

COLORADO'S SWEEPING OIL AND GAS LAW: ONE YEAR LATER

To Our Clients and Friends:

A year ago, Colorado ushered in a new era of oil and gas regulation when Governor Jared Polis signed Senate Bill 19-181 (“**SB-181**”) into law.^[1] For opponents of oil and gas development, SB-181 represented a significant victory—and a reversal of fortune. Over the course of the previous year, Colorado voters had soundly defeated Proposition 112, a statewide initiative that would have mandated aggressive setback rules for new wells,^[2] and the Colorado Supreme Court issued its unanimous decision in *Martinez v. Colorado Oil and Gas Conservation Commission*, which upheld a decade’s worth of rulemaking by the Colorado Oil and Gas Conservation Commission (“**COGCC**”) under the state’s prior regulatory regime.^[3]

In response to these developments, newly elected Governor Polis, with the support of a Democratic majority in both houses of the Colorado General Assembly, vowed to push for legislation to “reform” the COGCC and “make sure health and safety are prioritized.”^[4] The result was SB-181, which was touted as a solution to the long-simmering “oil and gas wars” between environmental activists and industry groups in the state.^[5]

A year has now passed since the signing of SB-181. In that time, the COGCC and other state regulators have begun the process of implementing the law. It has become clear, however, that the “oil and gas wars” are not over. Rulemaking at the COGCC remains contentious, and local governments continue to flex their muscles and threaten to significantly restrict oil and gas development within their borders. Meanwhile, legal challenges to these regulations are likely on the horizon, and voters may once again be asked to decide whether to impose new regulations on the industry when they head to the ballot box for this year’s election. While the current COVID-19 crisis and the related turmoil in global markets have recently dominated concerns about the future of oil and gas development in Colorado, determining the state’s long-term regulatory scheme remains a top priority for both the proponents and opponents of Colorado’s oil and gas industry.

A Recap of SB-181’s Major Changes

SB-181 made fundamental changes to Colorado’s regulatory structure for the oil and gas industry, in some cases reversing assumptions that had been a part of state law for decades.

First, SB-181 granted local governments power to regulate future oil and gas development within their jurisdictions, including the power to preempt less restrictive statewide regulations promulgated by the COGCC.^[6] This decentralization of authority was a dramatic shift in Colorado’s regulatory approach. In the decades before SB-181, lawmakers had been hesitant to grant local governments significant

control over the industry. Doing so, they feared, would lead to an impractical patchwork of regulations across the state.^[7] SB-181 was an about-face: a local government may now impose oil and gas regulations that are stricter than those promulgated by the COGCC, and those stricter rules will govern oil and gas development within the local government’s jurisdiction.^[8] SB-181’s only limitations on local regulatory powers are that these powers must be exercised in a “reasonable manner” and any regulations imposed on the industry must be “necessary and reasonable” to protect public health and the environment—limitations that are undefined and have yet to be tested by the courts.^[9]

Second, SB-181 altered the overall mission of state regulators. Previously, the COGCC was charged with a statutory mandate to “foster” development of oil and gas resources to achieve the “maximum efficient rate of production.”^[10] Protection of public health and the environment was a significant goal, but the COGCC pursued that goal in tandem with oil and gas development. Now, under SB-181, the COGCC is required to “regulate”—not “foster”—oil and gas development in Colorado, and it must do so “in a manner that protects” public health and the environment.^[11] In effect, SB-181 required the COGCC to reevaluate its regulatory approach while deemphasizing full utilization of state oil and gas reserves. Consistent with this “mission change,” the COGCC is required to collaborate with the Colorado Department of Public Health and Environment (“CDPHE”) to address the “cumulative impact” of oil and gas development.

Third, SB-181 called for the restructuring and professionalization of the COGCC.^[12] Previously, the COGCC was composed of nine members. Seven were unpaid volunteers, three of whom were required to have substantial experience in the oil and gas industry.^[13] By July 1, 2020, however, membership will be reduced by two commissioners, and each of the seven will be paid, full-time government employees. Five will be newly appointed by the Governor, only one of which is required to have industry experience. The remaining two are the Executive Directors of the Colorado Department of Natural Resources and CDPHE, who will serve as *ex officio* non-voting members.^[14] SB-181 mandates that the newly appointed commissioners be free from conflicts of interest, which are defined to include working as a registered lobbyist at the state or local levels, serving in the Colorado General Assembly within the past three years, or serving in an official capacity with an entity that advocates for or against oil and gas activity.^[15] The COGCC began accepting applications for the full-time commissioner positions in January 2020, but Governor Polis has not yet announced his nominations.^[16]

Delays in the Statewide Rulemaking Process

To implement its wide-reaching reforms, SB-181 required the COGCC to undertake major rulemaking initiatives on a range of subjects, including (1) updates to the COGCC’s hearing procedures (the so-called “500 Series” rules); (2) public disclosure of flowline locations; (3) criteria for the selection of drilling sites, including consideration of alternative locations; (4) wellbore integrity; (5) minimizing the cumulative impact of oil and gas development (in consultation with the CDPHE); and (6) the overall “mission change” of the COGCC.^[17] In addition, SB-181 instructed CDPHE to establish rules to minimize air and water pollution generated from exploration and development activities.^[18]

All of these rules were initially scheduled to be finalized by July 1, 2020, before the transition in the COGCC’s structure and membership.^[19] But the rulemaking process has proved more contentious than

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expected and has been plagued by delays. As a result, the COGCC has acknowledged that meeting the July deadline is unlikely.[20]

The COGCC attempted to ease into the rulemaking process in June 2019, just after SB-181 went into effect, tackling a subject thought to be relatively uncontroversial—the so-called 500 Series, which would amend existing procedural rules.[21] Instead, public rulemaking hearings became a battleground, with environmental groups demanding a moratorium on new drilling permits until a full suite of updated health and safety regulations could be drafted, approved, and implemented.[22] The COGCC eventually adopted updated 500 Series rules in July 2019 and new flowline rules in November 2019,[23] but delays continue to affect the COGCC’s other rulemaking proceedings.

The COVID-19 crisis has exacerbated these delays. Rulemaking hearings to address the “mission change” of the COGCC, cumulative impacts of oil and gas development, and drilling site criteria were delayed by several months.[24] Hearings to consider rules governing wellbore integrity were rescheduled from February 2020 to April 2020[25] and were rescheduled again to June 2020.[26] While the COGCC recently began holding hearings via videoconference to continue the rulemaking process, it has recognized the inadequacy of these virtual meetings for public testimony and open discussion with respect to especially controversial rulemakings, such as the mission change rules.[27] As a result, the COGCC has opted to reschedule public hearings on the mission change rules until August 24 through September 24, when the COGCC hopes to be able to hold in-person hearings, though it currently plans to proceed with the June 2020 public hearings on wellbore integrity rules, likely by videoconference.[28] Accordingly, the COGCC will not meet its July 1st goal of completing all of the rulemaking required by SB-181. While the current commissioners may be able to complete the wellbore integrity regulations before July 1st, the ongoing rulemaking process will be completed by the newly constituted COGCC, not the current commissioners.[29] It remains to be seen whether shifting the balance of the rulemaking proceedings to the new COGCC commissioners will further delay adoption of final rules or affect their content.

Meanwhile, CDPHE has been engaged in separate rulemaking proceedings through two of its divisions, the Air Quality Control Commission (“AQCC”) and the Water Quality Control Commission (“WQCC”). In December 2019, the AQCC adopted rules imposing increased leak detection and repair requirements on producing wells, comprehensive annual emissions reports, and more stringent controls on emissions from storage tanks—all of which will increase operation costs substantially, particularly for small producers.[30] At the same time, AQCC also adopted regulations requiring oil and gas producers to obtain air-quality permits (in addition to the permit to drill required by the COGCC) before they can begin exploration and production activities, eliminating a 90-day grace period under previous rules.[31] In a future rulemaking, the AQCC will consider rules intended to reduce emissions of hydrofluorocarbons and rules requiring oil and gas producers to track and report greenhouse gases emissions.[32] Separately, the WQCC is finalizing tighter regulations governing surface and ground water, which will affect injection wells, waste disposal, and other oil and gas operations.

Local Regulation: Renewed Drilling Moratoriums and a Patchwork Approach

Soon after the passage of SB-181, a number of cities and counties in the Denver-Julesburg Basin enacted moratoriums on new applications for local drilling permits, including Adams and Boulder counties and the cities of Berthoud, Broomfield, Lafayette, Superior, and Timnath. The stated intent of these moratoriums was to pause oil and gas development while the COGCC and local governments updated their regulations.[33] Given the delays plaguing the rulemaking process at the COGCC, however, some of these moratoriums have effectively banned new oil and gas development for as much as a year.[34]

The legality of these moratoriums is unclear. Under the pre-SB-181 framework, a number of cities and counties in Colorado attempted to impose lengthy moratoriums on oil and gas activity. But the courts struck them down, and the Colorado Supreme Court confirmed that local governments did not have the power to halt oil and gas development within their borders.[35] SB-181, however, granted local governments new powers—including, perhaps, the power to ban oil and gas activities. In the coming months, this question may soon be decided by a trial court in Boulder County. A group of anti-industry activists has asked for a ruling that would confirm the legality of the city’s ban on hydraulic fracturing under SB-181.[36]

In the meantime, local governments have proceeded to consider and impose new regulations for the oil and gas industry. One of the industry’s primary criticisms of SB-181 was that it would enable and even encourage a patchwork of local regulations across the state, something that lawmakers in Colorado had long attempted to avoid through preemptive state rules. As the opponents of SB-181 explained, neighboring localities might adopt wildly different—and perhaps inconsistent—regulations.[37] Operating under this kind of jurisdiction-by-jurisdiction patchwork would be difficult and expensive, if not impossible, for producers.

These fears appear to be well-founded.[38] The neighboring counties of Boulder and Weld are taking diametrically opposed regulatory approaches. Boulder commissioners are seeking the “toughest regulations [they] can get” and will likely adopt some of the most restrictive rules in the state.[39] Its proposed rules would impose more stringent restrictions on oil and gas exploration and production, and will at the same time add additional restrictions on noise, vibration, odor, and seismic testing.[40] In stark contrast, Weld county—home to nearly half of Colorado’s active wells—rejected a permitting moratorium and has taken steps to facilitate, rather than restrict, new oil and gas development. For example, local officials designated unincorporated portions of the county as “mineral resource areas of state interest,” prompting an agreement with the COGCC to address the backlog of permits affecting oil and gas development in the county.[41]

While these two counties represent extreme approaches, they highlight the difficulties facing the industry. Mineral rights, leasehold interests, and wells may all span more than one jurisdiction, and producers will now have to grapple simultaneously with several sets of different local rules and regulations—not to mention new state-level rules—increasing the cost and complexity of their operations.

Statewide Permitting Slows and New Ballot Initiatives Loom

One of the primary effects of SB-181 has been a steep decline in the approval of new well locations and drilling permits, which were down nearly 57% and 58%, respectively, in the six months after SB-181 was enacted.[42] While some of this decline can be attributed to local government moratoriums, the COGCC has also indicated that the permitting slowdown is “a reflection of the new emphasis on health, safety and the protection of the environment” created by SB-181.[43] Indeed, shortly after SB-181 was passed, the COGCC adopted interim permitting criteria requiring additional analysis of some drilling permit applications “to ensure the protection of public health, safety, welfare, the environment, or wildlife resources.”[44] The recent decline in permitting has exacerbated an existing backlog, increasing operators’ uncertainty, interrupting drilling programs, and decreasing overall production.[45]

Critics of SB-181 have long predicted that the new law could contribute to a slowdown in Colorado’s oil and gas industry.[46] This prediction was echoed by the University of Colorado’s Leeds School of Business, which warned in December 2019 that “economic and regulatory uncertainties could very well slow development in 2020.”[47] The delayed and uncertain regulatory outlook, when coupled with the COVID-19 crisis and the turmoil in global oil markets, have forced the industry to take dramatic steps, such as slashing capital expenditures, reducing or eliminating dividends, and furloughing or laying off employees. Such measures directly impact adjacent industries, including oilfield services companies, investors, and employees. So far, no major lawsuits have been filed to challenge state or local regulations promulgated under SB-181. As the Leeds School of Business explained, however, “the possibility of legal challenges” is “persistently looming” given the high stakes.[48]

In the meantime, citizen initiatives seeking further changes to Colorado’s regulatory framework may reach the ballot for the upcoming 2020 presidential-year election. The proponent of Proposition 112, the setback initiative that was voted down in 2018, is pursuing six separate initiatives this year. Five of them would impose well setbacks similar to those found in Proposition 112; another would require oil and gas companies to post a far more expensive bond for new wells. If any of these initiatives make the ballot—which is anything but certain, given the difficulty of obtaining petition signatures during the COVID-19 pandemic—the industry could face another expensive campaign season. In 2018, industry groups spent nearly \$40 million defeating Proposition 112.[49] A similar political fight in the midst of a presidential campaign may be even more expensive.

Conclusion

The implementation of SB-181 over the past year has been a difficult endeavor. The COGCC’s rulemaking process has been contentious, leading to repeated delays in the adoption of new regulations. Many local governments enacted moratoriums on new drilling applications, some of which have been extended due to the delays at the COGCC. These local governments have also taken different approaches to oil and gas regulation, creating a patchwork of rules across the state. With legal challenges to the implementation of SB-181 forthcoming and several new ballot initiatives on the horizon, SB-181 appears to have increased, not decreased, the clashes between proponents and opponents of oil and gas production in Colorado. Unfortunately for all involved, the end of the “oil and gas wars” in Colorado is a long way off.

[1] <https://www.denverpost.com/2019/04/16/colorado-oil-gas-bill-signed-gov-jared-polis/>.

[2] <https://www.sos.state.co.us/pubs/elections/Initiatives/titleBoard/filings/2017-2018/97Final.pdf>.

[3] *Martinez v. Colo. Oil & Gas Conservation Comm’n*, No. 17SC297 (available at http://blogs2.law.columbia.edu/climate-change-litigation/wp-content/uploads/sites/16/case-documents/2019/20190114_docket-17-SC-297_opinion.pdf).

[4] <https://www.denverpost.com/2019/01/14/colorado-supreme-court-oil-gas-martinez-decision/>.

[5] <https://www.denverpost.com/2019/04/16/colorado-oil-gas-bill-signed-gov-jared-polis/>.

[6] Senate Bill 19-181 §4.

[7] *City of Longmont v. Colo. Oil & Gas Ass’n*, 369 P.3d 573, 585 (Colo. 2016) (“The Oil and Gas Conservation Act and the Commission’s pervasive rules and regulations, which evince state control over numerous aspects of fracking, from the chemicals used to the location of waste pits, convince us that the state’s interest in the efficient and responsible development of oil and gas resources includes a strong interest in the uniform regulation of fracking.”).

[8] Senate Bill 19-181 §4; <https://www.denverpost.com/2019/05/06/colorado-oil-and-gas-local-regulations-181/>.

[9] Senate Bill 19-181 §4.

[10] C.R.S. 34-60-102 (2017).

[11] Senate Bill 19-181 §5.

[12] Senate Bill 19-181 §§8-9.

[13] C.R.S. 34-60-104 (2017).

[14] Senate Bill 19-181 §9.

[15] Senate Bill 19-181 §9(d).

[16] https://www.coloradopolitics.com/news/cogcc-solicits-application-for-full-time-commissioners/article_0c6e349a-42d3-11ea-b401-f3cbf6062c82.html.

[17] Senate Bill 19-181 §12.

[18] Senate Bill 19-181 §11.

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- [20] *Id.*
- [21] https://www.gjsentinel.com/breaking/cogcc-delays-action-on-first-sb-181-rules/article_7d09abd8-922c-11e9-b04d-6305eb780f5e.html.
- [22] <https://www.westword.com/news/colorado-oil-and-gas-environmental-groups-clash-in-first-round-of-sb-181-rulemaking-11384760>.
- [23] The 500 Series regulations and flowline regulations are available at 2 Code Colo. Regs. § 404-1-500 and 2 Code Colo. Regs § 404-1-1100, respectively. Both sets of regulations may be found online at:
<https://www.sos.state.co.us/CCR/GenerateRulePdf.do?ruleVersionId=8521&fileName=2%20CCR%20404-1>.
- [24] https://cogcc.state.co.us/documents/sb19181/Overview/SB_19_181_Rulemaking_Update_20190801.pdf; https://cogcc.state.co.us/sb19181_calendar.html#/rulemaking_mission_change.
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- [29] <https://coloradosun.com/2020/04/24/zoom-colorado-oil-and-gas-rule-meeting/>.
- [30] 5 Code Colo. Regs. § 1001-9; <https://www.colorado.gov/pacific/cdphe/news/oil-and-gas-rulemaking>.
- [31] 5 Code Colo. Regs. § 1001-9; <https://www.colorado.gov/pacific/cdphe/news/oil-and-gas-rulemaking>;
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<https://www.denverpost.com/2019/06/28/boulder-county-oil-gas-moratorium/>.
- [34] <https://www.bouldercounty.org/news/boulder-county-commissioners-extend-oil-and-gas-moratorium-to-july-31-2020/>.
- [35] *City of Fort Collins v. Colo. Oil & Gas Ass'n*, 369 P.3d 586 (Colo. 2016); *City of Longmont v. Colo. Oil & Gas Ass'n*, 369 P.3d 573 (Colo. 2016).
- [36] *Our Health, Our Future, Our Longmont v. Colorado*, 2020cv30033 (Dist. Ct., Boulder Cty.).
- [37] https://www.coga.org/uploads/1/2/2/4/122414962/sb19-181_summary_3-15-19.pdf.
- [38] <https://coloradosun.com/2019/08/05/colorado-oil-gas-rules-patchwork-sb181/>.
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