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INDEPENDENT REGULATORY
REVIEW COMMISSION

Thank you Mr. Chairman. My name is Shane Flannery and I am the General Manager for Drake Manufacturing and Drake Machining. We are located in Sheffield, PA which is in Warren County, and is a fairly active area for conventional oil and gas wells. Drake manufactures series 10, 16 and 25 pump jacks that are sold through distribution locally and in other parts of the country. We also have a machine shop that supports our pump jack manufacturing as well as direct work for many local companies, many of which are oil and gas related. Drake employs about 20 people.

I am here today to voice my opinion that the proposed changes to Chapter 78 of Act 13 will have a dramatic negative impact on small businesses, like Drake. The changes being proposed for Chapter 78, Subchapter C of Act 13 - which the Environmental Quality Board accepted on August 27, 2013 for publication as a proposed rule, is the primary regulation of oil and gas operations in Pennsylvania. DEP has developed, proposed and finalized a variety of policies, permits and forms within the last twelve months that have hampered and will continue to hamper the conventional oil and gas industry, often with unclear environmental benefit.

DEP should review and revise its regulatory proposals and must provide clear direction from the central office to the regional offices where discretion should be exercised to avoid the unnecessary imposition of costs and burdens to conventional operations, which have been a core Pennsylvania industry for over a century. Regulations developed for unconventional oil and gas operations are often inappropriate for conventional operations and impose a disproportionate regulatory burden on small businesses. In oil and gas regulations, one size does not fit all.

In the long history of oil and gas production in Pennsylvania, the overall environmental impact of conventional wells, from construction through production to plugging, is minimal. Conventional operations, however, have been caught in the crossfire of increasing unconventional drilling activity in Pennsylvania. Public anxiety about the potential impacts of hydraulic fracturing has caused the rush or impulse to regulate – indeed hyper-regulate - this development activity.

Here are some recommendations to ensure the viability of the conventional oil and gas industry in Pennsylvania.

1. DEP should restructure Chapter 78 to separate those regulations that apply exclusively to unconventional operations.

Given the stark differences in the nature of conventional shallow oil and gas activities and operations compared to unconventional oil and gas development, DEP should structure

Chapter 78 in a manner that clearly identifies and separates the provisions that apply only to unconventional operations and activities.

Many of the new provisions in Act 13 focus on the operations and impacts of unconventional well development. For example, Act 13 provides for specific requirements for unconventional wells related to: permit application notification requirements and comment opportunities, notifications to DEP, water management plans, site location setbacks, presumptions of impacts to groundwater, containment requirements for unconventional well sites, record keeping requirements for flow back, air emissions, inspections and penalties. These provisions do not apply to conventional operations and any Chapter 78 rules to implement these new provisions could easily be placed into a new separate subsection for unconventional wells.

This would assist the industry in understanding its compliance obligations, and would be helpful to both DEP staff and the public as well.

The current effort to revise Chapter 78 for the implementation of these provisions creates the ideal opportunity to segregate the rules that apply only to unconventional operations. If not done in the current rule revision, this task will be much more difficult in the future.

2. DEP's PNDI Policy and proposed changes to Chapter 78 for the consideration of well permit conditions to mitigate impacts to public resources ignore the status of the oil and gas mineral owner as the holder of the dominant estate.

The "public resources" provision in Act 13 was already adopted by the legislature (in the Oil and Gas Act of 1984) at the time of the PA Supreme Court's decision in Belden & Blake Corp. v. DCNR in 2009. In that case, the Pennsylvania Supreme Court affirmed the concept that any reconciliation of surface owner disputes, whether a private person or public entity, is through negotiation. Belden & Blake makes clear that a public surface owner cannot unilaterally impose conditions on the oil and gas operator.

In contradiction of Belden & Blake, the last paragraph of 78.15 would allow the state to unilaterally impose permit conditions foregoing negotiation between the dominant tenant and the public surface owner. Regardless of its authority under Act 13 to "consider" impacts to public resources, DEP does not have unbounded authority to disregard well-established principles of Pennsylvania property law. Accordingly, DEP may not create a rule that allows public agencies to circumvent their limitations under the guise of protecting public resources.

The Pennsylvania Supreme Court has already spoken to this precise question:

A subsurface owner's rights cannot be diminished because the surface comes to be owned by the government, or any other party with statutory obligations, regardless of their salutary

nature. That is, whatever its admirable obligations to the public, as concerns the owner of private property, the government and its agencies must be held to the same standard as any other surface owner. DCNR may seek additional conditions because of its mandate, but is has no authority to impose them unilaterally without compensation. Case 969 A.3d at 532-33.

Chapter 78 may not be used to create a permitting process that directly undermines these principles.

An additional problem with DEP's proposed revision to 78.15 is the cumulative nature of the obligations. The PNDI requirements for the protection of threatened and endangered species are time consuming and sometimes require modifications of well sites, activity times or dates, and other operational sequencing. There is a cost involved with paying a professional consultant to conduct the PNDI search and those costs increase when PNDI conflicts are encountered.

DEP's proposed addition to consider and mitigate impacts to "special concern species" during the well permit process raises both legal and practical concerns because: 1) those species have never been designated as such under rulemaking by any government agency; 2) the number of such species in the PNDI database is three times as many as the threatened and endangered species combined; and 3) DEP's proposal would instantly elevate protections for hundreds of such species to the status of threatened and endangered species without any opportunity for public review.

This proposal defies all principles of administrative law and rule making protections and is beyond DEP's statutory authorization under Act 13.

3. DEP's proposed Mechanical Integrity Assessment (MIA) guidance for reviewing casing and cementing standards ignores fundamental differences in the way conventional wells operate.

There is not a compelling need to impose significant new casing, cementing and inspection standards in view of the reported number of well integrity problems. Even if there is some justification, DEP's draft MIA forms and instructions for reviewing casing and cementing standards do not fully recognize fundamental differences in the way conventional wells are cased, cemented, and/or operated as compared with unconventional wells, or the disparate impact that proposed new inspection and other assessment standards will impose on the conventional industry.

DEP reportedly has recorded approximately 128 confirmed stray gas migration cases in Pennsylvania. Only 24 of these have any connection to well integrity issues, and of those, it is not clear whether the wells were operator-owned or orphaned. A failure of 24 wells out of the

approximately 135,000 wells operating in the state – a "failure" rate of 0.02% – does not justify the proposed burden to industry generally or the conventional industry specifically. The operating pressure of a conventional well is fundamentally different than that of an unconventional well. Conventional wells typically operate at only hundreds of psi of pressure or less, which means the surface shut-in pressure and surface producing back pressure inside the surface casing does not exceed the 0.433 psi standard set forth in 25 Pa. Code § 78.73(c). (If greater pressure than the 0.433 psi standard is encountered in a conventional well the industry practice is to introduce a second string of casing so that the surface casing is not exposed to that greater pressure.) This in turn means that if a shallow conventional well loses integrity, groundwater would migrate into the well bore, not the other way around where there would be a risk of gas or other fluids migrating from lower formations into fresh groundwater.

Much of the DEP's commentary during the recent MIA meetings and workshops seems not to have fully appreciated this point or the economic impact that new MIA program will have on small businesses.

The impact of the new MIA form is very significant to them. Using DEP's formula, it appears that a minimum of 1 additional employee may be required for every 500 wells. A conservative "all-in" cost to hire an inexperienced, entry-level employee would be approximately $65,000-$70,000 a year per 500 wells. Implementing the MIA guidance will be very work-intensive at the outset – educating existing technical staff (or creating a new position requiring additional team members) in inspection imperatives, constructing an inspection template compatible with the MIA form for each technician to use in the field, and training an office position with some knowledge of well mechanics to transfer the data from the field to the electronic MIA form. DEP has not fully considered this significant economic impact.

Conventional production should be allowed to comply with Section 78.88 as it is written, and categorically excluded from the new MIA program, for all the reasons stated above.

In summary, now is the appropriate time to restructure Chapter 78 to separate regulations and policy for conventional and unconventional oil and gas wells. It is vitally important to not impose undue financial and regulatory burdens on the conventional operators. This will allow these small independent companies to prosper and in turn will allow companies like Drake to grow and prosper.

Thank you and good evening.