



# Parks & Open Space

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## PARKS & OPEN SPACE ADVISORY COMMITTEE MEETING

Time/Date of Meeting: 7:00 p.m., Thurs., Aug. 25, 2022

Location: Virtual Meeting

<b>TO:</b>	Parks & Open Space Advisory Committee
<b>FROM:</b>	Tina Burghardt, Senior Land Officer Janis Whisman, Real Estate Division Manager Kate Burke, Senior Assistant County Attorney David Hughes, Deputy County Attorney
<b>AGENDA ITEM:</b>	Extraction Oil & Gas, Inc., offer to lease minerals
<b>DATE OF MEMO:</b>	August 15, 2022
<b>ACTION REQUESTED:</b>	Recommendation to the BOCC

*For much longer than Parks & Open Space's history of stewarding open space, the land in this community has been important to the diverse Indigenous communities that continue to thrive here. We are partnering with Indigenous people to make meaningful changes to how we do our work that include Indigenous people, incorporate their perspectives, and honor their land stewardship legacy.*

### **Summary**

In early July 2022, BCPOS received an offer from Extraction Oil & Gas, Inc. ("Extraction") to either lease the rights to drill for oil and gas under 552 acres of county open space land, or to convey a working interest or co-ownership in the wells that would drill those minerals. The county owns the mineral rights as well as the surface lands, both purchased with open space tax monies, so leasing or giving Extraction a share in the mineral rights would constitute a disposition of open space property. The open space sales tax resolutions define a process for consideration of any disposition of open space property, which begins with consideration by POSAC and its recommendation to the BOCC whether to follow through with the disposition. Under the particular circumstances of this leasing offer, staff is recommending rejection of the lease offer for a variety of reasons.

### **Background Information**

#### *The Blue Paintbrush Project*

In 2018, Extraction proposed a massive drilling project on the county border. Extraction would drill up to 32 horizontal wells on a 13-acre well pad in Weld County less than 1,000' from the Boulder County line. The project also entails a separate 10-acre storage and processing facility, together with access roads and pipelines between the facilities, all on the same property. Although the pad site is in Weld County, it is located on the Meglemre CE property over which Boulder County holds a conservation easement. Extraction's project was named "Blue Paintbrush."

The Blue Paintbrush wells are designed to drill vertically approximately a mile and a half down and then drill westward for two miles into Boulder County to extract oil and gas from four square miles of Boulder County open space lands. The drilling area is designated by the Colorado Oil and Gas Conservation Commission ("COGCC") as a drilling and spacing unit, or DSU. The DSU is 93% in Boulder County. A map showing the Blue Paintbrush DSU is

Attachment A. The wellbores will be hydraulically fractured or “fracked” to facilitate oil and gas extraction.

The county objected to the Blue Paintbrush project and the formation of the Blue Paintbrush DSU when Extraction applied for permits at the COGCC. Nonetheless, the COGCC granted all permits necessary to complete the project. The county went on to file two lawsuits related to the project: one challenging the COGCC’s hearing process and one alleging that the county’s conservation easements and many of the pre-existing oil and gas leases over lands in the DSU did not allow for the huge development. Neither of those suits were successful.

### *Mineral Rights Dispute*

In April 2022, after the lawsuits concluded at the appellate courts, the county learned that Extraction was preparing to construct the Blue Paintbrush well pad and planned to start drilling the wells in September 2022. Suspecting that the county owned significant mineral rights in the DSU, the County Attorney’s Office (CAO) initiated a thorough investigation into the county’s mineral ownership. In early June, Extraction sent notice that it had accelerated its drilling schedule to begin July 6. In response, the CAO requested that Extraction put off its plans. Extraction declined, so CAO asked both the chairman of the COGCC and State Senator Steve Fenberg for support in seeking a postponement of drilling until the mineral rights ownership issues could be addressed. As a result, Extraction agreed to pause its drilling plans until approximately February 2023. It began work on the Blue Paintbrush well pad itself in June, which is now largely complete.

In June and July, the mineral title inquiry wrapped up. The reports indicate that the county may own as much as 64% of the mineral acres in the DSU not subject to any oil and gas leases. A map of the county’s likely unleased mineral ownership is Attachment B to this memo. Extraction disputes the expiration of most of the Blue Paintbrush DSU leases.

### *Statutory or Forced Pooling*

In the meantime, Extraction sent the offer to lease 552 acres of the county’s mineral rights that is the subject of this memo and hearing. The offer is Attachment C to this memo. The offer provides three options to the county: to enter a lease with Extraction under the terms detailed below; to enter a co-ownership or working interest relationship with Extraction over the Blue Paintbrush facilities as detailed below; or to be subject to a statutory pooling order by the COGCC known as a forced pooling. Without one of these forms of permission to drill oil and gas owned by the county, Extraction cannot lawfully access those minerals. If the county rejects the offer to lease or enter a working relationship, Extraction will initiate a forced pooling proceeding.

Statutory or forced pooling is a mechanism allowed by state statute (§ 34-60-116(4), C.R.S.) and by COGCC rules (Rule 506). It allows the COGCC to order an unwilling mineral owner into a working interest relationship with an operator for development of the “nonconsenting” owner’s minerals. The nonconsenting owner is charged with its proportionate share of the costs of developing the wells and production facilities plus a penalty of an additional 100% (for 200% total) of its share of the drilling costs. The nonconsenting owner’s costs are taken out of its share of revenues until fully paid, after which the nonconsenting owner receives its share of revenue. The nonconsenting owner remains liable for operational costs throughout the lifetime of the well. Forced pooling has survived legal challenges; Colorado courts have determined that the forced pooling of nonconsenting individuals’ mineral rights does not create an unconstitutional taking.

Before the COGCC can hold a hearing on Extraction's forced pooling application, Extraction is required to send the County an offer to lease its minerals. *See* Rule 506.b. No hearing can occur until at least 90 days after that offer is sent. The lease offer must be made in good faith under reasonable commercial standards of fair dealing and without intent to defraud or seek unconscionable advantage. *See* Rule 506.b.(1). Therefore, the offer received by the county plays two roles: (1) it is a legitimate offer of terms on which the county's minerals can be developed, and; (2) it paves the way for the COGCC to force pool the county's minerals.

### *County Policy on Leasing of Minerals*

Parks staff and the BOCC have a long-time policy of rejecting offers to lease county-owned minerals. Such offers are received from time to time, but this is the first that is tied to an active drilling plan and, therefore, implicates imminent forced pooling and a massive drilling project on the county's eastern border. One reason for the leasing policy is that property purchased with open space funds, such as the county's mineral rights, are subject to the restrictions on open space property laid out in the open space sales tax resolutions. Fracking, extraction, and ultimate combustion of oil and gas are not recognized purposes of open space property as defined in the resolutions, the most relevant of which in this case is the conservation of natural resources. The restrictions on uses and management of open space property are strict enough that any disposition of open space property, such as leasing of mineral rights, is governed by an involved public process starting with consideration and a recommendation by POSAC with input from the public. POSAC will agree on a recommendation to the BOCC, which will be considered at a public hearing before the BOCC.

Second, drilling wells, the fracking process, the storage and processing of oil and gas, and the ultimate combustion of the hydrocarbons all have significant environmental impacts associated with them. In addition to overall environmental and air quality degradation, climate change is exacerbated by the emissions from oil and gas development and fossil fuel consumption. The county has expended and will be expending many millions of dollars in climate-related disaster recovery and prevention. Moreover, the extraction and combustion of fossil fuels carry known health risks. Staff will be providing additional information on these matters at the August 25 meeting.

### **Financial Terms of the Offer**

Although Extraction has permits to drill up to 32 wells on the Blue Paintbrush well pad, the documents it has provided to the County and COGCC indicate it will be drilling 16 wells at this time. The terms and numbers in the Offer relate to those 16 wells. At the time of writing this memo, staff is working with Extraction on financial projections for the project (projected revenues). We hope to have that information ready to present August 25. The terms set out in the Offer are:

1. Lease of minerals
  - a. A signing bonus of \$552,000
  - b. Royalties paid at 17%
  - c. No liability for costs
  
2. Working interest or "participation"
  - a. The County's interest is calculated at 20.342288% of the whole

- b. As a working interest owner, the County would be entitled to 20.342288% of revenues
  - c. The County would also be liable for 20.342288% of the drilling, surface preparation and completions costs (“preliminary costs,” as distinct from ongoing costs)
    - i. The total of the estimated preliminary costs from Extraction for 16 wells is \$104,051,240.00 (total preliminary costs are broken down per well at pages 31-46 of Attachment D)
    - ii. The County’s 20.342288% share of the estimated preliminary costs for 16 wells is \$21,166,402.90 (the County’s share of preliminary costs per well are listed at pages 7-22 of Attachment D)
  - d. The County may also be liable for ongoing operational costs and liability for incidents such as spills and accidents at 20.342288%
3. Statutory (or forced) pooling
- a. As above, under a forced pooling the County becomes a nonconsenting working interest owner
  - b. The County’s interest remains at 20.342288%
  - c. Not only does the County pay \$21,155,402.90 as its share of preliminary costs, it pays an additional \$4,770,344.24 (to total 200% of drilling-only costs) as a penalty for its nonconsent, for a total of \$25,936,747.10.
    - i. The County’s share of costs is subtracted from its revenue share at 87% for a gas well or 84% for an oil well until fully paid, at which time the County would receive its full 20.342288% of the revenue from the wells
  - d. The County would be liable for its 20.342288% share of ongoing operational costs, although as a nonconsenting owner it is not liable for the costs of spills or accidents (this is in addition to statutory protection from tort claims)

**Practical Implications of the Offer**

The Extraction offer raises complicated considerations, some of which are summarized here.

- 1. As discussed above, county policy disfavors any voluntary agreement for development of county-owned minerals. However, this situation is unique for reasons such as:
  - a. Hundreds of mineral acres and millions of dollars are at stake;
  - b. The mineral rights are in an active dispute; and
  - c. Extraction intends to seek a forced pooling order over the county’s minerals if no lease is granted or participation agreement accepted.
- 2. The Colorado Constitution prohibits counties from voluntarily entering working interest or co-owner relationships with private entities in many cases.
- 3. If Extraction does not get permission from the county to access its minerals (a lease or participation), it will initiate a forced pooling proceeding with the COGCC. In fact, Extraction already filed an application for a forced pooling hearing with the COGCC on July 7. No hearing on that application can occur before October at the earliest, but it demonstrates Extraction’s intent.

4. Extraction must prove that it owns or has control of more than 45% of the mineral rights in the Blue Paintbrush DSU to be eligible for a forced pooling order from the COGCC. The County Attorney's Office has legal opinions indicating that Extraction may not be able to meet that threshold.
5. If Extraction does obtain a forced pooling order over the county's minerals, the county will pay a \$4,770,344.24 penalty as a nonconsenting owner, in addition to becoming liable for drilling and ongoing operational costs.
6. If the county does not agree to lease its minerals or to participate in the Blue Paintbrush wells, and Extraction cannot obtain a forced pooling order, the Blue Paintbrush project will be reduced in size or prevented, in which case the county will not receive any revenue for its mineral rights.

### **Public Process**

The disposition process outlined in the open space sales tax resolutions begins with consideration by POSAC at a public hearing and, based on staff's presentation and recommendation and comments from the public, its recommendation to the BOCC on August 25, 2022. The BOCC will then hold a public hearing on the lease offer, consider POSAC's recommendation, staff's recommendation and comments received from the public, and make a decision on the question. If the BOCC determines to accept the lease or working interest offer and dispose of the mineral rights, a 60-day waiting period will follow, in which county residents may initiate a citizen referendum under § 29-2-104, C.R.S., to put the issue to a vote. If no referendum is initiated, the county may then proceed with accepting the lease or working interest.

### **Staff Recommendation**

For the reasons summarized in this memo and presented at the August 25, 2022, POSAC meeting, staff recommends that POSAC make a recommendation to the BOCC to reject Extraction's offer to lease county minerals or convey a working interest in the Blue Paintbrush wells.

### **POSAC Action Requested**

Recommendation to the BOCC whether to accept Extraction's offer to lease 552 acres of county-owned mineral rights, or to accept Extraction's offer of a working interest in the Blue Paintbrush wells, or to reject both offers.