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Colorado Oil and Gas Update

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COLORADO OIL AND GAS UPDATE

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I. INTRODUCTION

During the past year, a number of important judicial decisions and regulatory actions concerning oil and gas development occurred in Colorado. These decisions and actions should be of interest to all persons who are involved in Colorado oil and gas activity.

II. JUDICIAL DEVELOPMENTS

In *Colorado Oil & Gas Conservation Commission v. Grand Valley Citizens' Alliance*, the Colorado Supreme Court addressed the public's right to request formal hearings before the Colorado Oil and Gas Conservation Commission ("Commission") on various matters, including applications for permits to drill ("APDs").[1] The case arose out of a petition that several organizations and individuals filed with the Commission seeking hearings on APDs for wells located approximately three miles from Project Rulison.[2] Because Commission regulations do not authorize members of the public to request such hearings, the petition was treated as a complaint, and no hearing was

1. Colo. Oil & Gas Conservation Comm'n v. Grand Valley Citizens' Alliance, 279 P.3d 646 (Colo. 2012) (en banc).

2. *Id.* at 647–48. Project Rulison was the site of a 1969 underground nuclear detonation, and the petitioners alleged that the APDs therefore raised issues of public health, safety, and welfare. *Id.* at 647, 649.

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held.[3] After the Commission conditionally approved the APDs, the petitioners filed a lawsuit in Denver District Court.[4] The district court dismissed the lawsuit, but the court of appeals reversed.[5] In a potentially sweeping decision, the court of appeals held that the Commission is statutorily required to hold a hearing in response to any petition involving a matter within its jurisdiction, including APDs.[6]

The Colorado Supreme Court's review turned on its analysis of the Colorado Oil and Gas Conservation Act ("Conservation Act").[7] The court of appeals had based its decision upon section 108(7) of the Conservation Act, which states that "[o]n the filing of a petition concerning any matter within the jurisdiction of the [C]ommission, it shall promptly fix a date for a hearing thereon . . . ."[8] The Colorado Supreme Court concluded, however, that this provision refers to a hearing on a rule, regulation, or order.[9] The Court based this conclusion upon other language in section 108, as well as other provisions of the Conservation Act that specifically require hearings in certain circumstances or distinguish between rules, orders, and permits.[10] The Court further concluded that permits are governed by section 106(1)(f), which grants the Commission broad authority to promulgate regulations governing permitting, including authority to specify who may request a hearing.[11] Because Commission regulations do not authorize members of the public to seek APD hearings, the Commission properly denied the petition at issue.[12] The decision affirms the Commission's longstanding practices of defining by regulation who may request hearings on matters not involving rules, regulations, and orders and not allowing members of the public to request hearings on APDs. As the Court noted, members of the public may still voice their concerns, but they must do so through the submittal of comments and complaints.[13]

Another Colorado Supreme Court decision, *Larson v. Sinclair Transportation Co.*, addressed the use of eminent domain for petroleum pipelines.[14] That case arose out of a transportation company's condemnation of an easement across private property for the purpose of constructing an underground gasoline pipeline.[15] The Weld County

3. *Id.* at 647.
4. *Id.*
5. *Id.*
6. *Id.* at 648.
7. *Id.* at 648–49; COLO. REV. STAT. § 34-60-101 (2012).
8. *Colo. Oil & Gas Conservation Comm'n*, 279 P.3d at 648; COLO. REV. STAT. § 34-60-108(7) (2012).
9. *Colo. Oil & Gas Conservation Comm'n*, 279 P.3d at 648.
10. *Id.*
11. *Id.* at 649; COLO. REV. STAT. § 34-60-106(1)(f) (2012).
12. *Colo. Oil & Gas Conservation Comm'n*, 279 P.3d at 649.
13. *Id.*
14. Larson v. Sinclair Transp. Co., 284 P.3d 42 (Colo. 2012) (en banc).
15. *Id.* at 43.

District Court ruled that the company could condemn the property for this purpose pursuant to a Colorado statute that grants such authority to "telegraph, telephone, electric light power, gas, or pipeline compan[ies]."[16] The court of appeals affirmed this ruling on the ground that the condemning party was a "pipeline company" under the statute.[17] But the Colorado Supreme Court reversed in a four to three decision.[18] It held that the statutory language does not encompass pipelines that transport petroleum.[19] Instead, the Court narrowly construed the term "pipeline company" to refer only to pipelines that deliver electric power, such as those encasing underground electric wiring.[20] In reaching this result, it noted that the statute does not refer to petroleum products and therefore does not expressly grant condemnation authority for pipelines conveying such substances.[21] The Court also found that the statute does not implicitly convey such authority based on Colorado precedent that narrowly interprets condemnation statutes generally and on other statutory language and legislative history that it read to indicate that the statute as a whole concerns electric power infrastructure.[22] Accordingly, it held that the transportation company lacked authority to condemn the easement at issue.[23]

In *Chase v. Colorado Oil & Gas Conservation Commission*, the Colorado court of appeals addressed the adequacy of the Commission's administrative findings in a hearing on a split estate dispute.[24] In that case, the surface owners of an equestrian facility opposed oil and gas development and requested that the Commission deem the facility a Designated Outdoor Activity Area ("DOAA"), which would increase the well setback requirements.[25] The Commission denied the surface owners' request based on concerns that the facility did not fit within the DOAA definition or regulation and that such a designation would create waste.[26] The Commission also denied on jurisdictional grounds the surface owners' request that it interpret the mineral owner's lease, and it approved the third-party lessee's APD for the property subject to various conditions proposed by the surface owners.[27] The Denver District Court upheld the Commission's actions.[28] The court of ap-

16. *Id.*; COLO. REV. STAT. § 38-5-105 (2012).
17. *Larson*, 284 P.3d at 43.
18. *Id.* at 46.
19. *Id.* at 44–46.
20. *Id.* at 45.
21. *Id.* at 44, 46.
22. *Id.* at 45.
23. *Id.* at 46.
24. Chase v. Colo. Oil & Gas Conservation Comm'n, 284 P.3d 161, 165 (Colo. App. 2012).
25. *Id.* at 163.
26. *Id.* at 164.
27. *Id.*
28. *Id.* at 165.

peals likewise upheld the Commission's determination that it lacked jurisdiction to interpret the mineral lease.[29] The court of appeals also upheld the Commission's consideration of whether a DOAA designation would create waste because waste is specifically mentioned in the Conservation Act.[30] But the court of appeals concluded that the Commission's order did "not contain sufficient factual findings explaining why the [Commission] denied the DOAA."[31] The court of appeals therefore remanded the case so that the Commission could prepare "detailed findings of facts, including assessments of the evidence and testimony, and conclusions of law" regarding its denial of the DOAA.[32]

Two decisions by the United States District Court for the District of Colorado addressed analyses of future oil and gas development on federal land under federal environmental and public land statutes. In *Natural Resources Defense Council v. Vilsack*, the district court upheld a Forest Service environmental assessment and finding of no significant impact for a project involving up to forty-five natural gas wells, the construction of six well pads, and the creation of six miles of access road in Western Colorado.[33] At the outset, the court found that the plaintiff environmental organizations had adequately established standing, explaining that even generalized harm, limited causation, and minimal redressability are sufficient for this purpose.[34] However, the court held that the federal agencies had satisfied their environmental obligations under the National Environmental Policy Act ("NEPA"),[35] National Forest Management Act,[36] and Federal Land Policy and Management Act ("FLPMA").[37] Although the Forest Service did not model or otherwise quantitatively analyze the project's effect upon ozone because of the complexity and cost involved, the court determined that the agency's decision not to do so was entitled to deference and did not constitute arbitrary or capricious conduct.[38] The court also noted that the agency's analysis of ozone precursors did not indicate a violation of applicable air quality standards, that its analysis of visibility did not indicate a violation of Forest Plan require-

29. *Id.* at 167–68.

30. *Id.* at 170.

31. *Id.* at 171.

32. *Id.* at 171–72.

33. Natural Res. Def. Council v. Vilsack, No. 08-cv-02371-CMA, 2011 WL 3471011, at *1 (D. Colo. Aug. 5, 2011).

34. *Id.* at *3–6.

35. National Environmental Policy Act of 1969, 42 U.S.C. §§ 4321, 4331–4335, 4341–4347 (2006).

36. National Forest Management Act of 1976, 16 U.S.C. §§ 1600–1614, 472(a), 521(b) (2006 & Supp. 2011).

37. Federal Land Policy and Management Act, 43 U.S.C. §§ 1701–1702, 1711–1723, 1731–1748, 1751–1753, 1761–1771, 1781–1782 (2006 & Supp. 2011).

38. *Vilsack*, 2011 WL 3471011, at *9.

ments, and that it had set forth a plan for addressing cumulative visibility issues.[39]

In *Colorado Environmental Coalition v. Salazar*, the district court found deficient a Bureau of Land Management ("Bureau") environmental impact statement for the Roan Plateau Planning Area, which covers more than 120,000 acres in western Colorado.[40] The Bureau had prepared the statement at issue for a new Resource Management Plan, which was intended to coordinate public land management and facilitate mineral leasing as directed by the 1997 Transfer Act.[41] A number of environmental organizations challenged the Bureau's actions under NEPA and FLPMA.[42] The court upheld the Bureau's elimination of a proposed alternative that would have prohibited most leasing of land atop the Plateau because it did not comport with the Transfer Act's leasing requirements and because most of its features were included in other alternatives that were analyzed.[43] The court upheld the Bureau's justification of a twenty-year planning horizon for assessing environmental effects on the ground that longer forecasts would be speculative and unreliable.[44] The court also upheld the Bureau's broad analysis of cumulative effects on elk and mule deer, which essentially found that the effects from future drilling on private land outside the planning area would be proportional to the effects from future drilling on federal and private land within the planning area.[45]

The court concluded, however, that the Bureau's elimination of a community-proposed alternative and its analyses of air quality effects violated NEPA.[46] The court found that the community alternative was a reasonable alternative that warranted consideration in the environmental impact statement because it was consistent with the purpose of the proposed action, it was distinct from the other alternatives, and it was not treated as infeasible by the Bureau at the time of the decision.[47] The court also found that the Bureau failed to take a hard look at the cumulative air quality effects; the court noted that the Bureau had considered the air quality effects of future development on federal and private land within the planning area, but it had neither included the effects of future development on private land outside the planning area nor adequately explained why such information could

39. *Id.* at *10–11.

40. Colo. Envtl. Coal. v. Salazar, No. 08-cv-01460-MSK-KLM, 2012 WL 2370067, at *1, *20 (D. Colo. June 22, 2012).

41. *Id.* at *2; 10 U.S.C. § 7439 (2006).

42. *Colo. Envtl. Coal.*, 2012 WL 2370067, at *5.

43. *Id.* at *8–10.

44. *Id.* at *11–13.

45. *Id.* at *14–15.

46. *Id.* at *10–11, *15–19.

47. *Id.* at *10–11.

not be obtained.[48] Similarly, the court ruled that the Bureau failed to take a hard look at the potential ozone effects, either by conducting ozone modeling, by assessing future levels of ozone precursors, or by providing a more detailed explanation for its conclusions.[49] The court therefore set aside the decision embodied in the Resource Management Plan and remanded the matter to the Bureau, but the court did not cancel the leases that the Bureau had issued.[50]

As in several other oil and gas producing states, plaintiffs have filed lawsuits in Colorado alleging harm from hydraulic fracturing. In one of these cases, *Strudley v. Antero Resources Corp.*, the Denver District Court issued a special case management order, known as a Lone Pine order, and ultimately dismissed the case.[51] Before full discovery or other pretrial activities could proceed, the order required the plaintiffs to make a prima facie showing of exposure, injury, and causation.[52] The court issued the order because of "the significant discovery and cost burdens presented by a case of this nature" and because "ultimately [the plaintiffs] would need to come forward with this data and expert opinions in order to establish their claims."[53] The court also "relied on" an investigation by the Commission that determined that the "[p]laintiffs' well water was not affected by oil and gas operations" and on affidavits from defendants "that their activities were conducted in compliance with applicable laws and regulations."[54]

In response, the plaintiffs submitted some sampling data, letters from a chemist stating equivocally that the sampling results could be consistent with gas well contamination, and a toxicologist's affidavit noting a temporal connection between the plaintiffs' injuries and the defendants' activities and recommending that discovery proceed.[55] The court found this insufficient to establish the prima facie elements of the plaintiffs' case as required by the order:

> all [plaintiffs' expert] conclusively opines on is that 'sufficient environmental and health information exists to merit further substantive discovery.' Significantly, [plaintiffs' expert] makes no opinion as to whether exposure was a contributing factor to [p]laintiffs' alleged injuries or illness .... Plaintiffs' requested march towards discovery without some adequate proof of causation of injury is precisely what the [Lone Pine order] was meant to curtail.[56]

48. *Id.* at *15–17.
49. *Id.* at *17–19.
50. *Id.* at *19.
51. Strudley v. Antero Res. Corp., No. 2011CV2218, 2012 WL 1932470, at 2, 4 (Colo. Dist. Ct. May 9, 2012). Lone Pine orders originated in the case of Lore v. Lone Pine Corp., No. L-33606-85, 1986 WL 637507, at *4 (N.J. Super. Ct. Nov. 18, 1986).
52. *Strudley*, 2012 WL 1932470, at 2.
53. *Id.*
54. *Id.*
55. *Id.* at 2–3.
56. *Id.* at 3.

Accordingly, the court dismissed the plaintiffs' claims with prejudice, and the decision is currently on appeal.[57]

Finally, two preemption cases are pending in the Colorado courts: *SG Interests I, Ltd. v. Board of County Commissioners of Gunnison County*[58] and *Colorado Oil and Gas Conservation Commission v. City of Longmont*.[59] The *Gunnison County* case involves a lawsuit by an owner and operator of oil and gas interests seeking to invalidate county oil and gas regulations as preempted by amendments to the Conservation Act and the Commission's implementing regulations.[60] The challenged county regulations address a laundry list of issues, including well permitting, wildlife, water quality, water wells, cultural and historic resources, geologic hazards, mitigation, access to records, and financial guarantees.[61] In September 2011, the court denied partial summary judgment on the owner and operator's claims for express and implied preemption.[62] The court concluded that state law and regulations do not express a legislative intent to prohibit local land use authority over oil and gas development.[63] The court also found that the state's interest in oil and gas activity is not so dominant as to impliedly preempt such local authority.[64] In January 2012, the court determined that there is no operational preemption as a matter of law and that an evidentiary hearing would be required to address the issue.[65]

The *City of Longmont* case involves a lawsuit by the Commission seeking to invalidate portions of the city's new oil and gas ordinance as preempted by state law and regulations.[66] The challenged provisions prohibit surface facilities and operations in residential areas; address the use of multi-well pads and directional and horizontal drilling; impose requirements regarding setbacks, wildlife habitat protection, chemical reporting, visual mitigation, and water quality testing; and set forth a process for resolving operational conflicts.[67] Several of these provisions directly or indirectly address hydraulic fracturing, in-

57. *Id.* at 4.

58. Complaint, SG Interests I, Ltd. v. Bd. of Cnty. Comm'rs, No. 11CV127 (Colo. Dist. Ct. June 2, 2011).

59. Complaint for Declaratory Relief, Colo. Oil & Gas Conservation Comm'n v. City of Longmont, No. 12CV702 (Colo. Dist. Ct. July 30, 2012).

60. Complaint, *supra* note 58, at ¶¶ 1, 3, 162.

61. *Id.* ¶¶ 103–61.

62. Order on Plaintiff's Motion for Partial Summary Judgment as it Relates to the Fourth Claim for Relief and Defendant's Motion to Dismiss or in the Alternative Partial Summary Judgment at 5–6, SG Interests I, Ltd. v. Bd. of Cnty. Comm'rs, No. 11CV127 (Colo. Dist. Ct. Sept. 16, 2011).

63. *Id.*

64. *Id.*

65. Order of Cross Motions for Partial Summary Judgment at 5–6, SG Interests I, Ltd. v. Bd. of Cnty. Comm'rs, No. 11CV127 (Colo. Dist. Ct. Jan. 3, 2012).

66. Complaint for Declaratory Relief, *supra* note 59, at Introduction & Prayer for Relief.

67. *Id.* ¶¶ 42–116.

cluding those regarding chemical reporting and water quality testing. The Commission believes that all of these provisions involve "the regulation of oil and gas operations which, if countenanced, will undermine the Commission's statutory charge to foster the responsible development of Colorado's oil and gas resources in a manner consistent with the protection of public health, safety, and welfare, including protection of the environment and wildlife resources."[68]

III. Regulatory Developments

In August 2011, the Commission comprehensively amended Rule 318A—its Greater Wattenberg Area special well location, spacing, and unit designation rule—which governs the location of wells in the Greater Wattenberg Area north of Denver.[69] The amendments became effective on September 30, 2011, for all of the area except the City and County of Broomfield, and the Commission is expected to extend the Rule 318A amendments to Broomfield during the summer or fall of 2012.

Rule 318A generally authorizes the comingling of certain hydrocarbon resources; creates defined drilling locations; establishes procedures for adaptive spacing units; provides for the location of interior infill and boundary wells; and limits the number of producing completions per quarter section.[70] The Commission amended these requirements to reduce the number of well-location exceptions associated with the Niobrara Formation development and provide for additional environmental reporting.[71] Among other things, the amendments allow for smaller wellbore spacing units[72] and for flexible horizontal wellbore spacing sizes.[73] They also establish notice and hearing procedures for wells utilizing these concepts[74] and eliminate the limitation on the number of wellbore completions per quarter section.[75] From an environmental standpoint, they extend water well sampling requirements to the entire area[76] and require operators to file waste management plans.[77]

In December 2011, the Commission adopted a package of new and amended regulations to mandate the public disclosure of hydraulic

68. *Id.* at Introduction.
69. 2 Colo. Code Regs. § 404-1:318A (LexisNexis 2012).
70. *Id.*
71. *Amendments to Current Rules of the Colorado Oil and Gas Conservation Commission, 2 CCR 404-1, Amending Rule 318A*, Colo. Oil & Gas Conservation Comm'n, 2 (2011), http://cogcc.state.co.us/rr_docs_new/GWA2011/GWA2011StatementBasisPurpose.pdf.
72. 2 Colo. Code Regs. § 404-1:318Aa(4)C (LexisNexis 2012).
73. *Id.* § 404-1:318Aa(4)D.
74. *Id.* § 404-1:318Ae(6).
75. *Id.* § 404-1:318Af.
76. *Id.* § 404-1:318Ae(4).
77. *Id.* § 404-1:318Ah.

fracturing fluid chemicals. These new requirements became effective April 1, 2012, and build upon regulatory amendments adopted in 2008, which required the disclosure of such chemicals to state regulators and health professionals upon demand, and upon the voluntary public disclosure of such chemicals by certain operators through the "FracFocus" website.[78]

The centerpiece of the new disclosure regime is Rule 205A. It imposes tiered requirements on chemical vendors, service companies, and operators—vendors and service companies must provide chemical disclosure information to operators within thirty days after a hydraulic fracturing treatment is concluded, and operators must then post this information on the FracFocus website within sixty days after the treatment is concluded.[79] The information is posted in a standard format and includes data on the well and the fracturing treatment; information on additives, that is, trade products, may be reported separately from information on chemicals and concentrations in an attempt to reduce the need for trade secret claims.[80] All chemicals and chemical concentrations must be disclosed unless they constitute a trade secret.[81]

If information is withheld as a trade secret, the trade secret claimant must submit a new Form 41 to the Commission.[82] This form provides contact information for the claimant, justification for the claim, and certification of the claim's legitimacy.[83] Trade secret claims are subject to challenge through the Commission and the courts,[84] and trade secret information must still be promptly provided to the Commission and health professionals under certain circumstances.[85]

As part of the APD process, operators are required to provide surface owners with a standard information sheet on hydraulic fracturing.[86] Operators are also required to provide the Commission with at least forty-eight hours' notice before a hydraulic fracturing treatment occurs, and the Commission forwards this information to the local government.[87] The regulations also provide that the Commission will develop its own database if the FracFocus website does not become

78. *See* www.fracfocus.org. The website was developed and is administered by the Ground Water Protection Council and the Interstate Oil and Gas Compact Commission, both of which are interstate organizations of state regulators.

79. 2 COLO. CODE REGS. § 404-1:205A(b)(1)–(2) (LexisNexis 2012).

80. *Id.* § 404-1:205A(b)(2)(A).

81. *Id.* § 404-1:205A(b)(2).

82. *Id.* § 404-1:205A(b)(2)(C).

83. *Form 41: Trade Secret Claim of Entitlement*, COLO. OIL & GAS CONSERVATION COMM'N (Dec. 2011), http://cogcc.state.co.us/forms/PDF_Forms/Form41_0531 2012.pdf.

84. 2 COLO. CODE REGS. § 404-1:522(a)(1) (LexisNexis 2012); *see also* COLO. REV. STAT. § 34-60-114 (2012).

85. § 404-1:205A(b)(5), (d)(2).

86. 2 COLO. CODE REGS. § 404-1:305(e)(1)(A) (LexisNexis 2012).

87. 2 COLO. CODE REGS. § 404-1:316C (LexisNexis 2012).

searchable by chemical and time period by approximately January 2013.[88] The Commission plans to issue a report in April 2013 on the frequency of trade secret claims and any issues arising in connection with such claims.

In February 2012, Governor Hickenlooper created a task force to identify mechanisms to better coordinate state and local regulation of oil and gas development to better protect public health and the environment, avoid duplication and conflict, and encourage responsible development.[89] The task force's April 18, 2012, report did not recommend any new laws or regulations; instead, it recommended "a collaborative process through which issues can be resolved without litigation or new legislation."[90] To this end, the task force made several recommendations for strengthening the Commission's local government designee program and offered a series of protocols for education and outreach, inspections, and reporting and response.[91] The Commission subsequently conducted a series of stakeholder meetings during the spring and summer to discuss the issue of well setbacks. Several groups have urged modifications to the current setback requirements set forth in Rule 603, and the Commission initiated rulemaking on this subject in October of 2012.[92]

In April 2012, the Commission issued a notice to operators to clarify hydrogen sulfide reporting requirements under Commission Rule 607 and Bureau of Land Management Onshore Order No. 6.[93] The notice provides detailed guidance on when hydrogen sulfide reporting and planning are required, what information should be included, and how certain measurements should be calculated.[94]

Effective June 1, 2012, the Commission revised its Form 5A Completed Interval Report to include additional information on the well completion process.[95] As revised, the form requires operators to provide information on the total fluid, gas, acid, and proppant used in the

88. *Id.* § 404-1:205A(b)(3).

89. Colo. Exec. Order No. B 2012-002 (Feb. 29, 2012), *available at* http://www.colorado.gov/cs/Satellite/GovHickenlooper/CBON/1251616203275.

90. Press Release, John Hickenlooper, Governor of Colo., Oil and Gas Task Force Makes Recommendations Related to State and Local Regulatory Jurisdiction (Apr. 18, 2012), *available at* http://www.colorado.gov/cs/Satellite/GovHickenlooper/CBON/1251621390178.

91. *Id.*

92. *Notice of Rulemaking Hearing*, COLO. OIL & GAS CONSERVATION COMM'N (Oct. 15, 2012), http://cogcc.state.co.us/RR_HF2012/setbacks/NoticeRulemakingRESetbacksv2_1_.pdf.

93. *Notice to Operators Reporting Hydrogen Sulfide (H_2S): Clarifications for Implementation of COGCC Rule 607 and BLM Onshore Order No. 6*, COLO. OIL & GAS CONSERVATION COMM'N (Apr. 13, 2012), http://cogcc.state.co.us/RR_Docs_new/Policies/H2S_Guidance.pdf.

94. *Id.*

95. *Form 5A: Completed Interval Report*, COLO. OIL & GAS CONSERVATION COMM'N (June 2012), http://cogcc.state.co.us/forms/PDF_Forms/Form5A__20120705.pdf.

treatment, together with the amount of recycled and fresh water utilized.[96] Information is also required on the volume and disposition of flowback as well as whether green completion techniques were utilized.[97] Operators must file this information with the Commission within thirty days after a formation is completed.[98]

96. *Id.*
97. *Id.*
98. 2 COLO. CODE REGS. § 404-1:308B (LexisNexis 2012).