

FINANCIAL ASSURANCES AND WELL PLUGGING

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Oil and gas operators pay for plugging orphaned wells, taxpayers are not on the hook

Texas has maintained a well plugging fund (Oil Field Cleanup Fund) since 1965. In 1983 the fund was modified to be supported primarily from permit fees and other industry fees and taxes.

In 2011, the Texas Legislature authorized the Railroad Commission to replace the Oil Field Cleanup Fund with the Oil and Gas Regulation and Cleanup Fund, which expanded the use of funds to cover expenditures other than well plugging within the Commission's Oil and Gas Division.

Currently, well plugging and site reclamation is funded through the Oil and Gas Regulation Cleanup Fund, which continues to be predominantly funded from industry fees and industry related taxes.

Bonding was always meant to be a portion of the revenue used to pay for plugging orphaned wells

Revenue from bonds was always meant to be a part of how well plugging costs are paid.

Bond revenue is one of over **20 sources** of revenue that contributes to the Oil and Gas Regulation and Cleanup Fund. Examples of these sources include: costs recovered from investigations, assessment and cleanup of oil and gas waste, proceeds from a fee imposed on crude petroleum produced, and revenue from applications for exceptions to commission rules in the RRC Oil and Gas Division. (A full list can be found in the Oil and Gas Primer)

Revenue from key accounts make up a large amount of funding for plugging costs

In 1991, the legislature established an oil-field regulatory fee assessed from oil and gas production taxes. According to the fiscal analysis for this legislation, the fee is to be deposited in the Oil-Field Cleanup Fund and is to be utilized "to plug abandoned wells and control or clean up oil and gas wastes and other substances regulated by the Railroad Commission." In fiscal year 2015, revenue generated from this fee amounted to **\$12,027,098**.

Financial securities/bonds converted by the RRC due to a result of rule violations in fiscal year 2015 equaled **\$3,675,808**.

The revenue collected from the oil-field regulatory fee in addition to the bonds collected by the RRC in fiscal year 2015 was **\$15,702,906**.

According to RRC numbers in FY 2015, the Commission spent **\$11,772,895** on well plugging. The difference between what was collected (funds available) from the oil and gas production fees and bonds and what was spent amounts to **\$3,930,011**.

RRC has several key enforcements tools to address operators who abandon wells

Notice of Violation (NOV): The RRC sends a written NOV to the operator's that have violated a rule. The NOV requires a deadline for correction.

P-4 Cancellation (Severance Notice): If NOV issue is not corrected before deadline, a severance order is issued which prohibits the operator from producing, selling, or otherwise using their wells.

P-5 (Organization Report): An operator's Organization Report (P-5) must be active and maintained annually to perform ANY activities under the jurisdiction of the Railroad Commission.

SB 639 Flag: After an operator's P-5 becomes 30 days delinquent, a notice to sever the operator's highest producing lease is issued. If the P-5 becomes 60 days delinquent, a notice to sever all of the operator's leases is issued. This ultimately prevents non-compliant operators from doing business in the State of Texas for a period of seven (7) years from the date of the initial violation.

Referral to Attorney General: The RRC may refer violation orders to the Attorney General's office for enforcement and collection of administrative penalties.

If an oil and gas company goes bankrupt, their wells do NOT always remain orphaned

A common misconception about what happens when an operator goes bankrupt is that the operator abandons their wells and all these wells ultimately become and remain orphaned. This is not the case, oftentimes those wells are assets that other operators hope to secure.

For instance, Quicksilver Resources filed for bankruptcy in 2015 but many of their wells were purchased by a different operator with an active P-5 (Organization Report).

Further, according to RRC numbers, many operators with an out of date P-5 (which leads to orphaned wells) will renew their P-5 within one year. Currently, 30% of the RRC's orphaned wells have had an out of date P-5 for less than a year. These are likely to be remediated with an updated P-5 and will NOT remain orphaned.

The backlog of inactive wells and orphaned wells in Texas has decreased greatly since 2002

As of April 2016 there were 9,372 orphan wells in Texas. This is a reduction of 8,599 orphaned wells since 2002.

The percentage of total inactive wells in the state has also **decreased since 2002**. Previously, it was **31.41%**, as of April 2016 the percentage of total inactive wells was **25.80%**.

Plugging all of the orphaned wells in Texas does not happen in one year

The well plugging program was established to plug abandoned wells over time and according to need based off of the RRC's priority well plugging system. This system takes into account **26 human health, safety and environmental weighted factors** to rank wells for plugging. Since 1984, over 35,115 wells have been plugged at a cost of over \$251.1 million.

The RRC has the revenue to plug all wells that are potentially an environmental risk

The Railroad Commission has always had the revenue available to plug their highest priority wells. The RRC plugs an average of 800 wells annually.

Most wells are plugged by operators

According to the Railroad Commission, in fiscal year 2015, 92%, 7,763, of the wells plugged were plugged by the operators without the use of funds appropriated to the Commission.

The costs associated with increasing the bonding tiers does NOT justify the benefit

The Sunset Commission report recommends adding additional bonding tiers and increasing the bonding amounts for a few of the existing tiers. Calculating the current and proposed amounts of financial assurances, if the proposed changes were implemented, it would require operators to secure an additional **\$106 million in bonds**. According to the Sunset Commission Report this would only increase revenue for plugging at the RRC by **\$1.3 million annually**.

Requiring operators to secure an additional \$106 million in financial assurances for \$1.3 million in revenue is bad public policy that will have substantial repercussions for small to mid-size operators.