

WSR 24-24-055  
PROPOSED RULES  
DEPARTMENT OF  
NATURAL RESOURCES

[Filed November 26, 2024, 4:35 p.m.]

Original Notice.

Preproposal statement of inquiry was filed as WSR 24-19-083.

Title of Rule and Other Identifying Information: Update to geothermal lease rates on department of natural resources (DNR)-managed properties (WAC 332-22-200 through 332-22-230).

Hearing Location(s): On January 14, 2025, at 9-11 a.m., at the Natural Resource Building, Room 432, 1111 Washington Street, Olympia, WA.

Date of Intended Adoption: February 17, 2025.

Submit Written Comments to: Kelsay Stanton, Mining and Minerals Program, 1111 Washington Street, Olympia, WA 98504, email Kelsay.stanton@dnr.wa.gov, fax 360-902-1789, beginning December 18, 2024, 8 a.m., by January 17, 2025, 5 p.m.

Purpose of the Proposal and Its Anticipated Effects, Including Any Changes in Existing Rules: SB [ESSB] 6039 required DNR to update its geothermal resources lease rates for DNR-managed properties so that the lease rates are competitive with geothermal resource lease rates adopted by the federal government and other western states, while also maintaining obligations to trusts and not adversely impacting federally reserved tribal rights. The rule-making process changes WAC 332-22-200 through 332-22-230. The updated rules propose new lease rates as well as propose language to improve clarity of the DNR's geothermal resources lease process. This process does not address any other regulations on geothermal resources and only affects DNR and DNR-managed properties.

Reasons Supporting Proposal: The following provides justification for the proposed new rules:

WAC 332-22-200: The rule update is mandated to ensure that lease rates are competitive with other western states and the federal government (RCW 79.13.530). Some western states have rental rates documented in code/rules while others note the rate is set by a state lands board, often determined by fair market value or negotiation. While the DNR has higher rental rates than Montana, California, and Nevada, it has lower rental rates than the BLM. Additionally, discussion with state trust land managers for Idaho and Utah, which have rates determined by the board, indicates DNR has lower or comparable rental rates to those states. The proposed rule will lower the minimum rental fee to \$1.00 per acre for years one through five and \$2.00 per acre for years six through 10, while maintaining the current lowest total rent amounts (\$250 and \$500, respectively). This will make DNR competitive with other western states and the BLM with regard to the minimum rental fee, although actual rental fees may be higher depending on fair market value and contract negotiation. The lowest possible total rent amounts remain the same to ensure trust-lands are generating some value to beneficiaries. The proposed rule also includes language indicating that the lessee is required to obtain necessary local, state, or federal permits. This is standard practice with DNR contracts and is included in the WAC to ensure prospective lessees understand their obligations. The proposed rule also adds language addressing production facilities associated with the geothermal resource, noting that those will require a commercial lease and be sub-

ject to the commercial lease process. This is to ensure that trusts receive full and appropriate value for commercial sites.

WAC 332-22-210: DNR's production royalty is higher than some western states and the BLM, while similar to other western states. There are several western states that base their production royalty rates on fair market value. The proposed rule will change the DNR's production royalty for gross sales and products utilized but not sold to a range of two to 20 percent, and will reduce the royalty on gross proceeds of byproducts to five percent. This makes the byproduct royalty the same as DNR's royalty on minerals sold through mining contracts. The proposed rule includes clarification that the production royalty may be different for different products sold, such as electricity, heat, steam, etc. The proposed rule will make DNR competitive on some aspects with other states, such as Idaho and Utah, as well as the BLM, while setting the byproduct royalty at the same royalty for minerals sold through mining contracts, thus preventing potential confusion. Additionally, the proposed rule makes it easier for DNR to set different rates for different geothermal resource products sold or utilized, thus potentially improving DNR's competitiveness with other states and the federal government while also maintaining best value for trust beneficiaries.

WAC 332-22-220: While only one other state specifically notes a minimum royalty requirement in their code (California), discussion with Idaho and Utah state trust land managers indicate they include a minimum royalty in their leases. Idaho's minimum royalty is a set rate that increases with time. Utah has a rate of \$5 per acre for the minimum royalty. Because the DNR's minimum royalty replaces the annual rent starting year 11, the proposed rule will lower the lowest minimum royalty to \$2.00 per acre. The lowest possible total minimum royalty remains at \$2,000 to ensure some value to trust-beneficiaries. The proposed rule includes clarification that the minimum royalty calculation will be based off the total leased acreage, so as not to be confused with leased acreage within a production unit only. The ability to reassess the minimum rate through time will be maintained.

WAC 332-22-230: The proposed rule adds language WAC 332-22-230 to clarify that if a proposed consolidation with other entities includes plans for production facilities on state lands, that acreage will be removed from the original lease and will require a commercial lease. This ensures best value for commercial real estate for trust beneficiaries. There are no other changes to this rule, as it already notes that if leaseholds that are only partially included in a unit plan with other entities, then those portions shall be segregated into separate leases with the annual rent and minimum royalty paid independently from other lease areas. Additionally, it already notes that an appropriate accounting system will be used to ensure DNR receives the correct royalties.

Alternatives: The proposed rules aim to make DNR more competitive with most western states and the federal government while still giving DNR the opportunity to negotiate rates to benefit trust beneficiaries. There are many potential combinations of annual rental fees, minimum annual royalties, and production royalties. One alternative would require all rates/royalties to be determined by fair market value alone. However, this could introduce complications to the timeliness and cost of executing a lease by requiring DNR to obtain a fair market value assessment. Additionally, the proposed rule still allows for adjustment of rates and royalties with time, and only sets a minimum or

range, giving DNR flexibility to be competitive, provide the best opportunity for trust beneficiaries, and still reflect market values.

Statutory Authority for Adoption: This rule making is mandated by an amendment to RCW 79.13.590 and section 465, chapter 334, Laws of 2003, through section 2 of SB 6039.

Statute Being Implemented: RCW 79.13.590 and section 465, chapter 334, Laws of 2003.

Rule is not necessitated by federal law, federal or state court decision.

Agency Comments or Recommendations, if any, as to Statutory Language, Implementation, Enforcement, and Fiscal Matters: Please see above for justification for the proposed rule update to WAC 332-22-200 through 332-22-230. For more information about the research into other western states and federal government rates for geothermal resources, please contact Kelsay Stanton, Kelsay.stanton@dnr.wa.gov.

The proposed updates only apply to geothermal resources leases on DNR-managed lands. The implementation and enforcement of these rules are through normal DNR leasing processes and will not affect other agencies or their processes because DNR is the only agency managing leases on DNR-managed properties. The proposed updates do not change any rules or regulations associated with geothermal well permitting and per existing permitting rules, there will be a SEPA environmental review with opportunity for public comment prior to any geothermal well drilling or development. Revenue resulting from the lease of DNR-managed trust lands for geothermal resources or exploration will revert to the trust beneficiary for that specific trust land involved in the lease. Trust beneficiaries for DNR-managed land include public schools and universities.

Name of Proponent: DNR, governmental.

Name of Agency Personnel Responsible for Drafting, Implementation, and Enforcement: Kelsay Stanton, Natural Resource Building, 360-790-8179.

A school district fiscal impact statement is not required under RCW 28A.305.135.

A cost-benefit analysis is required under RCW 34.05.328. A preliminary cost-benefit analysis may be obtained by contacting Kelsay Stanton, Mining and Minerals Program, Mailstop 47014, 1111 Washington Street, Olympia, WA 98504, phone 360-790-8179, fax 360-902-1789, email Kelsay.stanton@dnr.wa.gov.

Scope of exemption for rule proposal from Regulatory Fairness Act Requirements:

Is not exempt.

The proposed rule does not impose more-than-minor costs on businesses. Following is a summary of the agency's analysis showing how costs were calculated. The small business economic impact statement (SBEIS) calculator provides a method to determine the potential impact to small business by the rule change. If the rule will impose more-than-minor costs, then an SBEIS is required. The geothermal lease rate rule update will change annual rental rates and royalties to make DNR more competitive with western states and the federal government, with the aim to attract interest in geothermal resource leases with DNR. This should benefit small businesses within the geothermal resource industry and should not affect small businesses outside of the geothermal resource industry. The rule update does not impose additional fees to what already existed and makes the lease rates more competitive with other western states. The calculator indicated that a full SBEIS is not required for this rule update.

A copy of the detailed cost calculations may be obtained by contacting Kelsay Stanton, Mining and Minerals Program, 1111 Washington Street, Olympia, WA 98504, phone 360-790-8179, fax 360-902-1789, email Kelsay.stanton@dnr.wa.gov.

November 26, 2024

Michael Kearney

Product Sales and Leasing Division Manager

## OTS-5987.1

AMENDATORY SECTION (Amending WSR 92-06-003, filed 2/20/92, effective 3/22/92)

**WAC 332-22-200 Geothermal resources lease—Annual rental and obtaining required permits.** The annual rental shall be set by the board of natural resources, but for years one through five the annual rental shall be not less than (~~(\$1.25)~~) \$1.00 per acre or \$250 whichever is greater, and for years six through (~~(ten)~~) 10, shall be not less than (~~(\$2.50)~~) \$2.00 per acre or \$500 whichever is greater. Production facilities, except for transmission infrastructure, shall be a separate lease, subject to commercial lease procedures. Lessee shall obtain all necessary permits for exploration or development purposes.

AMENDATORY SECTION (Amending WSR 92-06-003, filed 2/20/92, effective 3/22/92)

### **WAC 332-22-210 Geothermal resources lease—Production royalty.**

(1) Production royalty payments on geothermal resources leases shall be payable to the department for geothermal resources produced from the lease premises. The schedule of production royalty payments and method of calculating fair market value at either the well or point of shipment shall be detailed in the lease and plan of development: Provided, That production royalty rates shall be (~~(not less than)~~) based on negotiation to ensure trust beneficiaries receive fair market value and shall be the cumulative amount of(~~(r))~~):

(a) (~~(Ten)~~) No less than two percent and no more than 20 percent of the gross proceeds received from the sale of such geothermal resources which are derived, generated or manufactured from the premises sufficient for commercial sales, including electricity; and

(b) (~~(Ten)~~) No less than two percent and no more than 20 percent of the fair market value thereof of products utilized but not sold(~~(r))~~; and

(c) (~~(Ten)~~) Five percent of the gross proceeds for all by-products derived from the leasehold estate.

(2) The department reserves the right to assign different production royalty rates for different geothermal resources produced from the lease premises, such as electricity, heat, steam, and other products as defined by state law as geothermal resources. The department reserves the right to reassess the production royalty rate at year (~~(twenty)~~) 20 of the lease and every (~~(ten)~~) 10 years thereafter, and

adjust the rate to the then fair market value, however in no case shall the adjusted production royalty be less than the ~~((10 percent))~~ lowest rate specified in this section.

(3) Lessee shall have the right to commingle, for the purpose of utilizing, selling or processing the products produced from the leasehold estate with products produced from other land, provided that the lessee shall efficiently meter or gauge the production from the leasehold estate in a manner approved by the state, in order to compute royalty payable on the products or by-products produced from the leasehold estate. The lessee shall furnish a sworn statement showing production for accounting periods required by the department and pay any royalties due.

AMENDATORY SECTION (Amending WSR 92-06-003, filed 2/20/92, effective 3/22/92)

**WAC 332-22-220 Geothermal resources lease—Minimum annual royalty.** At the beginning of lease year ~~((eleven))~~ 11, or at the beginning of the year in which production starts, whichever occurs first, a minimum annual royalty of not less than ~~((ten))~~ two dollars per acre per year, or \$2,000, whichever is greater, shall be paid to the department, and shall replace the annual rental. Minimum annual royalty calculation shall be based off total leased acreage. Minimum annual royalty payments shall be credited against production royalties for that year. Minimum royalties paid during the term of the lease are nonrefundable and nontransferable.

The department reserves the right to reassess the minimum annual royalty rate at year ~~((twenty))~~ 20 of the lease and every ~~((ten))~~ 10 years thereafter, and adjust the rate to the then fair market value, however in no case shall the adjusted minimum annual royalty be less than the ~~((ten))~~ two dollars per acre, or \$2,000 specified in this section.

AMENDATORY SECTION (Amending WSR 92-06-003, filed 2/20/92, effective 3/22/92)

**WAC 332-22-230 Geothermal resources lease—Unit plans.** (1) The holder(s) of any geothermal resources lease may apply to the department to consolidate their leaseholding for geothermal resources with other entities, including lands not owned by the state, to collectively adopt and operate as a unit under a unit plan. Such consolidation will not serve to extend the term of the lease and all participants must agree to continue payment of royalties provided in the lease through the life of the unit and any extensions of the plan.

(2) When separate geothermal resource rights under lease cannot be developed and operated independently in accordance with an approved well-spacing or well-development program, the commissioner or the commissioner's delegate may require lessees to enter into a unit plan or drilling agreement with other entities when it is in the best interest of the state.

(3) As a condition for authorization to be part of a unit plan, the commissioner or the commissioner's delegate may alter the terms

and conditions of the lease(s) so involved when it is in the best interest of the state to do so, and such authorization may be further conditioned upon, but not limited to the following:

(a) Department access to reports and documents it deems necessary, at the sole discretion of the department, to determine if consolidation of the proposed unit plan is in the best interest of the state.

(b) Leaseholds which are only partially included in the unit shall be segregated into separate leases as to the lands committed and not committed as of the effective date of the unitization. The annual rental or minimum annual royalty shall be paid on the leased acreage in the unit independently from other segregated lease areas.

(c) Any apportionment of production or royalties among the separate tracts of land comprising the unit shall include an accounting system, and the department shall have the right to audit such system to protect the interests of the state.

(d) None of the rights of the state as landholder shall be limited or subordinated.

(4) If an application for consolidation includes plans for adding production facilities to state lands, except for transmission infrastructure, that acreage shall require a commercial lease and shall be removed from the original lease for geothermal resources.