

Minutes, October 7, 2011, meeting of the Marcellus Shale Advisory Commission
Approved November 15, 2011

The Commission held its second meeting on October 7, 2011 at Garrett College in McHenry, MD. In attendance were Chairman David Vanko and Commission members Shawn Bender, Steve Bunker, George Edwards, Peggy Jamison, Jeff Kupfer, Heather Mizeur, Jim Raley, Paul Roberts, Bill Valentine, Nick Weber, and Harry Weiss; Marci Ross attended for Dominick Murray. Also in attendance were Secretary Bob Summers (Maryland Department of the Environment, "MDE") and Secretary John Griffin (Department of Natural Resources, "DNR"), as well as staff of state agencies and members of the public.

Dr. Vanko called the meeting to order at 1:00 pm. He noted that the Commission's current focus is on the substance of the report that is due at the end of 2011. In the coming year, additional issues will be addressed. The Commission may want to hear from experts, take field trips, and conduct sessions with public comments. Working groups may be established on specific issues.

Dr. Vanko then referred to a draft set of goals, which he had circulated to the Commissioners, for guiding the Commission's work. There was some discussion, but no action was taken on the document. There was support for developing a work plan and timeline for the remaining parts of the study.

The minutes of the August 4 meeting were approved unanimously with Commissioner Jamison abstaining.

The Commission then addressed the issue of standards of liability for damages that may be caused by gas exploration and production activities. A briefing paper had been distributed in advance of the meeting that described the current liability rules and alternatives that could be available to address deficiencies. Brigid Kenney framed the issues. Those who lease or sell their mineral rights can negotiate for protection or compensation. In some circumstances, a person who alleges damages could bring a civil lawsuit based on trespass, negligence, private nuisance, or strict liability for an abnormally dangerous activity. While these remedies are available, lawsuits are expensive to bring and defend and take a long time to resolve. In addition, the technical issues are likely to be complex and require investigation and testimony by consultants and experts. Some liken a dispute between a landowner and an energy company to a David versus Goliath contest. Ways of addressing these perceived problems include shifting the burden of proof by establishing a presumption that damage that occurs close in place and time to drilling activity was caused by the activity, expanding strict liability, and enacting a Surface Owners Protection Act.

The Commissioners discussed the issues. Later, the audience was able to offer comments. To summarize:

1. Presumptions

- a. Not every type of damage should trigger the presumption. Contamination of water is the usual type of damage covered by the presumption.
- b. Pennsylvania's laws establish a statutory presumption that a well operator is responsible for the pollution of a water supply that is within 1,000 feet (it was reported that Pennsylvania has changed this to 2,500 feet) of the oil or gas well, where the pollution occurred within six months after the completion of drilling or alteration of such well.
- c. In Pennsylvania, Chevron voluntarily tests wells within 3,000 feet of the vertical borehole.
- d. What distance is appropriate? Is 1,000 feet a good number? A distance should be established from both the vertical and horizontal portion of the well.
- e. What interval of time is appropriate? Six months from the activity seems too short.
- f. After expiration of the time period, the presumption would not apply, but a person who alleged damage could still bring a lawsuit and prove the cause and effect relationship.
- g. Establishing the presumption is an incentive for companies to test wells and establish background conditions in advance of their activities.
- h. Would establishing the presumption put the leasing landowner at risk of liability? Those bringing a lawsuit will probably sue everyone involved.
- i. If a landowner refuses to allow pre-drilling testing, he should not get the benefit of the presumption.
- j. Audience comment: do we know enough about the groundwater regime to figure out where the effects of drilling or fracking might occur? Aquifers in Western Maryland are complicated and not well studied.

2. Strict Liability

- a. The concept is like Superfund; the polluter pays even if the activity that resulted in the pollution was legal and there was no negligence.
- b. A question was raised about the scope of an existing Maryland statute, Nat. Res. Code Section 5-1703, is unclear. Does it apply to all State land? All leased State land? All land? If the statute is ambiguous, it should be clarified.
- c. Secretary Griffin explained that the law was a response to proposed drilling beneath the Chesapeake Bay. The Board of Public Works was to promulgate leasing regulations (it never did) and the law was meant to address State lands that were leased.

- d. Extending strict liability to all lands is like declaring gas drilling in the Marcellus Shale an abnormally dangerous activity. This would discourage gas companies from coming to Maryland at all.
3. Trespass
- a. Subsurface entry without permission would be considered trespass.
 - b. “Rule of Capture” is a common law concept that relates to natural resources like groundwater, oil and gas, and wildlife. The general rule is that the first person to "capture" such a resource owns it. Under this principle, if, without actually entering onto or drilling under another’s land, “X” were able to extract oil or gas that underlay “Y’s” land, X would not be liable to Y and would not have to pay Y for the oil or gas.
 - c. The Rule of Capture would probably not come into play with shale gas, because gas on an adjacent property can probably not be “captured” without drilling under the adjacent land.
4. Surface Owner Protection Act “SOPA”
- a. Can SOPA address a decline in the value of real estate? It was noted that a bill has been introduced in the New York Legislature (later identified as S5879, The Property Owner’s Bill of Rights) that requires a producer of gas by hydraulic fracturing to pay the owner of real property 150% of the value that the real property had before drilling if soil or groundwater on that real estate is contaminated.
 - b. In the absence of a SOPA, it is not easy for a landowner to enforce the common law limitation of “reasonable access.” The landowner would have to go to court.
5. Other mechanisms for protecting landowners and addressing damage
- a. The language of the deed or lease can establish or waive protections.
 - b. Permit conditions can establish rules of responsibility for addressing problems.
 - c. Performance bonds provide financial assurance that sites will be properly closed and reclaimed. In some areas, bonds are not released for a full five years after the site is completely closed and reclaimed. We should look to the Maryland law on coal mines.
 - d. Tax money could go into a fund to remediate damage that does not appear for a long time – even after final closure of a well. The coal tax was cited as an example.
 - e. Should a landowner be empowered to require a driller to perform a pre-drilling survey to establish conditions?
 - f. Could an ombudsman be appointed to assist landowners?
6. Overall Goal
- a. Prevent harm.

- b. Think creatively about ways to address prevention and remediation of harm.
- c. Audience comment: Whatever the Advisory Commission recommends should be fair to drilling companies.

The Commission then addressed the issue of a State-level source of revenue from gas exploration and production activities. A briefing paper had been distributed in advance of the meeting that summarized existing Maryland taxes, described the taxing structure of some other oil and gas producing states, discussed HB 852 (2011) that would have funded a study with a per-acre fee on leased land, and permit and production fees. Joe Gill framed the issue using the four elements the Advisory Commission was charged with analyzing: desirability, identifying one or more revenue sources, state activities that would benefit from any revenues generated and impacts. The Commissioners discussed the issues. Later, the audience was able to offer comments. To summarize:

1. Personal property tax

- a. A personal property tax is a tax on property used to conduct a business. In the case of gas drilling the personal property might include the drill rig and other equipment.
- b. Senator Edwards noted that Garrett County exempts all corporations except utilities from personal property tax.

2. Study Fee

- a. Delegate Mizeur noted that industry had supported a compromise bill that assessed a per acre fee for a study.
- b. The amount of money needed for a study should be determined and divided by the number of leased acres to set a fee.

3. Severance Tax

- a. It was noted that Garrett County has in place a 5.5% severance tax on natural gas; 5% goes to the county's general funds and 0.5% goes to the municipalities. Senator Edwards predicted that a similar measure would be adopted for Allegany County.
- b. What happens if the tax is not adopted for Allegany County?
- c. Could the severance tax be adjusted to incentivize the hiring of local workers?
- d. Various suggestions were made for an appropriate severance tax. The most commonly mentioned was a 10% total severance tax (5.5% County; 4.5% State). Other suggestions included:
 - i. 1.5% for the first 60 months; 5% thereafter; 1% on marginal wells; no tax on stripper wells;
 - ii. 10% severance tax on the gross or market value of the gas for the lifetime of the well;

- iii. Wells with very low yields should not be taxed;
 - iv. The severance tax should be set to raise the amount of money we need – how can this be estimated?
 - e. Money collected from severance taxes should go back to the impacted community because not all of Maryland will be affected by drilling.
 - f. The impacts (roads, schools, emergency services) are local; in Pennsylvania, the local impacts have been the most important.
 - g. Severance taxes should not go to the general fund; some should be reserved to address problems that may become evident years later.
 - h. The existing Oil and Gas Fund may be a good mechanism for addressing problems that may not become evident for years.
 - i. A good legislative strategy would be to start with a high tax rate and be prepared to compromise.
 - j. We should start with figuring out what severance tax money should be used for and how much money will be needed. That's how you budget.
 - k. Maryland needs to remain competitive.
 - l. The Utica Shale may yield oil; should we impose a severance tax on oil as well as gas, and Utica as well as Marcellus?
4. Royalties
 - a. Maryland should set a minimum royalty payment.
 - b. Pennsylvania set a 12.5% minimum royalty; what do other states do?
 - c. Maryland could realize income by leasing State lands, as Pennsylvania has.
5. Permit Fees
 - a. In setting additional taxes or fees, we should be mindful that the State will charge for permits.
 - b. The permit fee should be set high enough to pay the engineers and inspectors Maryland will need; the compensation must be competitive with industry salaries.
 - c. Permit fees can address some on-site impacts.
6. Timing
 - a. There is a need to build capacity (staff, expertise) in State and local government before the drilling starts.
 - b. The scale of drilling in Maryland will probably be less than in Pennsylvania; much less land is involved.
 - c. The State should control the rate of drilling by issuing a number of permits that matches our resources to manage.

7. Information needs

- a. What do the State and State agencies need; *e.g.*, funds for studies, enforcement, etc.?
- b. What impacts can be anticipated? What will it cost to address them?
- c. Considerable work has been done to identify impacts.
- d. Long-term and cumulative impacts must be considered.
- e. Will the Garrett County severance tax of 5.5% raise enough to meet its needs? Will the money be directed to those local impacts?
- f. How much additional revenue (sales taxes, gasoline taxes, income taxes) will be raised from the drilling activity?
- g. Wages in jobs in the gas field are very high – business generates income tax revenue.

Additional comments from the audience and Commissioners:

1. The openness of the meeting and process is appreciated.
2. We need to train people to get the jobs of the future and avoid a boom and bust economy.
3. There is a good local workforce but the gas companies don't hire them.
4. Drilling will bring some jobs, but the high paying drill jobs are filled by out of state workers.
5. Local workers do the grading, electrical work, and other jobs for gas companies.
6. We are losing jobs in western Maryland.
7. Smart landowners can protect themselves with lease language; the Farm Bureau can help; landmen get bonuses for leases with low per acre cost.
8. Is there a way of ensuring that jobs are given to local people? One Commissioner has a crew working on a drill site out of State, and 50% of them are local.
9. In order to encourage local employment, there should be no preference given to minority and women-owned businesses.
10. There is no one on the Commission who owns a large amount of land in the area.
11. A lessor receives value from the lease, and possibly from royalties. There should be no additional compensation for "damage."
12. Damage to roads is a big issue. A company should be required to restore the roads to the condition that existed before the company began using the road. Garrett County has obtained bonds from companies against damage caused to roads by their expected heavy truck traffic.
13. Taxing the gas is taxing the citizens, because the citizens own the gas.
14. The gas boom will bring the State a lot of tax money paid by local landowners. The money should benefit the areas from which the gas is produced.

15. The State has invested in other businesses to entice them to western Maryland; why should the gas industry have to pay for everything? The State should invest in this industry at least to the extent of doing the study.
16. Adjacent landowners get the impact but no income.
17. In other states, companies test well water but don't share the data with the government or with other landowners; Maryland should assure that the data are available.
18. Any study should be on a watershed scale.
19. Is there a way to ensure that surface owners are notified when the mineral rights are resold or re-leased?

Chairman Vanko said that he would discuss with Paul Roberts his suggestion that the Advisory Commission establish a subcommittee to work with the two departments on developing recommendation on revenue issue, including best fiscal practices.

The next meeting will be the week of November 14. The Commissioners will be polled about their preferences.

Chairman Vanko adjourned the meeting at 4:00 pm.