

In 2012, the North Carolina General Assembly legalized “fracking” in North Carolina, overriding a veto of then Governor Bev Perdue. This rolled back state laws dating back to 1945 that prohibited horizontal drilling and the injection of wastes into wells, creating a *de facto* ban on hydraulic fracturing (“fracking”). The law placed a moratorium on the issuance of permits “until the General Assembly takes legislative action to allow the issuance of such permits,” and approves regulations crafted by the Mining and Energy Commission (“MEC”). Because North Carolina has no active oil and gas production, there is no comprehensive regulatory program for the oil and gas industry. The law therefore reconstituted North Carolina’s Mining Commission as the Mining and Energy Commission, and charged that body with creating the rules that will govern gas extraction in North Carolina.

The MEC is divided into six committees that draft the rules, which are then voted on by the full Commission. The six committees are: mining, civil penalty remissions, environmental standards, water and waste management, administration of oil and gas, and rules. Study groups, comprised of MEC members and other interested stakeholders, were also formed to look into specific issues: compulsory pooling, local government regulation, coordinated permitting, trade secrets, and funding levels and sources. The full set of regulations is scheduled to be completed by the MEC in May 2014. There will be three public hearings in June and July of 2014, and the public comment period is currently scheduled for June 2 through August 1, 2014. The MEC is then scheduled to adopt the final rules in September 2014, and the legislature is expected to act on the rules in the 2015 long session.

The 2013 legislative session saw repeated attempts to lift the moratorium on issuing drilling permits until all safety rules are written and the legislature votes to approve those rules.

- On of these bills, Senate Bill 76, known for most of the session as “the fracking bill,” but titled “The Domestic Energy and Jobs Act” ultimately passed and became law in July, 2013. The final version of the bill, however, promotes offshore drilling, but does NOT include some of the worst provisions proposed by the Senate, including fast-tracking permitting before regulations are completed and allowing underground injection of fracking wastes.
  - As introduced, this bill would have allowed for injecting flowback fluid and produced waters, the waste of a fracking operation, deep underground. This would have rolled back 40 years of state law. From 1968 to 1972, Hercules, a company that manufactured the raw materials used in the production of polyester fabrics, used coastal aquifers for chemical injection. The wells clogged and leached chemicals into a sand, gravel and limestone aquifer. Monitoring wells in upper aquifers later showed that the chemicals also traveled past a clay containment zone and contaminated upper aquifers. That underwater leakage led to the state’s ban on deep injection wells. DENR, in a 484-page report published in 2012, urged against legalizing deep disposal of fracking wastes, and state geologists say the underground geology west of Raleigh is not porous enough to absorb fluids, forcing the pressurized injections to seek fissures and faults, potentially contaminating freshwater supplies. Further, an EPA assessment of industrial waste injection sites nationwide classified western North Carolina as unfavorable under all conditions and coastal North Carolina as unsuitable under most conditions. We (the environmental lobby) were able to fight back this provision. Coastal legislators were

vocal in their opposition as were local governments, several of which passed resolutions against the underground injection of fracking wastes.

- The bill also would have prohibited local governments from taxing any aspect of oil or gas extraction, hindering the ability of local governments to adequately address negative impacts from oil and gas exploration and development activities.
- Eliminated the requirement that DENR establish a registry of landmen operating in North Carolina. Eliminating this requirement would have limited DENR's access to information about entities operating in North Carolina, and would relieve operators from the obligation to provide the agency with information about their record in other states. The final version of the bill instead directed the MEC to study "issues related to establishment and implementation of the registration requirements for landmen."
- On the final days of session, there was a last ditch effort to pass a bill that would lift the moratorium, when fracking provisions were inserted in Senate Bill 127, which dealt with the reorganization of the N.C. Department of Commerce. This attempt, however, also failed.
- House Bill 74, which was signed into law in August, 2013, also touches on the fracking issue, as it weakens protections of groundwater, and limits environmental ordinances.

We expect to see more energy legislation in the 2014 short session, which convenes mid-May and will likely wrap up by the end of June. There were rumors of Governor McCrory convening a special session to address energy issues, but this no longer appears likely. They could certainly try again to lift the moratorium early and allow permitting to occur before the rules are finalized. Other topics we might see include:

- Forced pooling - Forced Pooling, or "compulsory pooling," is used to create a drilling unit by forcing non-consenting landowners into participating in a proposed drilling unit. Gas companies like it because it maximizes recovery. But it also takes away a property owner's right to control his or her own mineral resource. Approximately 40 states authorize forced pooling, but it is not necessary for fracking to occur. For example, Pennsylvania and West Virginia (which both contain the Marcellus shale formation) do not allow forced pooling. The North Carolina Oil and Gas Conservation Act authorizes the use of forced pooling in NC, but is silent on the details of how it should be accomplished, and the legislature is expected to act to clear this up. For example, what is the minimum acreage that must be leased before the other landowners in the drilling unit are pulled along? Senate Bill 820, which legalized fracking, directed the MEC to study the State's current law on integration or compulsory pooling and to report its findings and recommendations to the legislature. The compulsory pooling study group submitted their recommendations to the full MEC ahead of the October 1<sup>st</sup> deadline, recommending a 90% acreage requirement, which in Lee County could still force pool 55% of landowners. Although DENR did submit the report to the Joint Legislative Commission on Energy Policy and the Environmental Review Commission as planned, they also recommended that "prior to establishing new laws related to compulsory pooling, the General Assembly should consider the rules adopted by the Mining and Energy Commission related to oil and gas exploration." In other words, they recommended that the legislature wait to decide on the details of forced

pooling until they have the entire suite of rules before them. As such, it is uncertain if this issue will come up in the 2014 short session.

- Waste disposal – Over years of gas production, a single well can produce millions of gallons of waste fluids that can contain many pollutants. These pollutants include naturally occurring chemicals derived from formation water in addition to chemicals added to fracturing fluid. Federal hazardous waste storage, transportation, and disposal requirements do not apply to wastewater produced through shale gas extraction, and regulatory decisions regarding wastewater treatment and disposal are therefore left to the states. The options for wastewater disposal include injection into underground disposal wells, partial treatment at publicly owned treatment works (POTWs) followed by discharge into nearby surface water, land application, commercial wastewater treatment, and reuse in future hydraulic fracturing operations. North Carolina law currently prohibits the injection of fracking waste underground. Even if the ban were lifted, the state may not possess suitable geologic storage formations. Therefore, if the state did lift the ban on underground injection, other disposal methods for wastewater produced through shale extraction may be necessary. The MEC is working on this issue, but we will be vigilant in case the legislature decides to move forward on this issue.
- S76 directed MEC to conduct three additional studies, and we may see legislation pertaining to the results of the studies in the 2014 session. The MEC was directed to study: “the development of a coordinated permitting program for oil and gas exploration and development activities,” “an appropriate rate of severance tax that should be imposed in association with oil and gas exploration and development activities,” and “issues related to establishment and implementation of the registration requirements for landmen.”
- In November, representatives from the American Petroleum Institute (API), the American Natural Gas Alliance (ANGA) and the Interstate Oil and Gas Compact (IOGC) provided recommendations to the Joint Legislative Commission on Energy Policy on what North Carolina should include in a modern oil and gas statute. Based that presentation, we will be watching for revisions to the landowner protection section of the NC law – according to the presenters goes way beyond national standard and creates economic and operation disincentive for operators. Will also watch for the creation of development incentives – discovery well tax incentives, high cost well payout provisions, secondary recovery tax credits to incentivize complete extraction.