

The Texas Lawbook

Mapping the Regulatory Landscape for CCUS in Texas

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2021 marked the beginning of rapid increases in carbon capture, utilization and sequestration (CCUS) activity, with more than 100 new facilities being announced. CCUS saw a record high of \$6.4 billion in global investment in 2022.

Progress has continued in 2023. 166 million tons per annum of potential storage capacity is expected to enter development within the year, and many stakeholders are predicting another record-setting year of investment growth. Significant M&A activity has also occurred this year. In August, Occidental Petroleum announced that it agreed to pay \$1.1 billion dollars to purchase Carbon Engineering Ltd., with whom it had been working on numerous CCUS projects. In July 2023, Exxon announced that it had purchased Denbury Resources in an all-stock deal valued at \$4.9 billion, citing Denbury's CO₂ infrastructure.

The Inflation Reduction Act and other recent incentives have coupled with public support and focus on ESG to spur this recent investment. CCUS is a key tool in combatting climate change, with significant growth in CCUS being required to reach net zero emissions, and Texas is a potential CCUS hotspot. However, regulatory action in Texas will be required for CCUS to meet its full potential.

Texas boasts particularly high CCUS capability — with expansive formations suitable for storage, many nearby emitters of CO₂ and existing energy expertise. Texas has seen increasing CCUS activity, including high-profile deals such as Equinor's acquisition of a 25 percent interest in Bayou Bend CCS LLC, a joint venture involving Chevron and Talos that is focused on CCUS along the Texas Gulf Coast. Despite these positive signals, a lack of regulatory certainty in Texas could hold back the full extent of at-the-ready investment dollars.

First, the fundamental question of who owns the pore space in which CO₂ is injected remains technically unanswered in Texas. While case law has suggested that, in at least some cases, the pore space would belong to the surface estate (the majority rule in the U.S.), a court has yet to make a definitive, broad ruling on the issue. A petition for review of *Myers-Woodward v. Underground Services Markham, LLC*, involving cavern space created via salt mining, is pending before the Supreme Court of Texas, which has

the potential of providing more definitive guidance. The Texas Legislature attempted to answer this question through a bill proposed in the most recent legislative session, which provided for ownership by the surface owner.

The draft legislation would have provided a relatively robust CCUS regulatory regime, including by providing a mechanism for liability to be transferred to the state and providing a unitization process similar to what exists for traditional oil and gas. States with similar statutes to this draft legislation, including Wyoming and Montana, are seeing heightened interest in CCUS. Regulatory uncertainty is seen as a barrier to the energy transition generally, making the passage of a comprehensive CCUS statute in Texas a critical path item.

In addition, a key piece of the regulatory landscape is the Class VI permitting process. Class VI permits are required for the injection of CO₂ and are administered by the Environmental Protection Agency. The Class VI permitting process is demanding, and processing times with the EPA have been staggering. States can gain primary enforcement control over the Class VI process (referred to as “primacy”). Primacy can allow for permits to be granted in months as opposed to the EPA’s multiyear processing times. Some CCUS developers have specifically cited primacy as the reason for pursuing projects in Wyoming and North Dakota, the only two states with primacy (although Louisiana is expected to gain it soon). Texas is currently pursuing Class VI primacy, and recently enacted amendments to further align Texas Railroad Commission regulations with federal requirements. Gaining primacy will also be key to unlocking the full potential for CCUS in Texas.

A number of structural deal trends have emerged in CCUS projects as the regulatory regime develops and projects increase in number. There is typically an agreement between the emitter and the capturer and an agreement between the capturer and the user or storer. These agreements are generally modeled after constructs seen in the natural gas space. Pore space leases may be entered into as well, which are structured similarly to oil and gas leases with a bonus, a primary term (allowing for the lengthy permitting process) and royalties based on the amount of CO₂ injected. Other agreements include easements, surface use agreements and transportation agreements. As regulatory certainty grows, more established deal structures are also expected.

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