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LATHAM&WATKINS LLP

June 12, 2014

Santa Barbara County Board of Supervisors
105 East Anapamu Street, Room 407
Santa Barbara, CA 93101
Attn: Clerk of the Board

Re: <u>Board of Supervisors June 13, 2014 Meeting, Departmental Agenda Item No. 1, the Initiative to Ban Energy Production in Santa Barbara County</u>

Dear Chair Lavagnino and Honorable Supervisors:

We are writing on behalf of our client, Californians for a Safe, Secure Energy Future ("CSSEF") regarding the Initiative to Ban energy production in Santa Barbara County.

At your May 20, 2014 meeting, your Board directed County staff to prepare a report addressing the topics identified in Elections Code section 9111 regarding the Initiative. County staff has now completed its analysis. County staff's Impact Analysis Report on the Initiative ("Report") shows the Initiative for what it is – an attempt to stop all oil drilling in the County under the guise of prohibiting hydraulic fracturing and acid stimulation. The Report's independent and impartial analysis confirms that the Initiative would dramatically curtail all oil production in the County by banning traditional production techniques.

The Initiative speaks to alleged concerns over hydraulic fracturing. But the Report confirms that there is no hydraulic fracturing or acid well stimulation in the County today and that none is proposed. The Initiative argues that it would create both environmental and economic benefits. But the Report confirms that the Initiative's limits on oil production activities could substantially harm the County's finances and would shrink the County's budget. The Initiative argues that Santa Barbara County's existing oil and gas industry does not contribute to a healthy economy. But the Report confirms that hundreds of millions of dollars in economic activity could be lost if the Initiative is adopted and oil and gas extraction activities are curtailed or eliminated as a result.

Ultimately, the Report speaks for itself. The Initiative, if adopted, would have substantial financial impacts and no environmental benefits.

A. The Report Confirms That Hydraulic Fracturing and Acid Stimulation Are Not Used in the County

Existing oil and gas operations. The Report concludes that no existing onshore wells in the County use hydraulic fracturing or acid stimulation. The Report identified 1,167 active onshore wells in the County. Regarding these 1,167 active wells, the Report concluded:

> No wells in Santa Barbara County are hydraulically fractured, nor are any wells produced by high pressure acid stimulation. (Report, p. 2.)

Recently approved and proposed oil and gas operations. The Report concludes that no recently approved or proposed wells in the County would use hydraulic fracturing or acid stimulation. County staff reviewed each project that recently received approvals, has applied for permits, or is in the process of applying for permits for new oil and gas wells. Of those 903 new wells, the Report identified none that propose to use hydraulic fracturing or acid stimulation.

The Initiative asserts that high-intensity petroleum operations, particularly hydraulic fracturing and acid stimulation, are occurring with greater frequency in the County today and will occur with greater frequency in the future. The Report confirms that this is wrong. The Report confirms that Initiative is targeted at a condition – the use of hydraulic fracturing and acid stimulation – that does not now exist and will not exist in the near future.

B. The Report Confirms That The Initiative Would Ban Routine Production and Maintenance Methods Used At Every Active Well In The County

Regarding the oil and gas extraction activities that actually are occurring in the County today, the Report found:

> One hundred percent of the active wells use at least one secondary or enhanced recovery technique identified in the measure, if for no other reason, than well maintenance. (Report, p. 2.)

Further, the Report found that maintenance activities are routine and expected in oil and gas extraction activities:

> For example, acid and other chemical treatments are routinely added to wells to remove scale and other impurities which clog well perforations and impede hydrocarbon flow from the production zone. These chemicals flow to the surface with the hydrocarbons and are removed during processing. (Report, p. 2.)

These production methods are required because "historic oil field production has greatly reduced field pressures and therefore most wells soon require some type of enhanced recovery to assist the flow of hydrocarbons to the surface." (Report, p. 2.) The Report specifically finds that these processes are routine and that substances used in these processes flow to the surface and are removed. (Report, p. 2.)

To assist in the flow of hydrocarbons, producers in the County routinely inject safe substances such as water and steam into the formation. The Report states:

> Waste water extracted from the oil production onsite is also routinely re-injected back into the producing formation, to stimulate flow or for final disposal. Air, steam, CO2, nitrogen and other gases are also used to aid in production, depending on reservoir characteristics. (Report, p. 2.)

The Report's findings regarding proposed new wells are similar. Regarding proposed wells, the Report states:

> In summary, of the permitted, proposed and anticipated 903 new wells, 804 (89%) propose, or are anticipated to propose well stimulation treatments, and use secondary and enhanced recovery operations over the life of the project to develop the hydrocarbon reserves. (Report, p. 3.)

These wells, which would use extraction methods that "include the injection of substances such as water, steam, air or gases to produce the oil at the surface," (Report, p. 2), could not be permitted under the Initiative.

C. <u>The Report Confirms That The Initiative Would Stop All Oil And Gas Production</u>

If adopted, the Initiative would shut down the oil and gas industry in Santa Barbara County. The Report concludes that the history of oil production in the County has greatly reduced field pressures, making conventional extraction methods increasingly obsolete. As a result, the Report concludes:

> [M]ost wells soon require some type of enhanced recovery to assist the flow of hydrocarbons to the surface. (Report, p. 2.)

The Report acknowledges that once "vested right" wells produce all of their available oil using conventional methods, future wells could only use traditional methods because all enhanced methods would be prohibited, and "the trend line would likely move toward fewer barrels of oil." (Report, p. 3.) But the Report does not address the Initiative's prohibition on all new permits for ***existing*** projects that use these routine methods that the Initiative would ban. Oil operations are dynamic and complex, and constantly require new permits for changing operations, for new construction, and to permit continued County oversight. If no new permits could be issued for ***existing***, permitted enhanced recovery activities, those operations would be required to shut down in short order.

D. The Report Confirms That The Initiative Would Cost The County At Least $16 Million In Direct Revenue Every Year

Santa Barbara County's oil and gas industry is a major contributor to the County's budget. Regarding the oil and gas industry's direct property tax payments, the Report found the following:

> In 2013, oil production companies paid approximately $16.4 million in local property taxes to all tax receiving entities. This includes taxes paid on the assessed values of real property (e.g. land and property improvements) owned by oil production companies, but also the ad valorem tax collected on the assessed value of proven oil reserves in the ground. The $16 million represents 2.65% of the secured property tax roll collected by the County of Santa Barbara. (Report p. 3.)

The Report found that the County spends this $16.4 million in revenue from the oil and gas industry as follows:

- Fire Protection: $2.1 million
- Schools: $10.2 million
- County Government: $3.57 million
- Special Districts: $493,000

Thus, if the Initiative passes, the County would see shortfalls of two million dollars in its fire protection budget and more than ten million dollars in its education budget.

The Report states that if the Initiative were adopted, the property values that support these taxes would decline. As a result, property tax collection from oil production companies would also decline. Moreover, if oil production companies sell off their capital assets and infrastructure, this would "accelerate the tax revenue loss" even more. (Report, p. 4.)

E. The Report Confirms That The Initiative Would Harm the County's Economy

The oil and gas industry is also a major contributor to the County's economy generally. Relying on the University of California at Santa Barbara Economic Forecast Project study of the economic impact of the oil and gas industry from 2013 by Dr. Peter Rupert, the Report states:

> Doctor Rupert reported a total (direct, indirect, and induced) economic impact of $291.4 million attributable to the onshore oil and gas extraction business in 2011. (Report, p. 4.)

These economic impacts relate to direct economic activity from oil and gas generation, indirectly related but attributable sourcing of service and supplies to the oil and gas extraction business, and induced economic activity of broad local spending from employees of the oil and gas extraction companies. If the Initiative is adopted, all of this economic activity, as well as the stable, high-paying jobs provided by the oil and gas industry to County workers, would be at risk.

* * * * *

The County's Report concludes that the Initiative will effectively stop all existing oil drilling in Santa Barbara County and that there is no hydraulic fracturing or acid well stimulation occurring or planned. The Report also concludes that stopping existing oil and gas operations would have substantial economic impacts and does not identify any environmental benefits from the Initiative.

In addition to the items addressed in the Report, the Initiative raises significant legal issues under the U.S. and California Constitutions and the California Environmental Quality Act, as discussed in our prior correspondence with the Board. The potential financial exposure and liability to the County in defending the Initiative against the likely takings, preemption, and other legal challenges are substantial and provide additional reasons for the Board not to adopt or support the Initiative.

Therefore, consistent with the Report's conclusions and for all the reasons stated therein, we urge you not to adopt the Initiative at your June 13, 2014, meeting.

Very truly yours,

George J. Mihlsten
of LATHAM & WATKINS LLP

cc: Michael C. Ghizzoni, Santa Barbara County Counsel
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