



# Ohio Legislative Service Commission

## Final Analysis

Eric Vendel

### Am. Sub. H.B. 133 129th General Assembly (As Passed by the General Assembly)

**Reps.** J. Adams, Beck, Blessing, Boose, Brenner, Buchy, Burke, Combs, Gonzales, Goodwin, Grossman, Hackett, Hall, Hayes, Huffman, Landis, Maag, Martin, McKenney, Rosenberger, Ruhl, Sears, Stebelton, Thompson, Uecker, Wachtmann, Young, Amstutz, Blair, C. Hagan, Hottinger, Mecklenborg, Newbold, Roegner, Slaby

**Sens.** Faber, Schaffer, Bacon, Coley, Daniels, Hite, Jones, Jordan, Niehaus, Seitz, Widener, Wilson, Lehner

**Effective date:** September 30, 2011

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## ACT SUMMARY

- Creates the Oil and Gas Leasing Commission to oversee and facilitate the leasing of land that is owned or controlled by a state agency, including a state university, for the purpose of the exploration for, development of, and production of oil and natural gas resources.
- Repeals prior authority for certain state agencies to enter into oil and natural gas leases.
- Establishes four classifications for all property that is owned or controlled by a state agency, and requires each state agency to inventory and classify each parcel of land that is owned or controlled by the agency.
- Prohibits a state nature preserve from being nominated or leased under the act for the purpose of exploring for and developing and producing oil and natural gas.
- Authorizes a state agency, beginning on the act's effective date and ending on the effective date of the rules adopted by the Commission under the act, and in consultation with the Commission, to lease a formation within a parcel of land that is owned or controlled by the state agency for oil and gas drilling.

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\* This version updates the effective date of the act.

- After the effective date of the rules, generally requires the state agency that owns or controls the parcel of land that is the subject of a nomination approved by the Commission to enter into a lease with the Commission's selection of the highest and best bidder.
- Establishes a procedure by which certain persons may submit lease nominations to the Commission, and requires the Commission to approve or disapprove a nomination based on specified factors.
- Requires the Director of Natural Resources to adopt rules establishing procedures and requirements for publishing notice on the Department's web site of each nomination received by the Commission for at least 21 days prior to the Commission's approval or disapproval of a nomination.
- Establishes procedures to be used by the Commission governing the advertising for and selection of bids for leases for the extraction of oil and gas from state land.
- Requires the Commission to adopt rules governing the oil and gas leasing program.
- Establishes the State Land Royalty Fund to which proceeds from lease signing fees, rentals, and royalty payments generally are required to be credited, and requires that money in the Fund be used to acquire land and to pay capital costs of state agencies whose land is leased for oil and gas extraction.
- Creates the Forestry Mineral Royalties Fund and Parks Mineral Royalties Fund, and requires money from signing fees, rentals, and royalties from oil and gas leases entered into under the act on Division of Forestry or Parks and Recreation land to be deposited into the applicable Fund and used for the purposes discussed above.
- Requires money from signing fees, rentals, and royalties from oil and gas leases entered into under the act on Division of Wildlife land to be deposited into the continuing Wildlife Habitat Fund and used for the purposes established in law unchanged by the act for that Fund.
- Requires at least 30% of the proceeds from a lease executed on or after the act's effective date for the exploration and production of oil or gas within or under a state park to be credited to the applicable fund created in the state treasury that supports the state park, and requires the Department of Natural Resources to use the money for capital improvements in that state park.
- Establishes the Oil and Gas Leasing Commission Administration Fund consisting of nomination fees and bid fees credited to it under the act, and requires the Fund to be used to pay the Commission's and the Department of Natural Resources'

administrative expenses for the act's implementation and to pay certain expenses of Commission members.

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## CONTENT AND OPERATION

### Oil and Gas Leasing Commission

The act creates the Oil and Gas Leasing Commission to oversee and facilitate the leasing of state property for the purpose of developing oil and natural gas resources on state lands.<sup>1</sup> It repeals prior authority for certain state agencies and state universities (see "**Definitions**," below) to enter into oil and natural gas leases (see "**Background**," below). However, it provides that a lease of any lands that are owned or controlled by one of those state agencies or a state university for the purpose of exploring for, developing, and producing oil or natural gas that was entered into prior to the effective date of the act remains in effect until the term of the lease expires as provided for in the lease.<sup>2</sup>

The Commission consists of the Chief of the Division of Geological Survey in the Department of Natural Resources and the following four members appointed by the Governor:

(1) Two members from a list of not less than four persons recommended by a statewide organization representing the oil and gas industry;

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<sup>1</sup> R.C. 1509.71(B).

<sup>2</sup> Section 3.



(2) One member of the public with expertise in finance or real estate; and

(3) One member representing a statewide environmental or conservation organization.

The act provides for staggered five-year terms for the Governor's appointees and includes standard procedures governing their appointment, the filling of vacancies, and removal of appointees.

The Chief of the Division of Geological Survey is the chairperson. Three members constitute a quorum, and no action of the Commission is valid unless it has the concurrence of at least three members. The Commission must keep a record of its proceedings. Members of the Commission serve without compensation, but must be reimbursed for their actual and necessary expenses incurred in the performance of their duties. The Department of Natural Resources must provide clerical, technical, legal, and other services required by the Commission in the performance of its duties.<sup>3</sup>

### **Inventory and designation of property into classifications**

The act requires a state agency to submit to the Oil and Gas Leasing Commission an inventory of each parcel of land that is owned or controlled by the state agency. The inventory must classify each parcel as a class 1, class 2, class 3, or class 4 property. Class 1 property is property concerning which there are no encumbrances or deed restrictions that limit the exploration or drilling for oil or gas on the property. Class 2 property is property owned or controlled by a state university or college or by another state agency concerning which there is a federal encumbrance or monetary interest that limits or prohibits the exploration or drilling for oil or gas on the property. Class 3 property is property that is not class 2 or class 4 property, is of insufficient size or shape to meet the requirements for drilling a well on the property that are established under the Oil and Gas Law, and is necessary for pooling with other parcels of property for the purpose of forming a drilling unit in order to meet the requirements for drilling a well that are established under that Law. Finally, class 4 property is property concerning which there is a provision in the deed that limits the exploration or drilling for oil or gas on the property.<sup>4</sup>

The Commission may request a state agency to submit documentation supporting the classification of each parcel of land.<sup>5</sup> In addition, the act requires a state agency to classify a parcel of land acquired after the act's effective date not later than 90

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<sup>3</sup> R.C. 1509.71(B) to (G).

<sup>4</sup> R.C. 1509.70(A) to (D).

<sup>5</sup> R.C. 1509.72(A).

days after its acquisition and submit the classification to the Commission.<sup>6</sup> Finally, the Commission must provide to the Department of Natural Resources the information that is necessary for the Department to post on the Department's web site a listing of each parcel of state land and its corresponding classification. The act requires the Department to post the information.<sup>7</sup>

Under the act, a state agency that has classified a parcel of land as a class 2 property must make reasonable and appropriate efforts so that the parcel could be classified as a class 1 property.<sup>8</sup>

### **Exemption of nature preserves**

The act prohibits a nature preserve, which is an area that is formally dedicated under the Natural Areas and Preserves Law, that is owned or controlled by a state agency from being nominated or leased under the act (see "**Temporary leasing authority for state agencies**," "**Lease nominations**," and "**Lease procedures**," below) for the purpose of exploring for and developing and producing oil and natural gas resources.<sup>9</sup>

### **Temporary leasing authority for state agencies**

The act authorizes a state agency, beginning on the act's effective date and ending on the effective date of the rules adopted by the Oil and Gas Leasing Commission (see "**Rules**," below), in consultation with the Commission, to lease a formation (see "**Definitions**," below) within a parcel of land that is owned or controlled by the state agency for the exploration for and development and production of oil or natural gas. The state agency must establish bid fees, signing fees, rentals, and at least a 1/8 landowner royalty. On and after the effective date of the rules adopted by the Commission, such a formation may be leased for the exploration for and development and production of oil or natural gas only in accordance with the act's nomination and leasing procedures (see "**Lease nominations**" and "**Lease procedures**," below).<sup>10</sup>

### **Lease nominations**

Leases entered into by a state agency beginning 270 days after the act's effective date must be awarded pursuant to a nomination and bid process established by the act.

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<sup>6</sup> R.C. 1509.72(B).

<sup>7</sup> R.C. 1509.72(C).

<sup>8</sup> R.C. 1509.76.

<sup>9</sup> R.C. 1509.73(I) and 1517.01, not in the act.

<sup>10</sup> R.C. 1509.73(A)(1).

Not earlier than 270 days after the act's effective date, a person that is an owner (see "**Definitions**," below) and is interested in leasing a formation within a parcel of land that is owned or controlled by a state agency for the purpose of exploring for, developing, and producing oil or natural gas may submit a lease nomination identifying the parcel of land.<sup>11</sup>

The nomination must be in the manner and form, and include the information and nomination fee, that are required by rules adopted by the Commission under the act (see "**Rules**," below). Not less than 30 days, but not more than 120 days following the receipt of a nomination of a parcel of land, the Commission must conduct a meeting for the purpose of determining whether to approve or disapprove the nomination for the purpose of leasing a formation within the parcel of land that is identified in the nomination. The Commission also must review the nomination to determine if the parcel of land has been classified (see above). If the parcel of land has not been classified, the Commission immediately must send a copy of the nomination to the state agency that owns or controls the parcel. The state agency must classify the parcel of land as a class 1, class 2, class 3, or class 4 property and submit the classification to the Commission not later than 15 days after receipt of a copy of the nomination. On receipt of the state agency's classification of the parcel of land, the Commission must provide the Department of Natural Resources the information that is necessary for the Department to post the parcel and its corresponding classification on the Department's web site.<sup>12</sup>

After a parcel of land that is the subject of a nomination has been classified, the Commission must approve or disapprove the nomination.<sup>13</sup> In making its decision, the Commission must consider all of the following:

(1) The economic benefits, including the potential income from an oil or natural gas operation, that would result if the lease of a formation that is the subject of the nomination were approved;

(2) Whether the proposed oil or gas operation is compatible with the current uses of the parcel of land that is the subject of the nomination;

(3) The environmental impact that would result if the lease of a formation that is the subject of the nomination were approved;

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<sup>11</sup> R.C. 1509.73(A)(2).

<sup>12</sup> R.C. 1509.73(B)(1).

<sup>13</sup> R.C. 1509.73(B)(1).

(4) Any potential adverse geological impact that would result if the lease of a formation that is the subject of the nomination were approved;

(5) Any potential impact to visitors or users of a parcel of land that is the subject of the nomination;

(6) Any potential impact to the operations or equipment of a state agency that is a state university or college if the lease of a formation within the parcel owned or controlled by the university or college that is the subject of the nomination were executed;

(7) Any objections to the nomination that are submitted to the Commission by the state agency that owns or controls the land on which the proposed oil or natural gas operation would take place;

(8) Any comments or objections to the nomination submitted to the Commission by Ohio residents or other users of the parcel of land that is the subject of the nomination; and

(9) Any other factors that the Commission may establish in rules adopted under the act.<sup>14</sup>

The act requires the Commission to disapprove a nomination of a parcel of land that is a class 3 property. The Commission must send notice of the disapproval by certified mail to the person that submitted the nomination.<sup>15</sup>

Prior to making its decision to approve or disapprove a nomination, the Commission must notify the agency that owns or controls the land on which the oil or gas operation would take place.<sup>16</sup>

The Commission must approve or disapprove a nomination not later than two calendar quarters following the receipt of the nomination. Notice of the decision must be sent by certified mail to the person that submitted the nomination. If the Commission approves a nomination, the Commission must notify the state agency that owns or controls the parcel of land that is the subject of a nomination of the Commission's approval. The notification must request the state agency to submit to the Commission special terms and conditions that will apply to the lease of a formation within the parcel of land because of specific conditions related to the parcel. The state

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<sup>14</sup> R.C. 1509.73(B)(1)(a) to (i) and 1509.74(C).

<sup>15</sup> R.C. 1509.73(B)(2).

<sup>16</sup> R.C. 1509.73(B)(3).

agency must submit the special terms and conditions not later than 60 days after receipt of a notice from the Commission.<sup>17</sup>

If the Commission approves a nomination for a parcel of land that is a class 1 property, the Commission must offer for lease each formation that is within the parcel of land (see "**Lease procedures**," below). If the Commission approves a nomination for a parcel of land that is a class 2 or class 4 property, the Commission cannot offer for lease any formation that is within the parcel of land unless the state agency that owns or controls the parcel of land notifies the Commission that a formation or formations that are within the parcel of land may be offered for lease.<sup>18</sup>

### **Public notice**

Not later than 270 days after the act's effective date, the Director of Natural Resources must adopt rules in accordance with the Administrative Procedure Act establishing procedures and requirements for publishing notice on the Department's web site of each nomination received by the Commission for a period of at least 21 days prior to the Commission's approval or disapproval of a nomination. The notification must identify the parcel of land that is the subject of the nomination and include a statement that a person may submit comments to the Commission concerning the nomination. The act requires the Commission to provide to the Department the information necessary for the Department to comply with the requirement.<sup>19</sup>

### **Lease procedures**

Each calendar quarter, the Commission must advertise for bids for a lease for a formation within a parcel of land that was the subject of a nomination approved during the previous calendar quarter that is a class 1 property or that is a class 2 or class 4 property for which the Commission has received notice from the state agency that owns or controls the parcel of land that a formation or formations within the parcel may be offered for lease. The advertisement must be provided to the Department of Natural Resources, and the Department must publish the advertisement on its web site for a period of time established by the Commission. The advertisement must include the following information:

(1) The procedure for the submission of a bid to enter into a lease for a formation within a parcel of land;

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<sup>17</sup> R.C. 1509.73(B)(5).

<sup>18</sup> R.C. 1509.73(B)(6).

<sup>19</sup> R.C. 1509.72(D).



(2) A statement that a standard lease form that is consistent with the practices of the oil and natural gas industries will be used for the lease;

(3) A copy of the standard lease form that will be used;

(4) Special terms and conditions, if applicable, that apply to the lease because of specific conditions related to the parcel of land;

(5) The amount of the bid fee that is required to be submitted with a bid; and

(6) Any other information that is determined to be pertinent by the Commission.<sup>20</sup>

The act requires a person submitting a bid to enter into a lease to pay a bid fee that is established in rules adopted under the act (see "**Rules**," below).<sup>21</sup>

To encourage the submission of bids for leases and the responsible and reasonable development of the state's natural resources, the Commission must maintain the confidentiality of, and must not disclose, information contained in a lease bid that is submitted under the act before a person is selected as the highest and best bidder unless the Commission determines otherwise.<sup>22</sup>

The Commission must establish a deadline for the submission of bids for each lease regarding a particular parcel of land and notify the Department of Natural Resources of the deadline. The Department is required to post the deadline for the submission of bids for each lease on the Department's web site. A person must submit a bid in accordance with the procedures and requirements established by the Commission in rules adopted under the act.<sup>23</sup>

The act requires the Commission to select the person who submits the highest and best bid related to each formation within that parcel of land, taking into account the financial responsibility of the prospective lessee and the ability of the prospective lessee to perform its obligations under the lease. After the Commission selects a person, it must notify the applicable state agency and send the person's bid to the agency. The act

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<sup>20</sup> R.C. 1509.73(C).

<sup>21</sup> R.C. 1509.73(D).

<sup>22</sup> R.C. 1509.73(E).

<sup>23</sup> R.C. 1509.73(F).

requires the state agency to enter into a lease with the person selected by the Commission.<sup>24</sup>

## Rules

Not later than 270 days after the act's effective date, the Oil and Gas Leasing Commission must adopt rules in accordance with the Administrative Procedure Act that establish all of the following:

(1) The form of and the information to be included in nominations that are submitted to the Commission;

(2) Procedures for the submission of nominations and the amount of the nomination fees to be charged. The rules must require that if a person who has paid a nomination fee does not enter into a lease regarding the parcel of land that the person nominated, the fee must be refunded to the person, and, if applicable, the person that enters into the lease must pay the nomination fee. In addition, the rules must provide that a state agency is exempt from nomination fees and that a person who enters into a lease regarding a parcel of land nominated by a state agency must pay the nomination fee.

(3) Factors that may be considered by the Commission when determining whether to approve or disapprove a nomination;

(4) Procedures and requirements for the submission of bids for a lease;

(5) The amount of bid fees to be charged for the submission of bids to enter into leases;

(6) A standard lease form that is consistent with the practices of the oil and natural gas industries and that contains a landowner royalty of at least  $\frac{1}{8}$ , which must be used by state agencies for leases entered into under the act; and

(7) Any other procedures and requirements that are necessary to implement the act.<sup>25</sup>

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<sup>24</sup> R.C. 1509.73(F).

<sup>25</sup> R.C. 1509.74.

## Use of proceeds from leases

### State Land Royalty Fund

The act requires that except as otherwise provided in the act (see "**Forestry Mineral Royalties Fund; Wildlife Habitat Fund; Parks Mineral Royalties Fund,**" below), all money that is received by a state agency from signing fees, rentals, and royalty payments for a lease entered into under the act must be paid by a state agency into the state treasury to the credit of the State Land Royalty Fund created by the act.<sup>26</sup> Any investment earnings of the Fund must be credited to the Fund.<sup>27</sup>

Money in the Fund must be used by state agencies to acquire land and to pay capital costs, including equipment and renovations and repairs of facilities, of those state agencies that contributed to the Fund. A state agency is entitled to receive the amount that it contributed under the act and a share of the investment earnings of the Fund in an amount that is equivalent to the proportionate share of contributions made by the agency.<sup>28</sup>

### Forestry Mineral Royalties Fund; Wildlife Habitat Fund; Parks Mineral Royalties Fund

The act requires money from signing fees, rentals, and royalty payments for a lease entered into under the act on land owned or controlled by the Division of Forestry, Wildlife, or Parks and Recreation in the Department of Natural Resources to be paid into one of the following funds, as applicable: (1) the Forestry Mineral Royalties Fund, created in the state treasury by the act, (2) the continuing Wildlife Habitat Fund, or (3) the Parks Mineral Royalties Fund, created in the state treasury by the act.<sup>29</sup> Any investment earnings of each Fund created by the act must be credited to the Fund.

Money in the Forestry Mineral Royalties Fund and the Parks Mineral Royalties Fund must be used by the applicable Division to acquire land and to pay capital costs, including equipment and repairs and renovations of facilities, that are owned by the state and administered by the Division. The act requires expenditures from each of those Funds to be approved by the Director of Natural Resources.<sup>30</sup> Under law

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<sup>26</sup> R.C. 131.50(A) and 1509.73(G)(1).

<sup>27</sup> R.C. 131.50(A).

<sup>28</sup> R.C. 131.50(B).

<sup>29</sup> R.C. 1509.73(G)(2).

<sup>30</sup> R.C. 1503.012 and 1541.26.

unchanged by the act, money in the Wildlife Habitat Fund is used to acquire and develop land for the preservation, propagation, and protection of wild animals.<sup>31</sup>

### **Proceeds from oil and gas leases in state parks**

The act requires at least 30% of the proceeds from a lease executed on and after the act's effective date for the exploration and production of oil or gas within or under a state park to be credited to the applicable fund created in the state treasury that supports the state park. The Department of Natural Resources must use the money for expenses associated with the applicable state park. The act specifically requires the money to be used for capital improvements.<sup>32</sup>

### **Oil and Gas Leasing Commission Administration Fund**

The act creates in the state treasury the Oil and Gas Leasing Commission Administration Fund consisting of money received from nomination and bid fees. Money in the Fund must be used by the Oil and Gas Leasing Commission and the Department of Natural Resources to pay their administrative expenses regarding the implementation of the act. Money in the Fund also must be used to pay the actual and necessary expenses incurred by Commission members in the performance of their duties.<sup>33</sup>

### **Authority for state agencies to form drilling unit with class 3 property**

The act authorizes a state agency that owns or controls a parcel of land that is a class 3 property for which a nomination for that property has been denied by the Oil and Gas Leasing Commission to enter into written agreements to use that parcel of land to form a drilling unit that conforms to the minimum acreage and distance requirements that are established under the Oil and Gas Law.<sup>34</sup>

### **Declaration of state policy**

The act declares that it is the policy of the state to provide access to and support the exploration for, development of, and production of oil and natural gas resources owned or controlled by the state in an effort to use the state's natural resources responsibly.<sup>35</sup>

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<sup>31</sup> R.C. 1531.33.

<sup>32</sup> R.C. 1509.78.

<sup>33</sup> R.C. 1509.75.

<sup>34</sup> R.C. 1509.77.

<sup>35</sup> R.C. 1509.71(A).

## Definitions

For the act's purposes, "formation" means any of the following:

- (1) The distance from the surface of the land to the top of the Onondaga limestone;
- (2) The distance from the top of the Onondaga limestone to the bottom of the Queenston formation;
- (3) The distance from the bottom of the Queenston formation to the top of the Trenton limestone;
- (4) The distance from the top of the Trenton limestone to the top of the Knox formation; or
- (5) The distance from the top of the Knox formation to the basement rock.<sup>36</sup>

The Oil and Gas Law defines "owner" to mean the person who has the right to drill on a tract or drilling unit, to drill into and produce from a pool, and to appropriate the oil or gas produced therefrom either for the person or for others, except that a person ceases to be an owner with respect to a well when the well has been plugged in accordance with applicable rules adopted and orders issued under that Law.<sup>37</sup>

The act defines "state agency" to mean: (1) every organized body, office, or agency established by the laws of the state for the exercise of any function of state government, and (2) a state university or college, that is, each of the state universities identified in the State Universities Law and the Northeast Ohio Medical University, including its board of trustees.<sup>38</sup>

## Background

Under former law, there was no centralized state governmental body that oversaw the leasing of state lands for the development of oil and natural gas resources. Instead, several agencies and the board of trustees of a state university had authority to lease state lands for that purpose. The Department of Administrative Services had authority to lease to any person any tract of land owned by the state and under the control of the Department, or any part of such a tract, for the purpose of drilling for or

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<sup>36</sup> R.C. 1509.70(E).

<sup>37</sup> R.C. 1509.01, not in the act.

<sup>38</sup> R.C. 1509.70(F), by reference to R.C. 1.60 and 3345.12.

the pooling of oil or gas.<sup>39</sup> The Chief of the Division of Wildlife in the Department of Natural Resources, with the approval of the Director of Natural Resources, had authority to enter into oil and gas leases on lands owned and controlled by the Division.<sup>40</sup> In addition, the Director of Mental Health, the Director of Rehabilitation and Correction, and the Director of Developmental Disabilities had authority to enter into oil and gas leases on lands controlled by their respective agencies.<sup>41</sup> Finally, the board of trustees of a state university was authorized to enter into contracts for the removal of oil or gas from land under the supervision of the board.<sup>42</sup>

As noted earlier, the act repeals the authority of the various state agencies and state universities discussed above. However, it retains the authority of the Director of Natural Resources to issue permits and enter into leases to remove minerals from and under the bed of Lake Erie. Currently, that removal is precluded by federal law.

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## HISTORY

ACTION	DATE
Introduced	03-01-11
Reported, H. Agriculture & Natural Resources	05-24-11
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House concurred in Senate amendments (57-39)	06-21-11

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<sup>39</sup> R.C. 123.01.

<sup>40</sup> R.C. 1531.06.

<sup>41</sup> R.C. 5119.40, 5120.12, and 5123.23, repealed.

<sup>42</sup> R.C. 3345.181.

