STATE OF NEW MEXICO
ENERGY, MINERALS AND NATURAL RESOURCES DEPARTMENT
OIL CONSERVATION COMMISSION

IN THE MATTER OF THE APPLICATION OF THE NEW MEXICO OIL CONSERVATION Division FOR REPEAL OF EXISTING RULE 50 CONCERNING PITS AND BELOW GRADE TANKS AND ADOPTION OF A NEW RULE GOVERNING PITS, BELOW GRADE TANKS, CLOSED LOOP SYSTEMS AND OTHER ALTERNATIVE METHODS TO THE FOREGOING, AND AMENDING OTHER RULES TO CONFORMING CHANGES STATEWIDE.

CASE NO. 14015
Order no. R-12939

THE INDEPENDENT PETROLEUM ASSOCIATION OF NEW MEXICO'S APPLICATION FOR REHEARING

COME NOW the Independent Petroleum Association of New Mexico a party of record in this case, hereinafter referred to as "IPANM," to request a rehearing pursuant to §70-2-25 NMSA (2005) and 19.14.14.1233 NMAC on order number R-12939 of case no. 14015, in the matter of the application of the New Mexico Oil Conservation Division for repeal of existing rule 50 concerning pits and below grade tanks and adoption of a new rule governing pits, below grade tanks, closed loop systems and other alternative methods to the foregoing, and amending other rules to conforming changes statewide. The basis for IPANM's application for rehearing is a challenge to the jurisdictional authority for changes in the rule; the lack of scientific basis or testimony in the record for sufficiency of the findings; and the failure to meet the statutory requirements of the Small Business Regulatory Relief Act §14-4A NMSA 1978. IPANM submits this Application for Rehearing on behalf of all 280 companies it represents, many of whom operate exclusively in New Mexico and therefore are adversely affected by Oil Conservation Commission Order No. R-12939. In addition, IPANM supports and adopts all positions taken by Mr. William Carr, in the Industry Committee's Application for Rehearing.

Background

1. On September 21 2007, the New Mexico Oil Conservation Division ("Division") filed an Application for Rulemaking seeking an order repealing Rule 50 of the General Rules and Regulations of the Division and adopting proposed new rules governing pits, below grade tanks, closed loop systems and other alternative methods to the foregoing. In addition, the Division proposed conforming changes to rules 7[19.15.1.7 NMAC], 21[19.15.1.21 NMAC], 52

[19.15.2.52 NMAC],114 [19.15.3.114 NMAC], 202 [19.15.4.202NMAC] and 1103 [19.15 .13.1103 NMAC]. For the purpose of this motion, these rules will hereinafter be referred to as the "Pit Rules."

2. The Division's first draft of the Pit Rules was released in March 2006 after an industry presentation to the Division and subsequently all parties to the case, including IPANM, issued comments. No action was taken on the public comments until an additional draft and stakeholder meetings were held in January 2007. In March 2007, the Division announced that a Governor appointed taskforce was convened to advise the Division on the complex issues involved in the Pit Rule.

3. The Task Force met during April, May and June 2007 and, on July 10, 2007. The taskforce had 14 members and was 'facilitated' by Reese Fullteron, deputy secretary of the Energy, Mineral and Natural Resources Department and supervisor to Commissioner Fesmire and both Division members assigned to the taskforce. At no time during the taskforce process was a disclosure in writing made by Mr. Fullerton as to his true role in the proceedings. On July 10, 2007, the taskforce released a report in which it identified those items on which the Task Force had reached agreement and other issues where there was no consensus. On the items that there was no consensus, the Division made recommendations to the Commission at the hearing. (TR. 19, 845). Several other issues never discussed during the taskforce were added to the final proposal by Division staff. Additional definitions were never shown to some members and industry members were misled to believe that in-place burial would be incorporated in the final proposal, which it was not. (Testimony of John Byrom). Mr. Byrom, current President of IPANM and a small producer, also testified at the hearing that while the question of additional costs to operators was mentioned at the taskforce meetings, no economic data was ever produced by the Division for a true discussion on the economic impacts on businesses or on the state. There were also allegations made at the time of the taskforce, causing one member to withdraw alleging improper participation and agenda control by Division staff. (TR. 569). At the subsequent hearing, Mr. Brad Jones admitted that Secretary Prukop, Secretary of the Energy, Minerals and Natural Resources Department set the agendas with a letter by Chairman Fesmire setting the parameters of the meetings (TR. 569). In addition, private email communications

between members of the taskforce discussing the various provisions of the proposed rule were admitted over IPANM's objection. (TR. Exhibit , 11/07).

4. On September 21, 2007, two and half months after the Taskforce convened, the Division filed its notice of rulemaking and released the draft that was presented to the Commission at the hearing.

5. On October 22, 2007, the Commission, under heard opening statements from the Division, the Citizens for Clean Air and Water and the Oil and Gas Accountability Project. Mr. Brooks, on behalf of the Division, stated in his opening statement, " " Now we recognize that this is going to requires the use of closed loop systems in a significant part of our state ... It probably does cost some money up front, more money than use of a pit. We're not going to present you any evidence on what costs money because that's not our area of expertise. We believe that we have heard evidence through the taskforce that indicates that this not an undoable thing... " (Brooks: p. 23-24)

6. Based on the Division's representations in its opening statement, IPANM made the motion on the record to compel the Division to adhere to the statutory mandates of the Small Business Regulatory Relief Act [hereinafter 'SBRRA']. Ms. Foster stated, "The Independent Petroleum Association of New Mexico does represent 250 small businesses within the State of New Mexico ... and we will be significantly impacted by this Rule. The [SBRRA] mandates that the agency go through this economic analysis prior to the promulgation of a rule... and if they have done so, or if they have filed a letter with the Commission as is required by statute,.. that we get a copy of that letter and .. a copy of that economic analysis at this time." (TR. 33)

7. Mr. Brooks responded, "We have given the notice to the Small Business Regulatory Commission as required by the statute." (Brooks: p. 34). Commissioner Fesmire ordered the Division to respond to both motions in writing by October 29th. The hearing adjourned at 9:40 am.

8. On October 29, 2007, IPANM filed comments on the proposed rule alleging that: 1) the Division's pre-hearing process and the rule itself lacked adequate scientific basis for the change and 2) the Division failed to address the issues concerning the economic impact of the proposed

rule on small businesses and therefore violated the mandates of SBRRA § 14-4A NMSA 1978. Particularly, IPANM urged the Division to pay heed to the Legislature's statement that "the process by which state rules are *developed* and adopted should be reformed to *require agencies to solicit the ideas and comments* of small businesses, to examine the effect of proposed and existing rules on such businesses and to review the continued need for the existing rule" 14-4A-2(J)(emphasis added).

9. On November 6, 2007, Mr. Brooks responded to the IPANM motions stating, "the only thing the Division is required to do prior to the adoption of this by the Commission is to give notice ... the other requirements of the Act that apply prior to enactment are that the agency will consider the effects on small business. Since that directive is directed to the agency that adopts regulations, we construe that as being the obligation of the Commission to consider that matter." (Brooks: p. 303).

10. On November 7th, Mr. Brooks provided IPANM with a copy of an electronic notice made to the Small Business Regulatory Advisory Commission on Monday, October 22 at 10:37am. In the Statement, Division counsel states, "The Division does not believe that the proposed rule will have a disproportionately adverse effect on small businesses."

11. Evidence on Case No. 14015 was presented on November 5 through 9, 13 through 16, 26, 27, 30 and December 3,4,6,7.10 and 14, 2007.

12. Representative James Strickler, Representative Paul Bandy, Representative Candy Ezzel and Minority Whip Dan Foley all testified to the negative economic impact on the businesses and the State of New Mexico (TR. Nov 5). Mr. Wayne Price, Bureau Chief of the Environmental Division, testified that he believed the increased cost per well for small operators would be in the range of 30,000 to $80,000 and that no specific information had ever been developed by the agency (TR. 11/6). Exhibit 8, offered by Mr. Van Gotten, was rejected by the Commission as having no foundation. Exhibit 8 contained economic information created by another agency but not used or relied upon by the Division. Mr. Dana McGarr, small business owner testified that the potential impact on his business could result in laying off 9 workers (TR. 11/5).

13. Over the course of the hearing, the Commission heard from 19 sworn witnesses who testified without counsel on the negative economic impacts of the rule. IPANM presented testimony of Sam Small, Al Springer, Tyson Foutz, John Byrom and Tom Mullins who all reported negative economic impact on small businesses. Mr. Greg Wurtz and Mr. John Poole of Conoco Phillips reported a several million dollar economic impact on their business. In addition, several witnesses commented that the unintended consequences of the proposed rule would result in negative environmental impacts as well.

14. On April 16, 2008, the Commission specifically discussed their concern for small businesses by highlighting the fact that the Division's request for an automatic haul to landfill within a 100 mile radius was eliminated by the Commission. However, in the final rule, the Commission adopted testing and closure standards which are not supported by the substantial evidence in the record on by sufficient findings of the Commission.

ARGUMENT

Although the Commission did alter some of the recommendations made the Division in the final rule, the process by which the Commission reached its conclusions simply ignored its statutory duties to balance the protection of correlative rights and the prevention of wastes while administering, not creating new policy beyond the rules of the Water Quality Control Commission. The Commission also made a mockery of the Taskforce process which clearly took advantage of the good will of industry to attempt to reach true consensus. By admitting private emails into evidence and refusing to allow the Division to enter into neutral mediation on the non-consensus issues to discuss the impacts on small businesses, the powers that run the Division clearly had no good faith intent to follow the requirements of the Small Business Regulatory Relief Act. The fact that Counsel for the Division stated in his opening statement that the Division felt it did not have the responsibility to consider economic impacts and that he filed the 'no impact' statement after the IPANM motion and after the commencement of the hearing based on no analysis demonstrates the will to ignore very clear legislative direction on an issue very relevant to small businesses. Indeed, the final rule, with its arbitrarily set chloride and 3103 standards is the same result as a full haul mandate in the Southeastern part of the State. (19.15.17.13.F(3)(2) NMAC) In testimony, the Division recommended the adoption of a 5000

mg/l standard (translate to 100,000 mg/kg chloride) for onsite deep trench burial (Nov 7 Division Proposal, 19.15.17.13(F)(2)(d) while Dr. Stephens, industry expert, recommended the adoption of a 24,800 mg/kg standard. But the Commission, without explanation selected a limit of 250 mg/l (translate to 5000 mg/kg chloride).

Since the Commission wholly fails to provide a rational connection between the facts in the record and the choices made in the final order, industry is unable to understand how the Commission came to its final decisions on the ultimate questions of fact in this case. As such, a rehearing must be granted in this issue.

POINT I

THE COMMISSION EXCEEDED ITS JURISDICTIONAL AUTHORITY WITHOUT ADEQUATE FINDINGS

The Oil Conservation Commission was created by the Legislature under the Oil and Gas Act, and is empowered to 'prevent waste ... and protect correlative rights' *See Section 70-2-11(A).* The Commission must 'regulate the disposition of *nondomestic* wastes resulting from the exploration, development, production or storage of crude oil or natural gas to protect public health and the environment' *Section 70-2-12(B)(21).* The Commission is also tasked with *administration* of the Water Quality Act. *See,* NMSA §70-2-12(2006).

The New Mexico Water Quality Control Commission was created under the Water Quality Act, NMSA §§74-6-1 to -17(1967, as amended through 2003). The Commission is required to *adopt* a "comprehensive water quality management program, adopt water quality standards for surface and ground waters, adopt regulations to prevent or abate water pollution, and assign responsibility for administering its regulations to constituent agencies" *74-6-4-(B) to (E).*" *See Gila Resources Information Project v. N.M. Water Quality Cont. Comm'n,* 2005-NMCA-139. The Water Quality Act also requires that the Commission 'adopt water quality standards for surface and ground waters of the state based on credible scientific data and other evidence appropriate under the Water Quality Act [74-6-1 NMSA 1978] *74-6-4(C).* The legislature was very clear in the standards the WQCC must use in establishing rules and regulations pertaining to waters. The Court of Appeals has also noted that department's authority as a constituent agency of WQCC must be derived from statute. *Phelps Dodge Tyrone, Inc. v.*

N.M. Water Quality Control Comm'n, slip op. June 15, 2006, no. 25,027, p. 6 *citing In re Application of PNM Elec. Servs.,* 1998-NMSC-017, ¶10, 125 N.M. 302". Therefore, NMSA §74-6-4(C) states, "the standards shall include narrative standards and as appropriate, the designated uses of the waters and the water quality criteria necessary to protect such uses ... In making standards, the [WQCC] commission shall give weight it deems appropriate to all facts and circumstances, including the use and value of the water for water supplies, propagation of fish and wildlife, recreational purposes and agricultural, industrial and other purposes" *74-6-4(C).* The Act further stated that in "adopting regulations, the WQCC should consider, among other things, the economic impact of regulations" *Id* at 13. Reviewing the relevant statutes that give the Commission its authority, it is clear that the Commission is empowered to promulgate rules and regulations pertaining to disposal of nondomestic wastes and produced water. However, if the underlying intent and reasoning behind a rule by a constituent agency of the WQCC is to protect ground water, then the rule promulgation is within the statutory authority of the WQCC only, while the permitting process is left to the constituent agency. *See, Tyrone, supra at. p. 7*

In addition, under the Act, the Commission must give equal weight to each statutory responsibility, that is, while the duty to protect correlative rights and the Commission's environmental duties may conflict, if the Commission improperly elevates one duty over the other, it must provide a rationale for its decision to do so. Here, the Commission clearly opted to elevate its environmental role over the protection of correlative rights but there are no findings on the rationale for ignoring the statutory mandate to prevent waste or protect correlative rights. *See, Continental Oil Company v. Oil Conservation Comm'n,* 70 N.M. 310, 319 (NM 1962)(the prevention of waste is the OCD's primary duty and paramount power).

As a matter of law, "the actions of the Commission must be consistent with and within the scope of its statutory authority and the order is supported by substantial evidence" *Fasken v. Oil Conservation Commission,* 87 N.M. 292, 294, 532 P.2d 588, 590 (N.M. 1975), *citing Grace v. Oil Conservation Comm'n,* 87 N.M. 205, 531 P.2d 939 (NM 1975). *Fasken* further states, "in cases where the sufficiency of the Commission's findings is in issue or their substantial support is questioned,... the following must appear: A. Findings of ultimate facts which are material to the issues; B. Sufficient findings to disclose the reasoning of the Commission in reaching it ultimate findings; C. such findings must have substantial support in the record." *Id.* In the case at hand, the ultimate findings include 'the prevention of waste, the protection of correlative rights' *Id.*

However, nowhere in its finding does the Commission address its statutory duty to protect correlative rights or prevent waste, but rather concludes that the final rule will "provide a regimen for regulating the use of pits, below-grade tanks, closed-loop systems and sumps in a manner that will protect fresh water, human health and the environment" *See finding 299.*

The Supreme Court has also held in *Rio Grande Chapter of the Sierra Club. v. N.M. Mining Comm'n,* 2003-NMSC-005, 133 N.M. 97, 61 P.3d 806, that "... an agency rule would be arbitrary or capricious if the agency . . . failed to consider an important aspect of the problem, offered an explanation for its decision that runs counter to the evidence before the agency, or is so implausible that it could not be ascribed to a difference in view or the product of agency expertise." *Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43, 77 L. Ed. 2d 443, 103 S. Ct. 2856 (1983). A ruling by an administrative agency is also arbitrary and capricious if it is unreasonable or without a rational basis, when viewed in light of the whole record. *Snyder Ranches, Inc. v. Oil Conservation Comm'n*, 110 N.M. 637, 639, 798 P.2d 587, 589 (1990); *see Hobbs Gas Co. v. N.M. Serv. Comm'n*, 115 N.M. 678, 680, 858 P.2d 54, 56 (1993) (stating that burden on review of administrative decision under arbitrary and capricious standard is to show that the decision is "unreasonable or unlawful."). Finally, in *Tenneco Oil Co. v. New Mexico Water Quality Control Comm'n*, 107 N.M. 469, 474, 760 P.2d 161, 166 noted that "the courts are not free to accept post hoc rationalizations of counsel in support of agency decisions, because a reviewing court must judge propriety of agency action solely on grounds invoked by agency". In this instance, the testimony demonstrated that on site burial of the products of oil and gas drilling could be done in a matter that would protect the environment. However, the final rule has set such arbitrary and unreasonably low limits that operators will be hauling hundreds of loads of dirt on our state highways to centralized landfills. The rule poses risk of death to NM citizens, increases dust and air contaminants, causes increased costs to operators thereby reducing the supply and impacting correlative rights of the mineral interest owners and causing waste.

Rehearing must be granted to ensure adequate statutory balance of correlative rights and prevent of waste with the limited statutory responsibility of protection of the environment.

POINT II

THE SMALL BUSINESS REGULATORY RELIEF ACT REQUIRED ACTION BY THE DIVISION PRIOR TO THE HEARING DEMONSTRATING A GOOD FAITH EFFORT TO PROTECT SMALL BUSINESSES

In our pre-hearing motion IPANM urged the Division to pay heed to the Legislature's statement that "the process by which state rules are *developed* and adopted should be reformed to *require agencies to solicit the ideas and comments* of small businesses, to examine the effect of proposed and existing rules on such businesses and to review the continued need for the existing rule" 14-4A-2(J)(*emphasis added*). Clearly, the legislative intent was for an agency to examine effects of proposed rules and solicit input from small businesses during the development stages of the rule, not during an adversarial hearing process. However, Commissioner Fesmire overruled IPANM's motion at the hearing for a motion to compel the Division to produce economic data as well as IPANM's motion for a mediated rulemaking process under the Governmental Prevention and Resolution Act. Both motions were made a time when counsel for the Division made it clear in his opening statement that the Division had not done any economic analysis and infact, had not even given notice to the Small Business Regulatory Advisory Commission.

The Small Business Regulatory Relief Act, sponsored by Speaker Ben Lujan and signed into law by the Honorable Governor Bill Richardson on April 6, 2005, requires that all New Mexico state agencies must apply special standards when promulgating rules or regulations that may have a negative impact on small businesses. Under the law, a 'small business' is defined as "a business entity, including its affiliates, that is independently owned and operated and employs fifty or fewer full-time employees" *14- 4A-3(E) NMSA 1978.* A 'rule' means, "any rule, regulation, order, standard or statement of policy, including amendments to or repeals of any of those, issued or promulgated by an agency and purporting to ... affect persons not members or employees of the issuing agency". *14-4A-3(D) NMSA 1978.* In its findings, at the time of the creation of the Small business Regulatory Relief Act, the Legislature demonstrated an explicit understanding that 'a vibrant and growing small business sector is critical to creating jobs in a dynamic economy; [and that] small businesses bear a disproportionate share of regulatory costs and burdens" *14-4A-2(A, B).*. The SBRRA mandates that 'prior to the adoption of a proposed rule that may have an adverse effect on small business, the agency shall consider regulatory methods that accomplish the objectives of the

applicable law while minimizing the adverse effects on small business". *14-4A-4(B).* While there was some limited discussion on the record only during deliberations relating to changing or eliminating provisions of the rule to benefit small producers, only finding 300 addresses SBRRA, stating "the Commission has made those changes it found possible to the Division's proposal while still meeting its statutory duty to protect fresh water, human health and the environment". First, looking at the statutory intent of SBRRA, the mandate to work with small business is during the development of the proposed rule, "fundamental changes that are needed in the regulatory culture of state agencies to make them more responsive to small business can be made without compromising the statutory mission of the agencies" §14-4A-2(C). Second, whether it is the Oil Conservation Division or the Oil Conservation Commission which has the role of 'agency' under the SBRRA is unclear. However, to force small business participation with counsel in the rulemaking process in order to present a legal case to the agency Commission seems to be outside the intent of the SBRRA to assist small businesses, not burden them. Therefore, the more reasonable result is that prior to promulgating or declaring to the public the intent to go to the Commission for a new or change in a rule, the Division has the statutory responsibility to address small business needs by the completion of an economic impact statement. The Commission is nothing more than a final arbiter on technical issues relating to the proposed rulemaking action *See 19.15.14.1201.*

Moreover, the Legislature also ordered state agencies to review "*all* of its rules that existed on the effective date of the Small Business Regulatory Relief Act to determine whether the rules should be continued without change or should be amended or repealed to minimize the economic impact of the rules on small businesses, subject to compliance with the stated objectives of the laws pursuant to which the rules were adopted". If the agency determined a change in a rule was needed, the agency is **must** consider "(1) the continued need for the rule; (2) the nature of complaints or comments received from the public concerning the rule; (3) the complexity of the rule; (4) the extent to which the rule overlaps, duplicates or conflicts with other federal, state and local government rules; and (5) the length of time since the rule has been evaluated or the degree to which technology, economic conditions or other factors have changed in the topical area affected by the rule." *14-4A-6(C)(1-5) emphasis added.* In this case, the agency promulgated Rule 50 (old pit rule) in 2003 and started discussions of the new rule in 2006. As noted by counsel for the Division during that long time period, there was no consideration of analysis on economic impacts of the rule, moreover, once the agency determined a change to rule 50 was needed, the agency completely failed to address the

statutory requirements of §14-4A-6(C)(1-5). To say that Order R-12939 addresses a completely **new** rule is a shameless end-run around the process required by SBRRA for the change in rules noted above. *See, Divisions Response to IPANM's Motion to Compel, para. 11.* Since the common name for both old Rule 50 and New Rule 17 is "the Pit Rule", one can assume that it is a change in agency policy on the same issue. Therefore, the Division/agency must have considered the complexity of the proposed rule and the degree to which technology and economic conditions had changed since 2003. The Division specifically failed to 'solicit' comments or 'examine the effect' on small businesses of the rule prior to development of the proposed rule.

Clearly, the Division has little regard for the statutory requirements to protect small businesses. While both counsel for the Division and even the Commissioners made limited statements regarding SBRRA, the final actions of the Commission do not protect the Division from its statutory responsibility to address the issues affecting small business at the time of development or decision to change the rule. That the Commission ultimately made the arbitrary decision to impose unreasonable closure standards ultimately affects small businesses. That the Division failed to adequately provide the Commission with cost impacts of all parts of the rule, including those changes made during the hearing, left the Commission exposed to rendering a decision without merit in science or in fact.

CONCLUSION

In its final decision and adoption of the new Pit Rules, the Commission ignored its statutory responsibilities under the Oil and Gas Act, the Water Quality Act and the Small Business Regulatory Relief Act. Order No. R-12939 does not contain findings of fact sufficient to make rational connections to the facts presented at the hearing in testimony or even the final rule. As such, the findings do not rest on material facts supported by substantial evidence. The case must be set for rehearing to address each of these issues.

Respectfully submitted,
Chatham Partners, Inc.

By: _____

Karin V. Foster

ATTORNEY FOR THE INDEPENDENT
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CERTIFICATE OF SERVICE

I hereby certify that on this 229th day of May, 2008, I served copies of the foregoing application for Rehearing by U.S. Mail, postage paid to the following:

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