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August 10, 2018

The Honorable Patrick McDonnell, Chairman
Environmental Quality Board
16th Floor Rachel Carson State Office Building
P.O. Box 2063
Harrisburg, PA 17105-2063

Re: Proposed Rulemaking: Unconventional Well Permit Fee Increase (#7-542) – via electronic submission to cComment@pa.gov, RegComments@pa.gov and hand delivery

Dear Chairman McDonnell:

The Marcellus Shale Coalition (MSC) was formed in 2008 and is comprised of approximately 200 producing, midstream, transmission and supply chain members who are fully committed to working with local, county, state and federal government officials and regulators to facilitate the safe development of natural gas resources in the Marcellus, Utica and related geological formations. Our members represent many of the largest and most active companies in natural gas production, gathering, processing and transmission in the country, as well as the suppliers and contractors who service the industry.

Introduction

The MSC and its member companies recognize the importance of having a robust, professional oil and gas program with sufficient resources to fulfill its statutory obligations and ensure the protection of our shared natural resources. The unconventional natural gas industry has expressed its understanding of the need for new revenues during both the 2009 and 2013 permit fee increases, and supported each. Additionally, the unconventional natural gas industry has paid nearly \$1.5 Billion since 2012 under the Act 13 Impact Fee¹ with \$42 Million to date going to the Department of Environmental Protection (DEP or department) for industry oversight.

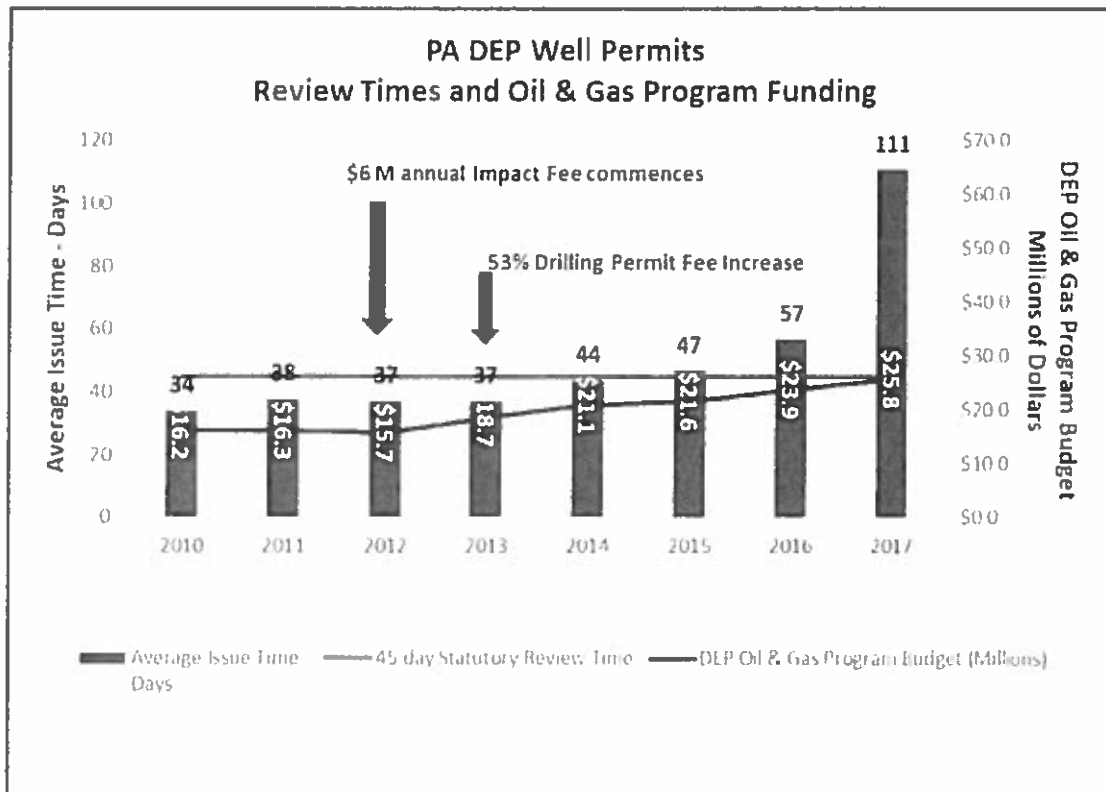
However, the proposed permit fee increase from the current \$5,000 per unconventional well application to \$12,500 per unconventional well application – representing a 150% increase – is excessive and not proportional to the costs incurred by the oil and gas program to oversee the unconventional natural gas industry. Additionally, excluding the department's \$6 Million Impact Fee allocation from the oil and gas program's operating budget seems counterintuitive to the purposes for which these revenues were intended.

¹ Act 13 of 2012

Well Permit Review Times

The Pennsylvania Oil and Gas Act requires the department to issue an oil or gas permit within 45 calendar days, unless the permit fails to satisfy one or more specific provisions of the Act.² Historically, the department has generally met this statutory obligation. However, in recent years – most noticeably calendar year 2017 – permit issuance timeframes have increased exponentially. For example, in 2013 the average time to issue an unconventional natural gas permit was 37 calendar days. In 2017, this average time had increased to 111 calendar days, or by 200%.

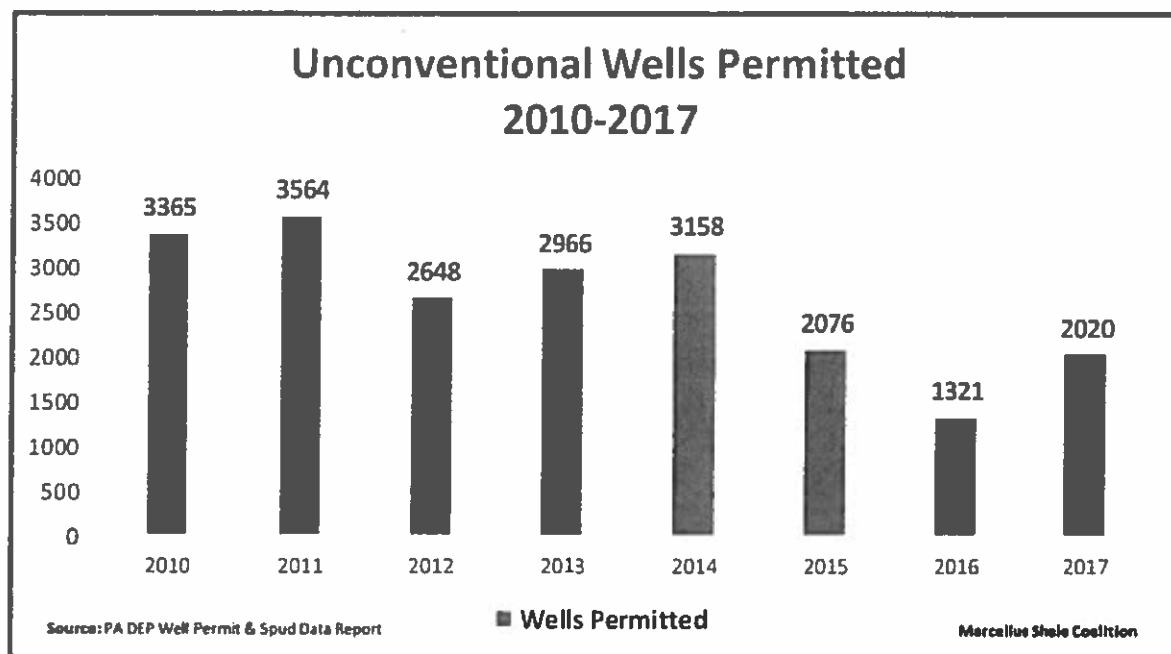
The chart below shows the average time to review and issue an unconventional well permit, overlaid with the annual operating budget of the oil and gas program, since the initial unconventional well permit fee increase in 2010:



This massive increase in permit review and issuance time came during a period of significant economic decline within the natural gas industry, and a commensurate decline in the number of permit applications submitted to the department. For example, in calendar year 2013 the department issued 2,966 unconventional natural gas permits; permits issued declined to a low of 1,321 in calendar year 2016, before rebounding to 2,020 last year. While review times have improved in calendar year 2018, they essentially have returned to review times already mandated by state law and if not properly managed, can revert to the significant delays of prior years.

² 58 Pa.C.S. §3211(e)

The following chart illustrates the annual number of unconventional natural gas permits issued by the department since 2010, by calendar year:



As demonstrated in the two preceding charts, prior increases in funding for the oil and gas program historically have not reduced or even maintained well permit review times, even as the permit review workload has decreased substantially. The operators who will be required to remit a significantly higher fee under this proposal remain concerned that there are no assurances of improved permit review and issuance timeframes, as it is clear that the regression in permit review times experienced over the past several years was not attributable to a lack of financial resources.

Statutory Authority & Unconventional Industry Workload

The statutory authority³ for PA DEP to impose and collect a permit fee states the following:

Each application for a well permit shall be accompanied by a permit fee, established by the Environmental Quality Board, which bears a reasonable relationship to the cost of administering this chapter.

It is important to note that this statutory authority does not in itself distinguish between unconventional and conventional well permits; rather the department is granted authority to collect a permit fee along with “each application for a well permit.” The MSC believes it is reasonable for the department to distinguish between conventional and unconventional permit

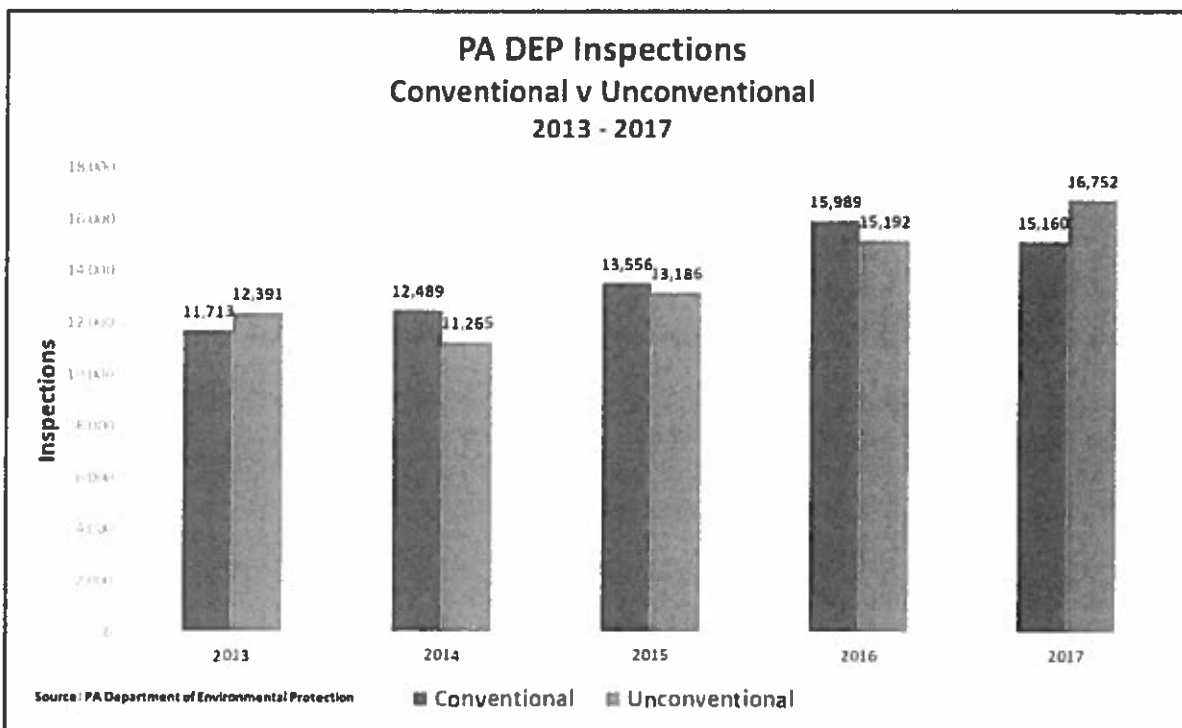
³ 58 Pa.C.S. §3211(d)

application fees. However, what the department *cannot* do is apply selectively the qualification that such fee “*bears a reasonable relationship to the cost of administering this chapter.*”

The MSC contends that PA DEP’s authority to levy a permit fee to accompany unconventional well permit applications must bear a reasonable relationship to the costs of administering the department’s obligations related to the *unconventional* natural gas industry and not subsidize the department’s obligations related to the conventional industry. The “3-Year Regulatory Fee and Program Cost Analysis Report” submitted by the department to the Environmental Quality Board (EQB or Board), and discussed at the Board’s April 2018 public meeting, provides a history of the Pennsylvania oil and gas program, history of permit fee increases, workload analysis, new policy initiatives, cost saving measures and finally the recommendation to increase the unconventional permit fee by 150%, to \$12,500 per application. However, what is noticeably absent from this report is a detailed analysis that examines the proportional costs incurred by the department to oversee the conventional oil and gas program.

As the department is aware, the Commonwealth has a long history of developing conventional oil and natural gas resources, and currently has over 65,000 active conventional oil and natural gas wells. These wells require a host of ongoing oversight obligations for the department staff, including site inspections to ensure the environment and local natural resources are protected, review of new permit applications, annual production submission, review of mechanical well integrity and other requirements.

The following chart illustrates the inspection workload relative to conventional and unconventional activities over the past five years:



The MSC believes that the program cost analysis prepared for the EQB, and available for review as part of the consideration of this rulemaking, should examine not only the oil and gas program's total costs, but the *proportional* costs as well which examine the costs borne by the program for oversight of the unconventional industry, the conventional industry, and ongoing legacy industry costs. For example, according to the department's own data, in calendar year 2016 approximately 51% of all inspections were conducted on conventional oil and gas well sites, demonstrating a significant resource commitment obligation of the program for non-unconventional industry activity.

While acknowledging that the overwhelming majority of new permit review work is related to unconventional well permit applications, it seems wholly disproportionate for the department to generate over 99% of its overall oil and gas program revenue from just one sector of the industry.⁴ The MSC does not endorse an increase in the conventional well permit fee – and recognizes that doing so would generate little revenue anyway given the lack of new permit applications. However, this reality strongly endorses the concept that some proportion of the oil and gas program's budget should be derived from sources other than the unconventional natural gas industry. Indeed, no other program relies solely on permit fees from one segment of one industry to fund its operations.

In summary, the costs borne by the unconventional natural gas industry to support the oil and gas program should bear some proportionality to the revenue (permit fees and Act 13 Impact Fees) the unconventional natural gas industry is required to pay. The MSC believes that the department is statutorily bound to ensure that the *unconventional* oil and gas permit fee bear a reasonable relationship to administering the *unconventional* responsibilities of the department as outlined in the Oil and Gas Act. This proportionality is not reflected in the current fee increase proposal and not consistent with the statutory authority of the Oil and Gas Act to establish a permit fee for the unconventional oil and gas industry.

General Fund Appropriation

Prior to the onset of significant Marcellus Shale activity in the Commonwealth, the oil and gas program received approximately 15% of its revenue from well permit fees and 85% from General Fund appropriations allocated to the program by DEP management. As significant unconventional activity ramped up, around 2008 and continuing to the present day, the oil and gas program transitioned to relying on permit fees, Act 13 Impact Fees, fines and penalties for 100% of its revenue. The program currently receives no General Fund support.

The MSC believes that some level of General Fund support for the oil and gas program is warranted. Most if not all other programs within the department rely upon a General Fund allocation, while relying upon permit fees from the regulated community for a portion of the program's operating revenue. For the current fiscal year, the General Assembly has appropriated

⁴ According to PA DEP, in 2017 conventional oil and gas permit revenue accounted for approximately \$61,050, translating to the unconventional natural gas industry paying 99.76% of total program costs.

nearly \$140 Million⁵ in General Fund general operating revenue for the department. Governor Wolf's proposed budget also included \$2.5 Million in new General Fund appropriations to support an additional 35 department employees dedicated to permit review and environmental enforcement. None of these positions are allocated by PA DEP to the oil and gas program. It is clear, therefore, that failure to allocate General Fund appropriations to the oil and gas program is a policy choice of the Administration. This policy choice undermines the alleged need to raise unconventional well permit fees by 150%, and should not result in one industry sector facing the imposition of excessive and prohibitive permit fees.

The MSC estimates that approximately 60% of the PA DEP Oil and Gas Program's work is related to the unconventional shale gas industry, with the balance of work related to oversight of the conventional oil and gas industry and inspection of legacy wells that are the responsibility of the department. The unconventional shale gas industry is already paying in excess of 99% of the total costs to underwrite the PA DEP oil and gas program. Therefore, from a practical perspective, this means that the proposed permit fee increase for unconventional operators is tantamount to underwriting the costs associated with the conventional industry and legacy well costs incurred by the department. While the MSC reiterates that its members do not support a permit fee increase for conventional oil and gas permit applications, this reality does support the case for allocating a portion of the department's \$140 Million General Fund appropriation to the oil and gas program. Identifying an appropriate mix of funding sources, including General Fund dollars, is all the more crucial considering the department has already acknowledged that even this proposed 150% permit fee increase may not be adequate to fund the program.⁶

Lack of Proper Reimbursement from Department Special Funds

Prior to imposition of higher permitting fees on the unconventional natural gas industry, the department should evaluate and provide transparent information to industry, the Independent Regulatory Review Commission (IRRC), the standing legislative oversight committees and the public regarding other potentially available sources of funding, including from special funds administered by the department.

For example, the MSC understands that nearly half of the authorized employee complement of the oil and gas program⁷ administers permit reviews and inspections related to the administration of the erosion and sediment control and dam safety and encroachments programs⁸ (Ch. 102 and Ch. 105 programs). According to the department, permits related to the Ch. 102 and Ch. 105 programs tied to the unconventional natural gas industry generate approximately \$2-\$4 Million in revenue annually. These permits cover activities such as access road and well site construction, pipeline and impoundment construction, and waterway encroachment and crossings.

⁵ General Appropriation Act of 2018 (Act 1A of 2018):

<http://www.legis.state.pa.us/cfdocs/legis/PN/Public/btCheck.cfm?txtType=PDF&sessYr=2017&sessInd=0&billBody=H&billTyp=B&billNbr=2121&pn=3747>

⁶ PA DEP Regulatory Analysis Form Item (10): "Thus, it is entirely foreseeable that the current fee proposal will not be adequate to fund the Program." (pg. 3)

⁷ According to PA DEP, the oil and gas program has an authorized complement of 190 employees.

⁸ 25 PaCode Ch. 102 & 25 PaCode Ch. 105, respectively

The revenue generated from the Ch. 102 and Ch. 105 permits is deposited in the Clean Water Fund and the Dam and Encroachments Fund, respectively. While the costs incurred to review and issue permits and conduct inspections and enforcement activities were borne by employees of the oil and gas program, the MSC understands that none of this revenue was transferred to the oil and gas program as reimbursement.

Conversely, other programs within PA DEP did request and receive reimbursement from the oil and gas program for services rendered. For example, in Fiscal Year 2016-2017, nearly \$795,000 was transferred from the oil and gas program to reimburse the Information Technology program within the department. This inconsistency in how the department administers its special funds and reimburses various programs from accounts segregated from an individual program's direct control should be thoroughly examined and rectified to ensure that all permit fees paid by the regulated community are properly credited.

As currently understood, it appears that the oil and gas industry is paying several million dollars in permit fees that are not being credited to the oil and gas program, thus in part necessitating – in the department's eyes – a 150% well permit fee increase. This lack of proper reimbursement certainly influences and affects the program's revenue gap, and thus proposed permit fee increase.

Many other industries regulated by PA DEP, such as agriculture, timber, and certain construction activities are able to obtain Ch. 102 and Ch. 105 program permits through county conservation districts. Most oil and gas operators do not have this option. Given that oil and gas program employees conduct the bulk of these permit reviews, it may be appropriate for the department to consider allowing this option and thus freeing up the workload of oil and gas program employees.

Adherence to Regulatory Review Act

The Regulatory Review Act (RRA) requires an agency promulgating a rulemaking to prepare and submit a Regulatory Analysis Form (RAF) which shall consider the impacts of the proposed rulemaking on small businesses.⁹ Included in the RAF is the requirement to prepare and submit a regulatory flexibility analysis that minimizes the adverse impacts on small businesses. Under the RRA, a small business engaged in natural gas extraction is defined as an entity which employs 1,250 or fewer employees.¹⁰

The majority of companies engaged in unconventional natural gas extraction within Pennsylvania, and therefore subject to this rulemaking, meet the definition of a small business. For example, nearly 74% of the exploration and production companies which obtained an unconventional well permit from PA DEP in 2017-2018 meet the definition of a small business.¹¹

⁹ Act 181 of 1982 §5(a)

¹⁰ Title 13 Code of Federal Regulations §121.201 – NAICS Code 211130

¹¹ MSC analysis of PA DEP unconventional permits issued: January 1, 2017 – June 30, 2018



Approximately 58% of the permits issued during this timeframe were to small businesses.¹² Therefore, the department's assertion in items (15) and (16) of the RAF is incorrect. Moreover, the RAF does not include the requisite flexibility analysis related to these small businesses; instead the department merely notes the (incorrect) percentage of affected industry operators that it believes qualify as small businesses under state law. As such, the RAF as submitted by the EQB related to the obligations to minimize the impacts on small businesses has not been addressed sufficiently and should be revised and resubmitted so that the regulated community can properly understand the considerations to be made for these small businesses, and comment accordingly. Additionally, failure to accurately represent the proportion of small businesses affected by this proposed fee increase and to prepare the required flexibility analysis raises questions regarding the department's appreciation of the impacts of its proposal on small businesses.

Demonstration of Need

Item (10) of the RAF asserts that the lack of staff resources has led to important program development initiatives being put on hold. However, just since 2016 DEP has finalized a comprehensive re-write of its regulations pertaining to unconventional wells (Chapter 78a), an Area of Review technical guidance document, a Replacement or Restoration of Private Water Supplies technical guidance document, new Guidelines for the Development of Operator Pressure Barrier Policy, and new Guidelines for Chain (Coal) Pillar Development and Longwall Mining Adjacent to Unconventional Wells among other initiatives. The MSC is hard-pressed to understand the need to promote even more program initiatives given that the pace of new policies and initiatives has only accelerated in recent years.

Additionally, the department appropriately has touted the improved efficiencies of utilizing iPads and an associated online application for electronic field inspections. According to the department, all 78 inspectors are either using the application currently or will be in the very near future. The Governor's Office estimates the savings from use of the electronic application to be approximately \$10,300 per inspector, which translates into a savings of over \$800,000 for the DEP oil and gas program.¹³

Ironically, the department fails to note the improved efficiencies and cost-savings of this initiative in the RAF.

Competitive Impact

The RRA charges IRRC to consider the adverse economic or fiscal impacts of a rulemaking on competition.¹⁴ Under this proposed rulemaking, Pennsylvania would impose the highest well permit fee in the United States.

¹² Ibid

¹³ Governor's Office of Transformation, Innovation, Management and Efficiency: <https://www.governor.pa.gov/go-time-new-ipad-app-makes-dep-oil-and-gas-site-inspections-more-efficient/>

¹⁴ Act 181 of 1982 §5.2(b)(1)(ii)

The following illustrates oil and gas well permit fees imposed by several leading production states that are competing with Pennsylvania for limited capital investment in oil and gas extraction:

State	Permit Fee
Pennsylvania	\$12,500/proposed \$5,000/current
Arkansas	\$300
Colorado	FREE
New Mexico	FREE
Ohio	\$500 - \$1,000
Oklahoma	\$175
Texas	\$500 - \$750
West Virginia	\$10,000/initial \$5,000/additional on pad

*The permit fee imposed by West Virginia for the initial well on a well pad represents the cost to review the engineering design related to well site construction and storm-water management. Pennsylvania reviews this work under a separate and distinct permit requirement, the Erosion and Sediment Control General Permit,¹⁵ which is subject to its own permit fee and preparation costs.

The requirement to consider the impacts on Pennsylvania's competitive economic climate compared to other states is also contained in Executive Order 1996-1, related to Regulatory Review and Promulgation. Specifically, the Executive Order requires agencies to adhere to the principle that regulations "shall not hamper Pennsylvania's ability to compete effectively with other states."¹⁶

National reports on industry investments show clear trends of increased land acquisitions and operations in the Permian Basin in Texas and New Mexico, where permit fees are substantially less costly than Pennsylvania's *existing* well permit fee and permit turnaround is 5 days, contrasted with the 111 day average review time Pennsylvania operators experienced in 2017. Given the department's proposal to increase the fee by 150%, the net effect will only be to make Pennsylvania more of an outlier and more poorly positioned from a competitiveness standpoint. It is therefore questionable whether DEP performed its due diligence to catch this obvious red flag and factor that into consideration of whether a 150% well permit fee increase would ultimately result in more or less industry investment in the Commonwealth.

It is important to note that the RAF prepared by the department only examines the competitiveness of fees in four states adjacent to Pennsylvania, two of which have legal

¹⁵ 25 PaCode §102.5(c)

¹⁶ Executive Order 1996-1 §1(l)

prohibitions on unconventional well development (New York and Maryland).¹⁷ PA DEP has failed to include relevant information, as cited in the chart above, of the Commonwealth's competitive balance relative to other unconventional oil and natural gas producing states. Moreover, PA DEP failed to provide context to the EQB and to the public regarding the scope of the permit fee imposed by West Virginia; notably that the first well permit application on a pad also contains the erosion and sediment control review and other engineering criteria related to stormwater management for the well pad itself, and that Pennsylvania imposes a separate permit requirement (and fee) outside of the well permit application for this process, namely the Erosion and Sediment Control General Permit requirement.¹⁸

Finally, from a competitive standpoint it is imperative to recognize that unconventional operators in Pennsylvania are constantly striving to improve efficiencies and lower costs in an effort to overcome chronic price differentials in the Commonwealth, compared to other natural gas-producing basins in the country. This fee increase, coupled with higher fees for air quality permits and the imposition of a new air quality permit for well sites (GP-5a), exacerbates the competitive imbalance within basins.

Cost of Compliance Error

In addition to failing to represent accurately the competitive impact of the fee increase with other states, Item (12) of the RAF incorrectly calculates the percentage increase of the proposed fee increase on the overall cost of drilling an unconventional well. The department states that a \$7,500 permit fee increase on an approximate \$8 million total well cost represents an increase of 0.001%. In fact, the increase is approximately 0.1%, meaning the department has understated the cost implications in the RAF by a factor of 100. This error is repeated in items (24) and (26) of the RAF.

Additional Department Permitting Fees

As this proposed rulemaking is evaluated, it is worth noting that the department intends to move forward with a separate proposed rulemaking that also will increase permitting costs for unconventional natural gas operators in Pennsylvania. On June 14th, PA DEP reviewed a proposed rulemaking with the Air Quality Technical Advisory Committee¹⁹ that will increase significantly air permitting fees. Combined with the recent finalization²⁰ of a new air quality

¹⁷ PA DEP Regulatory Analysis Form Item (12):

http://files.dep.state.pa.us/PublicParticipation/Public%20Participation%20Center/PubPartCenterPortalFiles/Environmental%20Quality%20Board/2018/May%2016/7-542_Unconventional%20Well%20Fees_Proposed/04_7-542_Unconventional%20Well%20Fees_RAF.pdf

¹⁸ 25 PaCode §102.5(c)

¹⁹ PA DEP Air Quality Technical Advisory Committee – June 14, 2018:

http://files.dep.state.pa.us/Air/AirQuality/AQPortalFiles/Advisory%20Committees/Air%20Quality%20Technical%20Advisory%20Committee/2018/6-14-18/6_2018_Fees_AQTAC_PPT_6-14-2018_for_posting.pdf

²⁰ *Pennsylvania Bulletin* – June 9, 2018: Issuance of General Plan Approval and/or General Operating Permit No. 5A for Unconventional Natural Gas Well Site Operations or Remote Pigging Stations (BAQ-GPA/GP-5A); Modified General Plan Approval and/or General Operating Permit No. 5 for Natural Gas Compressor Stations, Processing Plants and Transmission Stations (BAQ-GPA/GP-5):
<https://www.pabulletin.com/secure/data/vol48/48-23/890.html>

permit requirement that will affect many unconventional natural gas well sites, the proposal, if adopted, will levy a \$2,500 permit application fee along with an annual \$2,500 annual operating permit maintenance fee.

While these fees are being advanced by separate department programs for distinct purposes, each is proposed and would be imposed by the department on the unconventional natural gas industry. It is important that as the well permit fee increase is reviewed, it is evaluated in a manner that gives some consideration to the totality of cost increases to the unconventional natural gas industry. Individual policy choices by the department – for example, how to fund various programs and the establishment of permitting threshold requirements – have a cumulative impact that ought not be segregated but rather considered in their totality.

Recommendations

Prior to moving forward on an increase in the amount of an unconventional well permit application fee, the MSC recommends that the department and the Governor's Office consider the following recommendations:

- Allocate a reasonable amount of General Fund dollars to the oil and gas program, as the department does for every other program it administers;
- Identify the total costs of the oil and gas program to the unconventional industry, so that revenue generated from unconventional well permit fees and the Act 13 Impact Fee bear a reasonable relationship to this total cost, in accordance with the statutory authority of the Oil and Gas Act;
- Submit a revised and accurate RAF that properly considers the impacts of the proposed rulemaking on small businesses, analyzes the competitive impact and establishes the correct cost of compliance;
- Align special fund reimbursement policy within the department so that full credit and revenue is provided to the oil and gas program with respect to permit fees related to the Ch. 102 and Ch. 105 programs; and
- Include, and not totally dismiss, the \$6 Million annual allocation from the Act 13 Impact Fee in the base revenues utilized by the department to operate the oil and gas program as has been allocated as general practice every year since the imposition of the Impact Fee.²¹

Conclusion

More than sufficient revenues from the unconventional oil and gas industry are being paid to the Commonwealth through the Impact Fee to support oversight of the unconventional natural gas industry – nearly \$1.5 Billion since 2012, including approximately \$220 Million in 2018.

Moreover, the industry has paid billions of dollars directly to the state's General Fund through existing corporate and personal income, sales and use and other taxes imposed on businesses

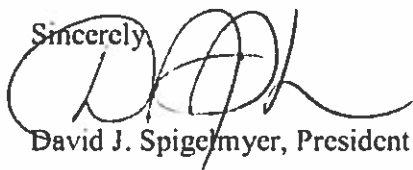
²¹ Item (10) of the RAF states that the \$6 million Impact Fee allocation "depends on the Department's immediate needs" and is therefore not included in the well permit application fee analysis. As the department notes throughout the RAF, one is hard-pressed to determine a more immediate need than funding the oil and gas program.

operating in Pennsylvania, much of which is then appropriated to state agencies, like the department, for general government operations.

Natural gas operators appreciate the constraints the oil and gas program currently faces to stretch one-time permit application fees to cover future activities related to the well's operation. However, these constraints – many of them self-imposed by the Administration's refusal to support a General Fund allocation or seek re-allocation of existing Impact Fee revenues – should not be overcome at the expense of imposing unreasonable permit application fees on the unconventional natural gas industry and deviate from the statutory authority of the department. The department should examine and quantify the costs of the oil and gas program attributable to unconventional natural gas operations, identify operational changes to address permit delays, and fully exhaust alternate revenue options before moving forward with such a drastic permit fee increase.

Thank you for your consideration of these comments. The MSC stands ready to discuss any of these concerns in greater detail.

Sincerely,



David J. Spigelmyer, President

cc: Scott Perry, Deputy Secretary
Office of Oil and Gas Management
Senate Environmental Resources & Energy Committee
House Environmental Resources & Energy Committee
Independent Regulatory Review Commission
Environmental Quality Board
Honorable Eugene DePasquale, Auditor General of Pennsylvania