

Legislative Analysis



ENHANCED ENERGY PRODUCTION

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House Bill 4885
Public Act 82 of 2014
Sponsor: Rep. Aric Nesbitt

House Bill 5255
Public Act 84 of 2014
Sponsor: Rep. Thomas F. Stallworth III

House Bill 5254
Public Act 83 of 2014
Sponsor: Rep. Rick Outman

House Bill 5274
Public Act 85 of 2014
Sponsor: Rep. Peter Pettalia

House Committee: Energy and Technology
Senate Committee: Energy and Technology
Complete to 10-29-14

A SUMMARY OF HOUSE BILLS 4885, 5254, 5255, AND 5274 AS ENACTED

BRIEF SUMMARY:

House Bill 4885 reduces the severance tax on oil and gas production achieved through carbon dioxide secondary or enhanced recovery projects.

House Bill 5254 revises the definition of "pipeline" to include a pipeline used to transport carbon dioxide (CO₂) substances.

House Bill 5255 grants the right to authorized entities to acquire rights-of-way for transport, installation, and maintenance of CO₂ pipelines by eminent domain for CO₂ substances.

House Bill 5274 amends the title and various provisions of Public Act 16 of 1929 that previously applied to crude or petroleum so that they also apply to CO₂ substances. The bill adds a definition of "carbon dioxide substance."

The bills are described in more detail later in the summary.

FISCAL IMPACT:

As written, House Bill 4885 has an unknown impact on state revenues. Because the severance tax is based on the market prices and production of oil and natural gas, none of which is known in advance, a precise fiscal impact cannot be determined. The extent to which the severance tax rate cut makes CO₂ injection recovery methods financially viable determines whether the proposed legislation has a positive or negative effect on state revenues. As an example, if 100,000 barrels of oil are produced using this method each year, and the price of oil is \$100 per barrel, the tax revenue under current law would be \$660,000; under the proposed legislation the severance tax revenue would be

\$400,000. If this oil would have been produced regardless of the tax rate, then state revenues would have declined \$240,000. Conversely, if none of this oil would be produced under the current tax rate, then revenues would have increased. As a reference, the oil and gas severance tax currently generates approximately \$60 million in General Fund revenue per year.

House Bills 5254 & 5255 would have no significant fiscal impact on the Department of Environmental Quality.

House Bills 5254, 5255, and 5274 would likely have a neutral fiscal impact on the Michigan Public Service Commission (PSC); PSC costs of reviewing applications and ruling on whether to approve construction and operation of pipelines to transport crude oil, petroleum, and (if HBs 5254, 5255, and 5274 are enacted) CO₂ are (would be) supported with revenue generated by Public Utility Assessments collected under the Costs of Regulating Public Utilities Act of 1972, which authorizes the PSC to prescribe fees to fund its regulatory responsibilities.

DETAILED SUMMARY:

House Bill 4885 amends the Michigan Severance Tax Act (MCL 483.2a), which levies a severance tax on gas and oil production. Under the act, producers or purchasers must report monthly on the oil and gas severed from the soil and pay a tax based on the value of the gas or oil extracted. Regardless of the extraction method used, producers currently pay a severance tax of 6.6 percent of the gross cash market value for oil (4 percent if from a stripper oil well) and 5 percent of the gross cash market value for natural gas.

Under the bill, for carbon dioxide (CO₂) secondary or enhanced recovery projects approved after March 30, 2014, a lower severance tax rate would apply to natural gas or oil extracted from a "carbon dioxide secondary or enhanced recovery project."

Specifically, the monthly severance tax required to be paid by each producer would be reduced to 4 percent of the gross cash market value for either oil or natural gas. However, the lowered severance tax rate would not be available to a producer convicted of an antitrust violation or conspiracy to commit an antitrust violation that is a crime under the laws of the state.

"Carbon dioxide secondary or enhanced recovery project" is defined by the bill to mean operations designed to increase the amount of oil or natural gas recoverable from a reservoir, as by injection of CO₂, either alone or as a primary component of a mixture with other substances, as long as the project had been approved as a secondary or enhanced recovery project by order of the Supervisor of Wells under the authority of Part 615 or 617 of the Natural Resources and Environmental Protection Act.

House Bill 5254 amends Section 2a of Public Act 16 of 1929 (MCL 483.2a), which regulates the transportation and sale of crude oil and petroleum through pipelines. Section 2a was added in 1997 to require persons conducting survey work for a proposed

crude oil or petroleum pipeline to notify affected property owners in writing before a survey crew enters the owner's property. Any offer to a landowner for an easement for locating, constructing, maintaining, and operating pipelines on agricultural property is required to include specific information that includes assurances that agricultural drainage tile damaged or removed during construction or repair of the pipelines will be returned to its original condition, that topsoil will be replaced, that the property owner will be compensated for lost productivity of the land and for damages incurred after the pipeline is constructed related to the exercise of easement rights by the pipeline owner, and that the landowner has rights under the Uniform Condemnation Procedures Act.

Previously, the definition of "pipeline" contained in Section 2a means a pipeline used or to be used to transport crude oil or petroleum. The bill adds transporting *carbon dioxide substances* to this definition.

Further, when *laying pipelines*, the current regulations described above regulating the notification requirements, repairs, and compensation to affected landowners would apply.

House Bill 5255 amends Section 2 of Public Act 16 of 1929 (MCL 483.2). Previously, the act granted the right for a corporation, association, or person to acquire necessary rights-of-way for transporting petroleum by pipeline via eminent domain.

The bill specifies that the authorized entities (which would be expanded to include a partnership, governmental entity, or other legal entity under House Bill 5274) is granted the right to condemn *property* by eminent domain and use of the state's highways to *acquire necessary rights-of-way* for any of the following purposes:

- To transport crude oil or petroleum or CO₂ substances.
- To locate, lay, construct, maintain, and operate pipelines for the above purposes.

In addition, the act previously required the condemnation (eminent domain) proceedings to be conducted *in accordance with the same procedure and in the same manner as is provided by the laws of this state for the condemnation of right of ways by railroad companies*. The highlighted portion has been eliminated and proceedings are instead be required to be conducted as provided in the Uniform Condemnation Procedures Act.

House Bill 5274 also amends Public Act 16 of 1929 (MCL 483.1 et.al). It includes certain substances consisting primarily of carbon dioxide within the act's purview. The bill amends the title to specify that the act also regulates the business of certain substances consisting primarily of carbon dioxide through pipelines, as well as regulate its purchase and storage.

The bill also revises the following sections that currently apply to crude oil and petroleum to apply also to *carbon dioxide substances*:

** Section 1: Specifies that the right of an entity to transport or to buy or sell these substances (crude oil, petroleum, or CO₂ substances), to engage in the business or

operations of the substances, or to locate the necessary pipelines along or under any present or future highway in the state, or have or possess the right of eminent domain, is authorized by and subject to the provisions of the act.

The bill defines "carbon dioxide substance" to mean a gaseous or liquid substances, consisting primarily of carbon dioxide, that will be put in storage or that have been or will be used to produce hydrocarbons in secondary or enhanced recovery operations.

"Person" is defined as an individual, partnership, corporation, association, governmental entity, or other legal entity.

** Section 3: Grants to the MPSC the power to control, investigate, and regulate entities carrying or transporting the substances through pipelines; exercising or claiming the right to engage in the business of piping, transporting, or storing the substances; or engaging in the business of buying, selling, or dealing in the substances within the state. Producers and refiners of crude oil and petroleum are exempted from regulation under this provision; the bill extends the exemption to refiners or producers of CO₂ substances.

** Section 4: Defines "common purchaser" and requires a common purchaser to purchase substances without discrimination. The bill includes CO₂ substances.

** Section 5: Defines "common carrier" and requires a common carrier engaged in the business of carrying or transporting the substances to do so without discrimination, directly or indirectly. The bill includes CO₂ substances.

BRIEF DISCUSSION OF THE ISSUES:

As a package, the bills revise current laws regulating the transport of crude oil and petroleum by pipeline to include carbon dioxide substances and to provide a tax incentive for companies to use CO₂ to recover additional oil or natural gas from existing wells. Even with today's technologies, some oil remains in the bottom of wells. Enhanced oil recovery (EOR) methods are used to recover an additional 15-20 percent of product that would be otherwise unrecoverable. Using CO₂, supporters say, reduces the demand for water in EOR operations and, by using and permanently storing sequestered CO₂, reduces the amount of carbon dioxide released into the atmosphere. The lowered severance tax rate for CO₂ operations should provide an incentive for drilling companies to invest in the infrastructure needed to transport and store the CO₂ required for an operation. Appropriately, a producer convicted of an antitrust violation, or attempted antitrust violation, would not be able to enjoy the lowered severance tax rate.

The other bills in the package put the regulation of CO₂ pipelines under the oversight of the Michigan Public Service Commission, expand current eminent domain authority to include CO₂ pipelines, authorize fair compensation for landowners and require companies to restore landowners' property after laying CO₂ pipelines, and apply other regulations currently in place for crude oil and petroleum pipelines to CO₂ pipelines. Procedures for taking land by eminent domain necessary to lay, maintain, operate, and

access pipelines for CO₂, crude oil or petroleum, would now be conducted under the Uniform Condemnation Procedures Act, which does contain protections for homeowners, rather than under procedures in place for railroad companies when laying track.

Supporters say the bills DO NOT apply to hydraulic fracking and would be used in existing injection wells to recover oil and gas that would otherwise not be recovered. Thus, supporters see the bill package as a "Win-Win" for all by collecting taxes on oil or gas recovery projects that would not be collected today, increasing available supplies of oil and natural gas, and providing a way to use – and permanently remove – carbon dioxide from the atmosphere that would otherwise contribute to damaging the environment.

However, concerns have been raised that include the following:

- The bills create another situation in which a landowner's property may be seized under eminent domain, a process that has subjected some property owners to having little say over where pipelines would be located on their property.
- While use of CO₂ in EOR operations may remove some pollutants from the atmosphere, building a new transport infrastructure for transporting CO₂ is not without other environmental and safety concerns, such as the potential to release even more greenhouse gasses into the environment.
- Though initially projected to be used in existing wells, the bills could encourage certain new wells to be drilled that may not otherwise have been drilled due to the amount of oil or natural gas deemed unrecoverable by current methods. If so, drilling could be increased, even in pristine areas, resulting in negative environmental impacts.
- Tax breaks are being given to a business segment that enjoys high profits already. Some say our severance tax rates are already lower than many other states and so a reduced tax rate that lowers state revenue should not be given to enterprises that may result in future environmental damage that affects, and eventually costs, Michigan residents.

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■ This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.