that the reference to 19.15.2 NMAC is a clerical error, and that the bill was intended to rescind the rules codified at 19.15.17 NMAC, the part of the rules which relates to pits, closed-loop systems and below-grade tanks. If 19.15.17 NMAC were rescinded in its entirety, as the bill purports to rescind 19.15.2 NMAC, that action would nullify all of OCD's rules relating to pits and below-grade tanks, leaving the construction, use and abandonment of pits and below grade tanks in oil and gas operations wholly unregulated.

Constitutional Issues - Separation of Powers - There are constitutional prohibitions on the Legislature's authority to repeal an Executive Branch rule. Under Article III, Section 1, of the Constitution, NM has always recognized and enforced a strict separation of powers among the three branches of government. HB 192 states pit rules "were adopted without legislative approval." Legislative approval of particular rules is neither usual nor contemplated in the dynamics of separation of powers. The pit rules are clearly within the OCC's statutory rule-making authority. The Legislature, by enacting NMSA 1978 Sections 70-2-12.B (15), (21) and (22), gave OCC general power to adopt rules governing the disposition of oil and gas waste for the purpose of protecting public health and the environment. Parties who have challenged the pit rules in court have not contended they are not within the purview of these statutory authorizations. The members of the OCC are full time professionals in relevant disciplines (petroleum engineering, hydrology and geology). It is their function, and that of the Executive Branch to evaluate technical evidence and determine sound governance.

Scientific Basis and Environmental Benefit of the Pit Rule - HB 192 statements that the pit rules "have no scientific basis" and "provide no environmental benefit" are incorrect. The OCC held 25 days of public hearings for the rules and amendments, comprising 15,000 pages, with testimony from diverse expert witnesses. Though the pit rules are lengthy and complex, many provisions are not controversial such as the prohibition of unlined pits and the necessary thickness of pit liners. Concern centers on the allowable maximum levels of contaminants, particularly chlorides, in wastes left in place. The testimony on this was extremely technical, but it rebuts the unfounded assertion that the rules have no scientific basis.

Random sampling of oil and gas pits found contaminant concentrations exceeding WQCC's ground water quality standards. Chlorides were identified in very large concentrations in all pits sampled in SE New Mexico. The oil and gas industry's hydrologist described computer modeling studies that predicted high concentrations of chlorides in pits that would eventually reach ground water, even if the degree of contamination was in question. Pit rules were based on extensive scientific evidence which no expert witness dismissed as frivolous. The OCC only adopted the OCD's recommendations with qualifications and numerous changes proposed by the industry.

AGO indicates: HB 192, if enacted, would be a "special law" and vulnerable to challenge under Article IV, Section 24 of the State Constitution. Article IV, Section 24, in pertinent part, prohibits the enactment of special laws "where a general law can be made applicable." Although HB 192 makes it clear that the legislature does not have approval authority over OCD's pit rules, it contains no guidance for OCD regarding what its regulations should state.

Thus, it is possible that OCD could adopt subsequent rules, in good faith, that do not comport with the legislature’s intent. The better course would be to amend the underlying law to make the Legislature’s intent clear. In other words, draft a law stating exactly what the Legislature wants and leave no room for interpretation by the agency.

NMED indicates: Ninety percent of New Mexicans rely on groundwater as their primary source of drinking water. It is significantly cheaper to prevent groundwater contamination through such rules, than to pay for the cleanup of groundwater after it’s contaminated. Even if a company had sufficient funds for cleanup, it is nearly impossible to restore a contaminated aquifer to its original quality. Protection of groundwater quality is a priority for OCD and NMED.

In one year, 369 pits had caused ground water contamination according to OCD’s records from 2008. The assertion that the pit rules are responsible for the decline in oil and gas production and revenue is unfounded. The oil and gas industry’s own data show that it is the price of oil and natural gas that determines the level of production, and that the dip in New Mexico’s production due to a collapse in prices has been similar to other western states, particularly Wyoming.

PERFORMANCE IMPLICATIONS

EMNRD notes: If the bill passes in its current form, OCD will be seriously hampered in every attempt to administer or enforce its rules by the uncertainty the bill will cause about the meaning of all terms, if the definitions currently in 19.15.2 NMAC are rescinded. If the bill is amended to instead rescind 19.15.17 NMAC, OCD will be left without the ability to protect groundwater for suitable drinking water, and mitigate the risks of serious environmental contamination resulting from oil field wastes.

TECHNICAL ISSUES

HB 192 as introduced does not affect or change any other part of OCC or OCD rules except 19.15.2 NMAC. However, HB 192 could have intended to refer to other parts of OCC rules, specifically 19.15.17 NMAC, as well as.

ALTERNATIVES

EMNRD notes: Allow the courts to determine whether the pit rule amendments are supported by substantial evidence.

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

OCD’s pit rules will remain in effect. Use of pits and below-grade tanks will continue to be adequately regulated, and the water resources of the State will be protected from contamination caused by improper management of oil field wastes.