N. Dakota Confronts Pore Space Issue

By Dan Larson

BISMARCK, N.D.–Now in its third year of recovery, North Dakota's oil and natural gas industry has reclaimed its role as a key driver in the state's economy. What to do with the resultant revenue surge was among the long list of contentious issues during this year's legislative session, reports the leadership of the North Dakota Petroleum Council.

With its odd-year focus on fiscal issues, the legislature tackled several big-ticket financial topics, including a crucial local infrastructure funding question early and a record-setting budget bill late.

Other key issues of industry interest this year included clarification of surface owners' protection in subsurface disposal disputes, resolution of a longstanding contest over oil tax apportionment on tribal lands, and an important step in the state's quest for primacy on federal air emissions rules, explains NDPC Government Affairs Manager Brady Pelton.

North Dakota's oil and gas industry continues to earn support in the Capitol for its important issues, Pelton affirms. "A big reason for that, in addition to oil and gas taxes accounting for more than 50 percent of all tax revenues collected in the last five years, is because our operators back scientific research, they come together to promote industrywide safety programs and are active in local communities," he assesses.

Pore Space

Of the many issues NDPC tracked in this year's legislative session, Pelton indicates, few were more important, or more complicated, than what came to be known as the pore space issue.

As it was originally written in 2009, the state code's carbon dioxide storage section was meant to authorize the use of subsurface pore space for permanent storage of CO_2 produced by the state's coal plants. However, in 2017, a North Dakota Supreme Court decision applied that law to a case involving a saltwater disposal well and ruled that, under the state's oil and gas production damage compensation law, the operator owed the surface owner damages for use of that owner's pore space.

The surface estate owned the pore space, the court ruled, and could seek damages not only for saltwater disposal wells, but also for underground natural gas storage and CO_2 enhanced oil recovery.

Introduced to clarify the intent of the pore space law, SB 2344 was amended in April to remove a reference to temporary natural gas storage, leaving intact the remainder of the bill to cover saltwater disposal wells and CO_2 injection used for EOR, according to the final version, which passed on April 17.

"We worked for many hours with landowners to ensure the final version protected the rights of those private property owners willing to have a subsurface injection facility on their land," Pelton recalls. "Most important, the bill clarifies that the use of pore space does not, in itself, damage that pore space."

He says the bill allows surface owners to continue earning payments for commercial saltwater disposal wells on their property. It also prevents other surface owners within a unitized field or their neighbors from claiming wastewater injected into the well is migrating into their pore space.

Once the temporary gas storage language was removed, the bill had enough support to pass both chambers and went to the governor's desk for signature, Pelton recounts.

Senator Jessica Unruh, R-Beulah, the bill's primary sponsor, told the media she pulled the gas storage language because of too many unresolved logistical questions. Temporary underground gas storage, even as a means of reducing gas flaring, is "a technology we don't quite have nailed down yet," Unruh is quoted.

The need to clarify authorized uses of pore space also has prompted the legislature to approve funding of continued research into both CO_2 EOR and temporary underground gas storage to reduce flaring. Late in the session, the House approved SB 2249, which allocated $5 million per biennium from the state's oil tax revenue to research these and other matters at the University of North Dakota's Energy and Environment Research Center.

Primacy Step

In 2017, the legislature approved SB 2327, which created a new cabinet-level Department of Environmental Quality. This year, the legislature passed HB 1024 to fund staff hires that would enable the new department to pursue an issue of importance for the industry, Pelton notes.

NDPC considers it a top priority for state regulators to secure primacy from the U.S. Environmental Protection Agency for administering federal regulations affecting oil and gas operations, he says. Passage of HB 1024 funds two full-time DEQ employees to help the department "get its ducks in a row and make that application for primacy right away," Pelton relates.

The budget bill includes funds for hiring eight additional DEQ staff next year to operate the program, he adds.

Among other regulations, primacy will give North Dakota oversight over air quality regulations such as EPA's 40 CFR Part 60 Subpart OOOO, the Quad O rules that set air emissions monitoring and reduction standards for oil and gas operations and mandate leak detection and repair programs, as well as Quad Oa standards for additional equipment, reporting requirements and specific methane emissions targets, Pelton notes.

Tribal Tax Shift

For much of the past decade, press accounts note, leaders of the Three Affiliated Tribes, whose Fort Berthold reservation produces about 20 percent of North Dakota's oil, have sought to increase their share of tax revenues generated by trust lands production. This session, lawmakers passed a bill to increase that share.

SB 2312 revises the agreement between the tribes and state to increase the tribal share of oil and gas taxes for trust land production to 80 percent from 50 percent. Conversely, the split for taxes on minerals produced within fee land was increased to 80 percent, from 50 percent for the state.

"We supported the change because a stable tax structure gives operators on the reservation greater certainty," Pelton explains. "That is expected to bring increased investment in Fort Berthold, and datasets indicate that the revenue shift will be offset with two additional rigs running."

The state has collected oil and gas taxes on Fort Berthold production since an historic agreement in 2008, under which the tribes agreed not to enact separate taxes.

"This was an issue where most everyone agreed on the long-term benefits of a stable business climate," Pelton says.

Operation Prairie Dog

Early in the proceedings, legislators resolved a local funding issue that prompted considerable debate in the weeks leading up to this year's session. Dubbed Operation Prairie Dog, HB 1066 allocates $250 million to local infrastructure projects, with an emphasis on areas impacted by oil and gas development, describes an article by Tax Commissioner Ryan Rauschenberger.

While it does allocate funding for infrastructure projects elsewhere in North Dakota, the bill provides a formula for distributing nearly a third of gross production tax revenue to counties, cities, townships and school districts in the western part of the state.

The bill will "allow western communities to continue investments in infrastructure important to workforce development, quality of life enhancement and further industry development," Pelton describes.

"This is the most positive movement for local governments we have seen in many years," a local newspaper quotes a North Dakota mayor.

Sharply Up

The industry monitored wrangling over the state's sovereign wealth fund, but did not take a position on the issue, which lawmakers ultimately moved to study during the interim, Pelton notes.

"We have long advocated for a plan that considers the road ahead," he describes. "After the somewhat stopgap measures of the past couple years, we are pleased with the decision to include the public in an interim study of the issue."

The issue boiled down to the fate of earnings generated by the $5.4 billion Legacy Fund voters approved in 2010. When state revenues fell off during the industry downturn, legislators shifted $200 million to the general fund in 2017, and this year it got $100 million from the fund, published reports note.

"The question gets down to what Legacy Fund earnings are to be used for, and how potential expenditures fit with the original intent of the fund," Pelton relates. "With that much money, everyone wants a bite at the apple."

As the industry's recovery has taken hold in the Bakken, the effect has been felt across the state's economy. A year-end report by the state's tax commissioner showed taxable sales and purchases increased 12.5 percent in 2018, the sharpest annual increase since 2012.

According to Rauschenberger's office, oil and gas development propelled 2018 taxable sales and purchases to $20.2 billion, up from nearly $18 billion in 2017. In the last 10 years, tax revenues generated by oil and gas production account for 44 percent of state tax revenue, indicates a new report co-sponsored by NDPC and the Western Dakota Energy Association.

For the 10 years ending in 2018, the state's separate oil extraction and production taxes raised almost $18 billion, of which more than $9.3 billion went to local communities and infrastructure, transportation and statewide water projects, the industry report details.

At the end of the 2019 session, legislators passed a record-setting, $14.7 billion state budget, which includes federal revenues but also reflects the increase in oil tax revenue and the effect of industry activity on the rest of the state's economy, Rauschenberger reports.

The state's general fund was approved at $4.8 billion for the next biennium, higher than the 2017-19 budget but still lower than the 2013-15 record of $6.9 billion, published reports indicate. ❒

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