

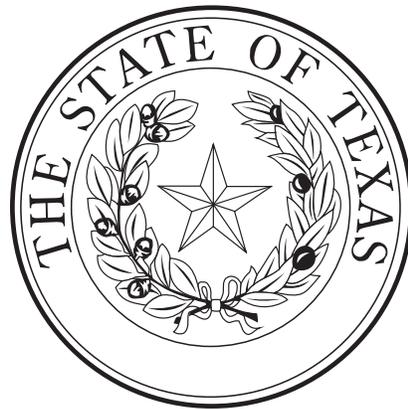


# Interim Report

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## to the 84th Legislature

House Committee on  
Energy Resources



January 2015

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**HOUSE COMMITTEE ON ENERGY RESOURCES  
TEXAS HOUSE OF REPRESENTATIVES  
INTERIM REPORT 2014**

**A REPORT TO THE  
HOUSE OF REPRESENTATIVES  
84TH TEXAS LEGISLATURE**

**JAMES "JIM" KEFFER  
CHAIRMAN**

**COMMITTEE CLERK  
BERNICE ESPINOSA**

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Committee On  
Energy Resources

January 8, 2015

James "Jim" Keffer  
Chairman

P.O. Box 2910  
Austin, Texas 78768-2910

The Honorable Joe Straus  
Speaker, Texas House of Representatives  
Members of the Texas House of Representatives  
Texas State Capitol, Rm. 2W.13  
Austin, Texas 78701

Dear Mr. Speaker and Fellow Members:

The Committee on Energy Resources of the Eighty-third Legislature hereby submits its interim report including recommendations and drafted legislation for consideration by the Eighty-fourth Legislature.

Respectfully submitted,

James "Jim" Keffer

Myra Crownover

Myra Crownover

Terry Canales

Phil King

Phil King

Chris Paddie

Chris Paddie

Gene Wu

Gene Wu

Lon Burnam

Lon Burnam

Tom Craddick

JM Lozano

JM Lozano

Ralph Sheffield

Ralph Sheffield

Tony Dale

Tony Dale

Myra Crownover  
Vice-Chairman

Members: Lon Burnam, Terry Canales, Tom Craddick, Tony Dale, Phil King, JM Lozano, Chris Paddie, Ralph Sheffield, Gene Wu



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## INTRODUCTION

At the beginning of the 83rd Legislature, the Honorable Joe Straus, Speaker of the Texas House of Representatives, appointed eleven members to the House Committee on Energy Resources. The committee membership includes the following: Jim Keffer, Chairman, Myra Crownover, Vice Chairman; Lon Burnam; Terry Canales; Tom Craddick; Tony Dale; Phil King; JM Lozano; Chris Paddie; Ralph Sheffield; Gene Wu.

During the interim, the committee was assigned eight charges by the speaker:

1. Study the impact of the expanding oil and gas exploration and production occurring across the state. Included in the study should be both the positive impacts of the exploration and production as well as the new challenges they are presenting. The study should encompass a review of the following issues:
  - a. The effect on the state budget and the Economic Stabilization Fund;
  - b. The overall impact on the state economy;
  - c. The impact on property values and local taxes;
  - d. The effect on roads;
  - e. The impact on local school districts;
  - f. The complex relationship between land owners, royalty owners, and operators;
  - g. The impact on the environment, including emissions and injection wells;
  - h. Projected water needs and how those fit with our state water plan; and
  - i. The housing issues created by the number of workers needed in areas of shale plays.
2. Study the P5 permitting process at the Railroad Commission to determine whether the process is efficient and effective and whether there are actions that can be taken to improve the process.
3. Study and review the appropriation of general revenue dollars allocated to the Railroad Commission for improvements in IT systems to ensure those funds are being utilized to streamline the permitting process and to allow access to information for all parties that conduct business at the Commission.
4. Review the application of Texas Business & Commerce Code, Section 9.343, to determine the legal rights of unperfected security interests of oil and gas producers with respect to subsequent purchasers, specifically in the context of a bankruptcy proceeding such as *Arrow Oil & Gas, Inc. v. SemCrude, L.P.* and subsequent cases.
5. Monitor the implementation of HB 2982 (83R) to ensure that the required rulemaking is completed efficiently and in a timely manner and SB 1747 (83R) to ensure effective implementation in keeping with legislative intent.

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6. Examine the impact on Texas' economy and businesses of the recent expansion of oil and gas production in Northern Mexico. Assess opportunities for economic growth in Texas and collaboration between Texas businesses and Mexico resulting from Mexico's energy reform, including Mexico's efforts to recover shale gas from the Eagle Ford Shale.
  7. Study the current conditions surrounding the increased seismic activity in the Barnett Shale and other areas of the State. Specifically, review the possibility that increased exploration and disposal well activity could impact seismic activity. The committee shall review active oil and gas activity and injection wells in areas experiencing increased seismic activity.
  8. Conduct legislative oversight and monitoring of the agencies and programs under the committee's jurisdiction and the implementation of relevant legislation passed by the 83rd Legislature. In conducting this oversight, the committee should:
    - i. consider any reforms to state agencies to make them more responsive to Texas taxpayers and citizens;
    - ii. identify issues regarding the agency or its governance that may be appropriate to investigate, improve, remedy, or eliminate;
    - iii. determine whether an agency is operating in a transparent and efficient manner; and
    - iv. identify opportunities to streamline programs and services while maintaining the mission of the agency and its programs.

The committee has completed its hearings and investigations and has issued the following final report and recommendations. Charge 7 was undertaken by the subcommittee on Seismic Activity and the rest of the charges were undertaken by the committee as a whole.

The committee wishes to express appreciation to the agencies, local government officials, associations and concerned citizens who testified at the public hearings for their time and efforts on behalf of the committee.

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## **CHARGE 1**

Study the impact of the expanding oil and gas exploration and production occurring across the state. Included in the study should be both the positive impacts of the exploration and production as well as the new challenges they are presenting. The study should encompass a review of the following issues:

- a. The effect on the state budget and the Economic Stabilization Fund;
- b. The overall impact on the state economy;
- c. The impact on property values and local taxes;
- d. The effect on roads;
- e. The complex relationship between land owners, royalty owners, and operators;
- f. The impact on the environment, including emissions and injection wells;
- g. Projected water needs and how those fit with our state water plan; and
- h. The housing issues created by the number of workers needed in areas of shale plays.

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## SUMMARY

The committee met on August 26, 2014, and heard testimony on a variety of issues related to Charge 1. The following is a summary of topics that were discussed:

### **The effect on the state budget and the Economic Stabilization Fund; overall impact of the state economy; and the impact on property values and local taxes**

James LeBas, former chief revenue estimator for the Texas Comptroller's office, briefed the committee on the overall impact of oil and gas exploration and production on the state and local economy, including the impact on property values. He estimated that the oil and gas industry paid 13.6 billion in direct state and local taxes for fiscal year 2013. Some of these taxes include ad valorem (property), franchise, sales, and production taxes. In addition, the energy sector pays out royalties to various state funds. The Economic Stabilization Fund continues to grow and will come close to the cap of 12.1 billion. Mr. LeBas also projected that the boom would continue for many years to come.

### **Effect on Roads**

The effect on roads was discussed on September 11, 2014 along with Charge 5.

### **Complex Relationship between Land Owners, Royalty Owners and Operators**

Candice Brewer, representing The National Association of Royalty Owners, testified on the complex relationship between land owners, royalty owners, and operators. The National Association of Royalty Owners (NARO) is composed of members that are land owners and royalty owners. NARO helps educate many of them on how to negotiate or audit their contracts. Ms. Brewer explained the relationship between land owners and mineral owners has improved mainly because of education and surface owner agreements. Surface owner agreements are agreements between the surface landowner and the operator to help restore the land and pay for any damages that occur during the exploration and production phases. She suggested that most mineral and property owners are willing to have the minerals developed if they are developed in a responsible and respectful manner. NARO continues work with many mineral and property owners that are new to the oil and gas boom.

### **Impact on the environment, including emissions and injection wells**

The impact on the environment, including emissions and injection wells, was addressed by Cyrus Reed with The Lone Star Chapter of the Sierra Club and Cory Pomeroy representing the Texas Oil and Gas Association.

Cyrus Reed testified that the environmental community recognizes that there have been some improvements made in the regulatory system that have helped minimize the impact on the environment. He cited the recent adoption of new well casing rules by the Railroad Commission of Texas as one positive action taken by industry regulators. He also stated that new inspectors and new air rules have helped address many concerns, but that work needs to continue to help address emissions by the oil and gas industry. Mr. Reed testified that permits for flaring have increased significantly and in some cases operators have not obtained permits. He is concerned that the significant increase in flaring will cause many cities to become non-compliant with federal air quality standards. Mr. Reed stated that he would prefer stricter air quality standards,

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but also recognized this change would cause many cities to be classified as non-attainment - a status that has economic consequences. He would also suggest that we start considering different solutions such as green completions, leak detection, compressor station maintenance, no-bleed pneumatic controllers, TERP funding, venting and flaring standards, and better inspections.

Cory Pomeroy testified that flaring is necessary to help address infrastructure challenges. Operators are facing equipment, supply and service shortages in addition to the extensive time and expense associated with acquiring right-of-way. He stated that recent fly overs by state agencies have monitored that only 5% greenhouse gas is attributed to oil and gas stations. Mr. Pomeroy also testified that the Railroad Commission issues permits for flaring and grants extensions on those permits. In 2013, 3,012 flaring permits were issued in relation to 144,000 active wells. Currently, the Railroad Commission allows for flaring to occur up to 180 days and extensions are granted as long as progress has been made on infrastructure to use or move product. Mr. Pomeroy recommended that each city be looked at individually with regards to attainment requirements. For example, Houston has different sources of pollutions compared to the Dallas-Fort Worth area. He does not believe flaring should be attributed to be the cause of non-attainment status.

#### **Projected water needs and how those fit with our State Water Plan**

The projected water needs and how those fit with our state water plan was addressed by Brent Halldorson, Texas Water Recycling Association, and Matt Nelson, Texas Water Development Board.

Brent Halldorson, Texas Water Recycling Association, testified that the recycling rules introduced by the Railroad Commission over a year ago have helped increase the use of recycled water. Mr. Halldorson testified that the costs for recycling have decrease due to competition and the ability to recycle larger volumes. Texas is the only state with a multi-location permit. A multi-location permit location is a permit issued to an oil and gas company which can be used in different locations. Most states require each location to have a permit. He also testified on the different options to recycle water and explained the different types of permits available for companies to obtain.

Matt Nelson, Texas Water Development Board testified about the current state water plan and how the oil and gas industry will affect it. The current state water plan meets all the needs for the state including the oil and gas impact. The current use of the oil and gas industry is minimal in comparison to the total use of water.

#### **Housing issues created by the number of workers needed in area of shale plays**

Major Ron Joy testified on behalf of the Texas Department of Public Safety (TxDPS) with regard to the impact shale plays have had on local workforce. The main issue for the loss of employees within TxDPS is the increase in cost of living and early retirements to work in the private industry. The amount of cases to investigate has increased and the current workforce cannot keep up with the current case load. TxDPS is using different initiatives to combat the current situation. Some initiatives that are currently being used are surge operations, increased

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man power requests and requests to the executive leadership for the hardship duty station's limits to be removed so that more stipends are authorized.

John Thomas with Region 18 Education Service Center testified on the issues facing many school districts and service centers with regard to the oil and gas boom. Teachers and staff are leaving the shale plays like the Eagle Ford and Permian Basin due to the cost of living. Many superintendents are reporting that new hires are backing out of contracts after they become aware of the cost of living. Another major issue affecting school districts and service centers is providing transportation for the students because bus drivers are leaving to work as drivers for the oil and gas industry. Some school districts are paying parents to drive children to school. Districts are buying and renovating older buildings into apartments to help alleviate the cost of living for teachers. They provide housing for multiple teachers living together to help keep the cost of living down. Other districts are passing bonds to help pay teachers higher salaries. Lastly, some districts have offered retention bonus and housing agreements. All these options have been implemented but many positions are still unfilled.

Chris Traylor, Deputy Commissioner with Health and Human Services Commission (HHSC) testified how difficult it is to keep caseworkers for Child Protective and Adult Protective Services in energy effected areas. The average amount of time to replace a caseworker is about 133 days. Steadily increasing costs of living near energy plays have caused many caseworkers to seek other forms of employment. The Eagle Ford Shale has been able to alleviate the challenge by drawing from the San Antonio Area but the Permian Basin is the critical area were HHSC continues to work on different solutions to their workforce shortage.

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## **RECOMMENDATIONS**

The committee makes the following recommendations on Charge 1:

The 84<sup>th</sup> Legislature should engage in continued dialog with the oil and gas industry to ensure the state has proper infrastructure to assist with the creation of a robust oil and gas economy.

The 84<sup>th</sup> Legislature should insist that the Railroad Commission of Texas and the Texas Commission on Environmental Quality work together to address the issue of flaring. This includes ensuring that the RRC notifies TCEQ in a timely manner when flaring permits are granted or extended. The committee also recommends a more thorough vetting by the RRC for these types of permits to ensure proper practices are being followed. Additionally, flaring permits and the status of those permits should be published in county by county searchable format on the RRC website for transparency.

The 84<sup>th</sup> Legislature should consider non-punitive ways to encourage the use of recycled and brackish water by the oil and gas industry, including consideration of a severance tax exemption.

The high cost of living in shale play areas has affected many state agencies. Many of the state agencies have been preemptive and implemented strategies to help alleviate the cost but many still need additional help and in many cases funds. The committee would recommend to the 84<sup>th</sup> Legislature to address the high cost of living in shale play areas be address and additional funding be given to the effected state agencies.

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## REFERENCES

Oral and Written Testimony by James LaBas, Texas Oil & Gas Association, Public Testimony, Texas House of Representatives Committee on Energy Resources, Austin, Texas, August 26, 2014

Oral and Written Testimony by Candice Brewer, National Association of Royalty Owners, Public Testimony, Texas House of Representatives Committee on Energy Resources, Austin, Texas, August 26, 2014

Oral and Written Testimony by Cyrus Reed, Sierra Club, Public Testimony, Texas House of Representatives Committee on Energy Resources, Austin, Texas, August 26, 2014

Oral and Written Testimony by Cory Pomeroy, Texas Oil & Gas Association, Public Testimony, Texas House of Representatives Committee on Energy Resources, Austin, Texas, August 26, 2014

Oral and Written Testimony by Brent Halldorson, Texas Water Recycling Association, Public Testimony, Texas House of Representatives Committee on Energy Resources, Austin, Texas, August 26, 2014

Oral and Written Testimony by Matt Nelson, Texas Water Development Board, Public Testimony, Texas House of Representatives Committee on Energy Resources, Austin, Texas, August 26, 2014

Oral and Written Testimony by John Thomas, Region 18 Education Service Center, Public Testimony, Texas House of Representatives Committee on Energy Resources, Austin, Texas, August 26, 2014

Oral and Written Testimony by Ron Joy, Texas Department of Public Safety, Public Testimony, Texas House of Representatives Committee on Energy Resources, Austin, Texas, August 26, 2014

Oral and Written Testimony by Chris Traylor, Texas Department on Health on Human Services, Public Testimony, Texas House of Representatives Committee on Energy Resources, Austin, Texas, August 26, 2014

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## **CHARGE 2.**

Study the P5 permitting process at the Railroad Commission to determine whether the process is efficient and effective and whether there are actions that can be taken to improve the process.

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## **SUMMARY**

The committee reached out to different industry associations and the Railroad Commission to offer an opportunity to make any recommendations for changes to the current process to obtain a P5 permit. The Railroad Commission and the different industry associations responded that the current process is working in an efficient manner; they made no additional recommendation, and stated that they would continue to work with the Railroad Commission on addressing any issues that may arise.

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## **RECOMMENDATIONS**

The committee will continue to monitor the P5 permitting process and work with the Railroad Commission to ensure the permitting process continues to work efficiently.

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### **CHARGE 3**

Study and review the appropriation of general revenue dollars allocated to the Railroad Commission for improvements in IT systems to ensure those funds are being utilized to streamline the permitting process and to allow access to information for all parties that conduct business at the Commission.

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## SUMMARY

The committee received an update from Brandon Harris, Chief Information Officer for Information Technology Services Division of the Railroad Commission, on the agency's efforts to modernize their information technology systems on August 26, 2014. Mr. Harris gave a broad overview of the current accomplishments and future goals. The current accomplishments and goals are listed below.

### ACCOMPLISHMENTS

- June 2014: Deployed New Redesigned RRC Public Website ([www.rrc.texas.gov](http://www.rrc.texas.gov))
- June 2014: Migrated RRC Online and other critical customer systems to newer, faster, more reliable hardware and software in the state data center (moving off of 10-12 year old equipment and software)
- June 2014: Allow for automated processing of some vertical wells located in fields with Horizontal Field Rules
- July 2014: New Surface Mining Permitting Application released for internal Commission staff
- August 2014: Provide queue screens to indicate whether a well has a vertical, horizontal, or directional wellbore profile
- August 2014: Electronic updates to identify gatherers and purchasers (Form P-4)
- September 2014: Allow Operators to enter Surface Well Location latitude and longitude in one of three formats
- October 2014: Updated Completions to display data recently submitted to the Commissions based on Rule 13 (Forms W-2/G-1)
- October 2014: Released the new GIS Public Viewer to a limited set of industry and state agency partners

### FUTURE GOALS

- Additional improvements to the Drilling Permit process
- Release of the new GIS Public Viewer
- Groundwater Protection Determination Letter (GW-1)
- SWR 13 Exception Letter
- Operator Portal functionality improvements
- GIS Technology Upgrades, including
  - Improved stability for GIS platform
  - Updated ability to receive data submissions (pipeline operators)
  - Improved performance of GIS applications used by staff to process permit applications
- Improvements to the Completions process

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- Submission of digital test charts and well logs
  - Additional improvements to the RRC Portal functionality
  - Pipeline Permit application and renewal (T-4)
  - Improvements/Enhancements to the Oil and Gas Inspection Process

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## **RECOMMENDATIONS**

The committee believes that the Railroad Commission must function to the highest level of efficiency and to do so it must have all the necessary tools to bring their antiquated information technology systems into the new century. At this time, the committee would recommend the continued monitoring of the implementation to ensure that the necessary upgrades are completed in a timely manner and within the budget allotted for this transition. The committee would also recommend that the 84<sup>th</sup> Legislature monitor ongoing technology upgrades and reach out to industry representatives to ensure that the technology improvements at the Commission are user-friendly.

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## **REFERENCES**

Oral and Written Testimony by Brandon Harris, Texas Railroad Commission, Public Testimony, Texas House of Representatives Committee on Energy Resources, Austin, Texas, August 26, 2014

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## **CHARGE 4**

Review the application of Texas Business & Commerce Code, Section 9.343, to determine the legal rights of unperfected security interests of oil and gas producers with respect to subsequent purchasers, specifically in the context of a bankruptcy proceeding such as *Arrow Oil & Gas, Inc. v. SemCrude, L.P.* and subsequent cases.

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## SUMMARY

The Committee on Energy Resources did not hold a hearing regarding Charge 4. Subsequent to the 83<sup>rd</sup> Legislative Session, the legal issues surrounding Charge 4 were resolved by the United States Bankruptcy Court for the District of Delaware *In re: SemCrude, L.P. et al.*, 504 B.R. 39 Bankr. Lexis3250 (June 28, 2013). The Court in *SemCrude* clarified a lower court decision and eliminated any potential confusion and uncertainty over the interpretation of Texas oil and gas lien laws. In light of the *SemCrude* decision, the Committee on Energy Resources has decided not to take action on Charge 4.

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## **RECOMMENDATIONS**

The committee on Energy Resources does not have any recommendations regarding Charge 4.

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## **CHARGE 5**

Monitor the implementation of HB 2982 (83R) to ensure that the required rulemaking is completed efficiently and in a timely manner and SB 1747 (83R) to ensure effective implementation in keeping with legislative intent.

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## SUMMARY OF HB 2982

The committee was able to get an update on the implementation of HB 2982 on August 26, 2014, from Mary "Polly" McDonald, Director of the Pipeline Safety Division. Mrs. McDonald gave an overview on the current efforts on the implementation of HB 2982. She also stated that HB 2982 was not going to be used to regulate Class 1 pipelines but instead to start gathering information on them. House Bill 2982 amends the Natural Resources Code to require safety standard rules of the Railroad Commission of Texas that apply to the intrastate transportation of hazardous liquids and carbon dioxide by gathering pipelines in rural locations and to related facilities in rural locations to be based only on the risks the transportation and the facilities present to the public safety, with certain exceptions to maintain federal compliance and delegation. The bill removes language exempting the movement of hazardous liquids or carbon dioxide through gathering lines in rural locations from rules that adopt safety standards. House Bill 2982 also amends the Utilities Code to authorize the Railroad Commission by rule to establish certain safety standards and practices for gathering facilities and transportation activities in Class 1 locations.

The Pipeline Safety Division under the direction of Mrs. McDonald has had several workshops around the state to inform pipeline operators of HB 2982 and the need to acquire information on Class I gathering lines. The Pipeline Safety Division also met and worked with several industry representatives to develop a survey for pipeline operators to provide information to the Railroad Commission on Class I gathering lines. The survey was distributed early November and is due back January. The Railroad Commission will gather the surveys and propose a rule to address the risk of the Class I gathering lines. The rule is expected to be proposed and adopted in 2015. The rule will be based on a risk.

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## **RECOMMENDATIONS**

The committee will continue to monitor the Railroad Commission Pipeline Safety Division and pipeline operators to ensure the intent of the bill is delivered. The committee would recommend that the 84<sup>th</sup> Legislature monitor the Railroad Commission to ensure a rule is purposed and adopted and in the event that a rule is not proposed legislative action be taken.

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## **SUMMARY OF SB1747**

Under Charge 1 and Charge 5, the committees was charged with examining SB 1747 and give a brief update of the current conditions of the shale affected roads.

A brief summary of SB 1747 is provided.

Senate Bill 1747 amends the Transportation Code to establish the transportation infrastructure fund, provide for its composition, and restrict appropriation of money in the fund to the Texas Department of Transportation (TxDOT) for the fund's purposes. The bill requires TxDOT to develop policies and procedures to administer a grant program to make grants to counties for transportation infrastructure projects located in areas of the state affected by increased oil and gas production and provides for the allocation of grants among counties. The bill sets out requirements regarding the grant application process, matching funds, and subsequent grant applications by a county.

Senate Bill 1747 authorizes a county to create a county energy transportation reinvestment zone in an area affected by oil and gas exploration and production activities, sets out applicable procedures and requirements regarding the creation of such a zone, including the establishment of a property tax increment account for the zone, and provides for the termination and extension of a zone. The bill also authorizes a commissioners court to enter into an agreement with TxDOT to designate a county energy transportation reinvestment zone for a specified transportation infrastructure project involving a state highway located in the proposed zone and provides for the alternative formation of a road utility district that has the same boundaries as a county energy transportation reinvestment zone in order to assist the county in developing a transportation infrastructure project. The bill provides for, as a condition of eligibility for a transportation infrastructure project grant, the creation of a county energy transportation reinvestment zone advisory board by a county.

Senate Bill 1747 requires a road condition report made by a county that is operating under a system of administering county roads to include, if reasonably ascertained, the primary cause of any road, culvert, or bridge degradation. The bill authorizes a commissioner's court to accept donations of labor, money, or other property to aid in the building or maintaining of roads, culverts, or bridges in the county.

Senate Bill 1747 specifies that its provisions relating to county energy transportation reinvestment zones and the advisory boards of such zones prevail over similar provisions in House Bill 2300, 83rd Legislature, Regular Session, 2013, and that those provisions in House Bill 2300 have no effect.

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Several witnesses testified on the effects on roads and on SB 1747. The following summarizes as whole the two charges.

General Joe Weber, Executive Director, spoke on behalf of TxDOT. 254 counties were eligible for grant money but only 191 counties applied for money. He was also able to testify as to how TxDOT provided the counties with many resources to help them apply for grant money. As of August 29, 2014, 175 agreements had been signed and 16 were pending. After the agreements are signed, the funds would be distributed. General Weber also gave an update on the lawsuit filed by Judge Joel Rodriguez, County Judge off La Salle County. Judge Rodriguez filed a lawsuit against TxDOT on the formula used to distribute grant money. La Salle County felt the intent of SB 1747 was to only appropriate funds to shale-effected counties. The lawsuit has since been dismissed and a court ruled that TxDOT had appropriated the money correctly and could continue with the distribution. At this time SB 1747 was implemented in a timely matter and has helped many counties find additional funding to restore dilapidated roads.

Judge Daryl Fowler, County Judge of Dewitt County provided the committee with testimony from a county's point of view. Judge Fowler was pleased with the process but asked for simplification of the grant application for future programs. He gave a board overview of the three CREZ's that La Salle county had created and explained how the grant money would help bring the roads to drivable conditions. Judge Fowler also introduced an idea to have the counties receive the royalties collected from the county right-of-ways maintained by the counties. The royalties and rent payments are currently appropriated to the state budget and not counties. The rent and royalty payments could help offset the cost of maintaining the county road system. Judge Fowler would like to the have legislature pass a bill that would help clarify the attorney general opinion that states that no county has lawful authority over an oil and gas lease unless given such authority under the legislature.

Bill Stevens, Texas Alliance of Energy Producers, also provided the committee with testimony on the impact of SB 1747 on behalf of the energy producers. Mr. Stevens stated that the bill has helped many counties that could not keep up with the current boom. He was very appreciative of the committee's hard work to pass a bill that could help the industry continue to grow. Mr. Stevens also indicated that they are currently working with the counties and TxDOT to help them identify where wells will be developed to help reinforce the roads. He also testified that he would continue to help the counties find funds for road maintenance.

Sally Velasquez testified on behalf of Judge Garcia, County Judge of Frio County. Frio County has not had production but is home to many disposal and injection wells. SB 1747 allowed for the volume of injected oil and gas waste to be added in the funding formula. Frio County was able to apply for grant money to help restore roads that were severely affected by the truck traffic. Frio County recommends that revisions to SB 1747 be conducted to help counties like Frio County. The main recommendation by Frio County was to define terms of disposed waste

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by injection, volume and reference point of origination for deposit with formula to classify eligibility.

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## **RECOMMENDATIONS**

The committee believes SB 1747 was a one-time grant program to help address the critical conditions of county roads. The committee would recommend that the 84<sup>th</sup> Legislature study and implement a long term funding solution.

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## **REFERENCES**

Oral and Written Testimony by Mary McDonald, Texas Railroad Commission, Public Testimony, Texas House of Representatives Committee on Energy Resources, Austin, Texas, August 26, 2014

Oral and Written Testimony by Judge Daryl Fowler, Dewitt County, Public Testimony, Texas House of Representatives Committee on Energy Resources, Austin, Texas, September 11, 2014

Oral and Written Testimony by General Joe Webber, Texas Department of Transportation, Public Testimony, Texas House of Representatives Committee on Energy Resources, Austin, Texas, September 11, 2014

Oral and Written Testimony by Sally Velasquez, Frio County, Public Testimony, Texas House of Representatives Committee on Energy Resources, Austin, Texas, September 11, 2014

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## **CHARGE 6**

Examine the impact on Texas' economy and businesses of the recent expansion of oil and gas production in Northern Mexico. Assess opportunities for economic growth in Texas and collaboration between Texas businesses and Mexico resulting from Mexico's energy reform, including Mexico's efforts to recover shale gas from the Eagle Ford Shale.

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## SUMMARY

The committee on Energy Resources traveled to Edinburg, Texas to have a joint hearing with the Committee on International Trade & Intergovernmental Affairs on September 29, 2014. The joint hearing was held to get an understanding of the oil and gas reforms occurring in Mexico. The following is a summary of the testimonies given.

Max Yzaguirre testified that Mexico has opened up oil and gas sectors and electricity sectors. He is very optimistic that these reforms will increase foreign investments. Mr. Yzaguirre stated that currently Pemex provides 1/3 of the total of Mexico's general revenue. Because revenue is declining, Mexico began to look for ways to expand their crude oil production. Mexico lacks adequate refineries and imports 1/2 of their gasoline and 1/3 of the diesel for the country's use from the United States. Mexico's natural gas markets are strained and currently import 1/3 of natural gas. Mexico has in recent years doubled the amount of natural gas they import. Mr. Yzaguirre gave a list of problems that need to be addressed for the reforms to be successful. Some of the problems are the creation of the rules for regulators to follow, Pemex's commitment to transparency, real estate title uncertainty and security concerns. Mr. Yzaguirre believes that the potential for significant revenue will outweigh the problems. In regards to Texas, opening up Mexico's shale will boost border towns' economies, generate 200,000 Texas jobs, increase opportunities for non oil and gas businesses, oil field supply businesses and increase Texas's general revenue.

Alejandra Bueno testified on how Mexico needed an energy reform and how the federal budget was intermingled with hydrocarbon production. The decline in the federal budget was the strongest advocate for the reform. Mexico currently sits on the 6<sup>th</sup> largest gas shale but it imports most of its gas. The current Mexican administration sees this reform as its main priority. Ms. Bueno also stated that the two important distinguishing characteristics between Texas and Mexico are mineral rights and at what level the production is regulated. Mineral rights belong to the federal government and regulation is also done at the federal level. Just like in Texas, mineral rights overrule surface rights. Royalties collected with regards to hydrocarbon production will go into the Mexican Petroleum Fund, similar to the Texas Economic Stabilization Fund. There are different rounds that will occur to divide the reserves. In each round, private entities will bid for reserves. In round zero, Pemex was able to acquire 83% of the probable reserves and the rest was awarded to the highest bidder. In round 1, private entities are allowed to bid for the 169 blocks. Of the 169 blocks, 109 are exploration and 60 are extraction. Ms. Bueno addressed three important topics, including domestic content rules, booking of the reserves, and surface use and right-of-way. Domestic content rules relating to Mexican participation has to be assured in the supply and productive chain. Booking of the reserves is a financial reporting practice that allows oil and gas companies to reflect the volume of reserves they have the right to produce and market. Surface use and right of way states that no eminent domain processes are authorized; every activity will be negotiated. The three important topics will be addressed after private entities acquire the blocks they bid on.

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George Baker spoke about Mexico moving from a state monopoly with regards to oil, gas and electricity into an uncertain future. Mr. Baker's major concern is the lack of an independent regulator. Currently, the owner of the gas pipelines regulates the same pipelines.

Grant Ruckel, Energy Transfer, testified that the new projects will help boost both sides of the economy. Mr. Ruckel testified on two specific pipelines being constructed and how the recent energy reform will allow for Energy Transfer to obtain a permit from the United States to Mexico. The pipelines will cross federal borders.

Jorge Pinon, University of Austin, testified on different major problems that would cause the energy reform to not produce the revenue it was created for. He stated that the biggest issue is the regulators. Regulators are the same oil and gas producers. This can cause for a big disconnect. Another reason for the reform to have issues is the fights between political parties relating to surface rights issues. Many farms have different families living in them without real estate titles or distinguishing between properties. Another issue that needs to be addressed is de-politizing the relationship between Mexico and the United States. De-politizing the relationship between the two countries can help grow the sense of trust between the two countries. One suggestion provided by Mr. Pinon is to allow the Railroad Commission to provide information to help regulators. The commission could share their expertise to help Mexico learn what has and has not worked.

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## **RECOMMENDATIONS**

The committee would recommend continued monitoring of the Mexican oil and gas reforms and provide any advice they may need.

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## **CHARGE 7**

Study the current conditions surrounding the increased seismic activity in the Barnett Shale and other areas of the State. Specifically, review the possibility that increased exploration and disposal well activity could impact seismic activity. The committee shall review active oil and gas activity and injection wells in areas experiencing increased seismic activity.

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## SUMMARY

The Subcommittee on Seismic Activity was appointed by Chairman Jim Keffer on January 16, 2014, to address recent increases in seismic activity in areas near oil and gas production. Chairman Keffer appointed Myra Crownover to Chair the Subcommittee, which also included Representatives Phil King, Terry Canales, and Chris Paddie. The first meeting of the Subcommittee was held on May 12, 2014. The following is a summary of the hearings.

### May 12th Subcommittee Hearing

During the May 12th hearing, the Subcommittee took testimony from the Mayors of Reno, Texas and Azle, Texas, academic experts and geologists, the Texas Railroad Commission, environmental groups, and oil and gas experts. At the beginning of the hearing, Chairman Crownover proposed, and committee members agreed, that all committee members and witnesses use the proper terminology in regards to the subject matter at hand. Three terms in particular were outlined by the Chair:

- **"Fracking"**: refers to "hydraulic fracturing" of rock by pumping water or other fluids at high pressures into rock formations to release oil and gas for production purposes during the completion of the well.
- **Injection Wells**: a broad category of wells that are permitted by the Railroad Commission and primarily used by oil and gas operators to pressurize an oil or gas field for "enhanced oil recovery" or "secondary recovery."
- **Disposal Wells**: a subset of injection wells that is used to dispose of water and other fluids that are a byproduct of oil and gas production.

### Disposal wells vs. Fracking

Testimony at the hearing was near universal that "hydraulic fracturing" was not related to the recent increase in earthquakes. Rather, "induced seismicity" –earthquakes caused by human activity– is most likely related to disposal wells. However, it was also noted multiple times that the relation between disposal wells and earthquakes was merely correlative in nature and that "correlation is not causation."

Oil and gas operations, by their very nature, produce mineral-laden waters as a by-product. Generally, the most economic means of handling this waste stream is to inject it back into the earth via disposal wells. The Texas Railroad Commission issued the first injection well permit in Texas in 1936.

According to Dr. Craig Pearson with the Texas Railroad Commission, as of May 1, 2014, there were 32,717 active injection (including disposal) wells statewide. The lion's share of these injection wells are used for secondary recovery of hydrocarbon resources through water-flood programs. The remainder of these active injection wells, numbering 7,725 as of May 1, 2014, is disposing of fluids into formations that are either productive or nonproductive of hydrocarbons.

### August 25th Subcommittee Hearing

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On August 25, 2014, the Subcommittee held its second and final meeting. Chairman Crownover announced before the meeting that all members of the public were invited to testify. While no private citizens chose to testify, the Subcommittee did take testimony from the Railroad Commission, the Sierra Club, the Environmental Defense Fund, and the Texas Oil and Gas Association.

The Railroad Commission opened the meeting by announcing that they had proposed new rules for permitting of injection wells. Testimony from the environmental community and the oil and gas industry was largely supportive of the rules and the Commission was praised for taking swift action.

### **Railroad Commission Rules for Disposal Wells**

- Require disposal well applicants to check the USGS database to make sure there has not been any seismic activity in the area of the proposed disposal well site;
- If scientific data indicates a disposal well is causing seismic activity, grant the Commission authority to require an operator to take action, including reducing injection volume and pressure or shutting down a disposal well; and
- If warranted by the Commission, require operators to perform more frequent monitoring and submit timely reports of the injection pressure and injection rate to the Commission.

On October 28, 2014, the Railroad Commission gave unanimous final approval for the new rules for disposal well permitting.

### **Increased Monitoring**

During the August hearing, many of the expert witnesses testified that Texas needed increased monitoring of seismic activity. Texas currently only has 16 seismograph stations that are continuously operating in the state. Texas is a large state, both in geography and population, and the Subcommittee heard from both the environmental and academic community that increased monitoring would greatly increase the State's ability to understand seismic activity and reduce the associated risks.

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## **SUBCOMMITTEE RECOMMENDATION**

The Subcommittee on Seismic Activity was pleased at the determination and hard work of all involved with this difficult issue. The Subcommittee would like to commend Mayors Alan Brundrett and Lynda Stokes for their commitment to public service and would further commend Railroad Commissioners Barry Smitherman, David Porter, and Christi Craddick for taking swift action to address the issue of increased seismic activity in Texas.

The Subcommittee finds no evidence to support a causal link between the process of oil and gas extraction known as “hydraulic fracturing” and increased seismic activity.

The Subcommittee supports the disposal well rules enacted by the Railroad Commission on October 28, 2014, and recommends that the 84<sup>th</sup> Legislature give the rules time to take effect before taking further legislative action regarding disposal wells or injection well permitting.

The Subcommittee recommends that the 84<sup>th</sup> Legislature examine all sources of revenue to increase funding for seismic monitoring in Texas, either through direct appropriations to the Railroad Commission, or through appropriations to an academic institution with expertise in Texas geology and that is capable of working with the Texas Railroad Commission and the United States Geological Survey, to increase the level and quality of seismic monitoring in Texas.

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## **CHARGE 8**

Conduct legislative oversight and monitoring of the agencies and programs under the committee's jurisdiction and the implementation of relevant legislation passed by the 83rd Legislature. In conducting this oversight, the committee should:

- i. consider any reforms to state agencies to make them more responsive to Texas taxpayers and citizens;
- ii. identify issues regarding the agency or its governance that may be appropriate to investigate, improve, remedy, or eliminate;
- iii. determine whether an agency is operating in a transparent and efficient manner; and
- iv. identify opportunities to streamline programs and services while maintaining the mission of the agency and its programs.

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## **RECOMMENDATIONS**

The current policy of the Railroad Commission relating to the media is concerning and lacks transparency. During the interim, the Commission received criticism about this policy from many outside parties, including media, the general public, industry and interest groups. As a response to this criticism, the Commission hired a Director of Communications who started in November. While the committee appreciates this action taken by the Commission, we are still concerned about the Commission's ongoing policy of disallowing media access to any division head or technical staff member other than the Executive Director or Director of Communications.