

Legal Issues Abound In Marcellus, Utica

Editor's Note: The Marcellus and Utica shales are transforming oil and gas development in the Appalachian Basin. But with the rapid increase in activity comes a new set of challenges across the entire operational spectrum for independent oil and gas companies as well as service and supply companies—from permitting and leasing, to well stimulation and production.

What are the most pressing legal issues impacting development activity in the Marcellus and Utica plays in Ohio, Pennsylvania, West Virginia and New York, and what can operators do to overcome the challenges these issues present to their businesses, employees and profit margins?

To answer these questions, *AOGR* presented a series of questions to a panel of legal experts from four law firms active in the Appalachian region focused on legal issues in four key areas: leasing and geophysical/drilling, hydraulic fracturing, air quality, and human resources. Panelists were Sharon O. Flanery, lead attorney for the energy team of Steptoe & Johnson in Charleston, W.V.; Joseph K. Reinhart, a shareholder and chairman of the natural resources development group of Babst Calland in Pittsburgh; David R. Overstreet, partner with K&L Gates in Pittsburgh; and Thomas S. Giotto, co-chair of the labor and employment section for Buchanan, Ingersoll & Rooney in Pittsburgh. Questions and answers from Joseph K. Reinhart follow:

Q: *Hydraulic fracturing has become the most scrutinized aspect of oil and gas development in the Northeast*

and other regions across the country. What are the key legal issues regarding fracturing as you see them in the Appalachian Basin, and what are the tangible risks related to fracturing for oil and gas companies as well as their service company partners?

REINHART: Because of the large volumes of water necessary to perform hydraulic fracturing, legal issues associated with water management present significant challenges to developing unconventional resources in the Appalachian Basin. Water management issues in the Appalachian Basin generally fall into two main cate-

gories. First is securing the necessary government authorizations to allow operators to obtain sufficient freshwater to conduct fracturing operations. Second is permitting and compliance obligations associated with the discharge, disposal and/or recycling of frac flow-back water. Both types of water management activities are receiving considerable public attention, which in turn, is causing the agencies overseeing these activities to aggressively enforce the rules associated with these operations.

Withdrawals of surface water and groundwater for use in fracturing operations in the Appalachian Basin are regulated by federal interstate compact commissions, as well as state government. Separate and distinct federal commissions may regulate consumptive water uses for operations located within the Susquehanna, Delaware and Ohio river basins.

For example, the Susquehanna River Basin Commission (SRBC) oversees many aspects of water sourcing operations that occur within a 27,510 square-mile watershed in central Pennsylvania, where Marcellus Shale operations are prevalent. The SRBC prohibits water withdrawals without prior approval, and the agency may impose significant restrictions on the quantity, timing and rate of withdrawal.

The SRBC also regulates certain transfers and diversions of freshwater into and out of the basin. The SRBC is authorized to issue cease-and-desist orders and penalties, and has taken enforcement actions against operators for failing to secure approvals prior to use. The Pennsylvania Department of Environmental Protection also requires operators to pre-



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pare and submit water management plans in order to obtain drilling permits for Marcellus Shale wells.

The disposal, recycling and discharge of flow-back water from Marcellus Shale wells is subject to comprehensive rules and regulations implemented by the DEP under several state laws. Pennsylvania DEP promulgated stringent new rules governing discharges of water containing high levels of total dissolved solids. Although Pennsylvania DEP initially grandfathered many treatment facilities under these rules, the agency has since directed the natural gas industry not to transport produced water to these facilities, causing many operators to significantly change their water disposal practices. Many operators now are transporting their produced water from well sites in Pennsylvania to underground injection wells in Ohio, and/or investing significant amounts of money in sophisticated water recycling and reuse operations.

The Pennsylvania DEP also requires Marcellus Shale operators to prepare and submit extensive reports regarding their produced water disposal practices. The agency has pursued numerous enforcement cases against operators and service providers for failing to secure permits for transferring produced water and for allowing unauthorized releases of flow-back water at well pads.

The risks posed to operators and service providers for water management activities associated with fracturing include delays associated with securing necessary approvals, and fines and penalties associated with unauthorized withdrawals of fresh-water or unpermitted discharges of produced water. In addition, the environmental laws impose obligations on operators to restore or replace public and private water supplies impacted by well drilling activities. These laws impose rebuttable presumptions in favor of the landowner that alleges damages to a water supply after drilling has occurred. Increasingly, landowners claiming damages to water supplies may also assert other claims for personal injury and property damage.

Q: *There have been a number of court rulings on issues related to hydraulic fracturing. What are the key cases as you see them for establishing precedent, and what implications may these decisions have for operators?*

REINHART: Although courts have issued some rulings in litigation related to hydraulic fracturing and claims by landowners, there remain many open questions in this developing area of the law. Cases filed to date show plaintiffs' attorneys exploring a variety of claims and theories based on a variety of factual scenarios, many of which have not yet been considered by courts in any published opinions. Operators can expect plaintiffs' attorneys to refine these claims and theories, and raise new ones as courts issue decisions.

At least one court, the U.S. District Court for the Middle District of Pennsylvania, has denied motions to dismiss strict liability claims on the basis that it was premature to decide at the beginning of a case whether natural gas was an abnormally dangerous activity. In *Fiorentino v. Cabot Oil & Gas Corp.*, 750 F. Supp. 2d 506 (M.D. Pa. 2010), and *Berish v. Southwestern Energy Production Co.*, 763 F. Supp. 2d 702 (M.D. Pa. 2011), the plaintiffs asserted claims relating to the defendants' drilling operations, and the defendants moved to dismiss the claims for strict liability.

In each case, the court held that more facts were needed to determine whether natural gas drilling was an abnormally dangerous activity. If these decisions are followed in other cases, plaintiffs will be able to pursue strict liability claims against operators through the discovery phase of a case before the court will decide the issue.

Additionally, another court applied an arbitration clause in an oil and gas lease and required that toxic tort and property damage claims relating to drilling operations and hydraulic fracturing be arbitrated. In *Phillips v. Chesapeake Appalachia LLC* (M.D. Pa., 3:11-mc-00126), the court granted a petition to compel arbitration filed by landowner plaintiffs. The court ordered the parties to proceed to binding arbitration under the American Arbitration Association commercial rules.

This means that operators potentially could be required to defend toxic tort and property damage claims in an arbitration forum, which may apply more permissive rules with respect to scientific evidence and may not provide an opportunity to appeal any decisions. Arbitration may offer benefits to operators defending claims as well, including less extensive discovery, a more streamlined process, and a decision maker who may be more experienced and knowledgeable about the issues than a typical jury.

Q: *Companies routinely disclose publicly data on fracturing/flow back fluids on a well-by-well basis. Is this an effective strategy and are their legal implications companies should be aware of before releasing such data? From a legal standpoint, what further steps can operators take to provide assurances to landowners (and the public at large) regarding the environmental safety of fracturing operations?*

REINHART: The public release of data identifying chemicals in fracturing fluids that may be labeled "hazardous" or "toxic" certainly has the potential to create alarm and provide opponents of shale development with an additional reason to oppose using the material at a well site. However, operators also should consider that many federal and state laws impose disclosure obligations on companies that store or use significant amounts of chemicals. These laws may apply to certain types of activities associated with hydraulic fracturing operations. These disclosure obligations are very specific and vary considerably, based on the volume and type of chemicals stored or used at a facility.

However, it is not unusual for industrial operations to maintain material safety data sheets for chemicals managed at their facilities, and these businesses also may be required to report the presence of these chemicals to government agencies and local officials. The purpose of these reports is to alert state and local authorities that chemicals posing potential risks to public health and safety are stored at a location in the event of a fire, spill or emergency. Owners and operators of tanks storing large volumes of petroleum or hazardous materials are required to maintain spill prevention and control plans in the event of an unplanned release. If implemented properly, these types of plans can assist first responders who arrive at the well site to manage spilled material appropriately and minimize potential threats to human health and the environment.

Similarly, the public disclosure of fracturing/flow-back water stored or managed on a well pad may be an appropriate element of a contingency plan designed to reduce the risks associated with an unplanned fire or release. Operators also may want to consider offering this information to landowners. If this effort is conducted properly, it may create an opportunity for the operator to explain the relatively small percentages of hazardous substances in fracturing fluids and elim-



inate the mystery often associated with fracturing fluids in newspaper articles.

Q: *All of the states with Marcellus activity are in the process of adopting comprehensive regulations to deal with drilling and fracturing, including areas such as water management and discharge, erosion and sedimentation control, and frac fluid disclosure. Of course, in New York, activity is at a standstill while the state drafts a supplemental generic environmental impact statement to address fracturing and horizontal drilling. What should operators know about these various rule-making initiatives and how they could impact hydraulic fracturing operations?*

REINHART: Operators who intend to

conduct drilling and fracturing operations within the Marcellus Shale region should anticipate that the rules and regulations governing those operations will become more complex, and that more stringent permitting and compliance standards will be imposed.

Although the states within the Marcellus Shale region have had laws and regulations in place for many years governing conventional oil and gas development, many of these laws and regulations did not contemplate horizontal drilling techniques and hydraulic fracturing operations associated with shale development. Therefore, operators should monitor changes to existing rules and regulations, as well as new rule-making initiatives.

In addition, operators should be aware that many agencies implementing existing environmental rules and regulations in

the Appalachian Basin are re-evaluating the manner in which permit waivers and general permits will be applied to Marcellus Shale operations. This re-evaluation process includes both state agencies and federal agencies, such as the Environmental Protection Agency and the Army Corps of Engineers.

Many operators have relied for years on general permits issued in lieu of individual permits as a means to expedite the drilling and development of well sites, as well as for constructing pipelines and compressor stations. It would be prudent for operators to both affirmatively engage in the rule-making process by monitoring and commenting on proposed new regulations, and to re-examine their drilling plans and construction schedules to ensure that adequate time has been set aside to secure the necessary authorizations. □