Presentation to House Resources

Monday, March 5, 2018

1. General update on drilling activity.
2. <u>Protecting the state from P&A Liability</u>

This is from a publication called "RISKS OF ACQUIRING AGING OILFIELDS" published by the Rocky Mountain Mineral Law Foundation

"As sure as death is the great certainty of life, so too is plugging the great certainty of petroleum development: every well will--at some future point unknown--cease to produce in paying quantities and require plugging. In transactions involving aging oilfield properties, both the seller and the purchaser must understand and appreciate their respective risk of plugging liability."

What is the scope of the issue? There are about 5200 wells in Alaska, meaning individual wellheads. Most are oil producers, some are injectors, either of water, gas, or a substance called miscible injectant, which is natural gas liquids at high pressure. A few are disposal wells.

While 5000 plus is a big number, keep in mind that Louisiana has over 200,000 wells, and Texas has over 500,000.

AOGCC holds bonds for the purpose of making sure the operator of a lease plugs and abandons their wells. We have begun the process of updating our bonding practices. We brought this issue to your attention last year.

We pointed out then that our regulations say that the bond for a single well "must not be less than $100,000" and "not less than $200,000 for a blanket bond covering all of the operator's wells in the state"

In practice, the agency has historically required no more than those amounts.

Many people are surprised to learn that all of BP's wells on the North Slope, of which there are about 1900, are covered by a $200,000 bond. Same is true of ConocoPhillips.

The headline about those hearings last year said, "'Paltry' bonding for oil operators puts Alaska at risk." That pretty well sums it up.

Over the summer the agency held a workshop to discuss the issue with industry and solicited their input directly and through written submissions. As we mentioned last year, we do not believe we need any additional statutory authority to take action; and comments we received from AOGA and ConocoPhillips (not a member of AOGA) after the workshop took the same position.

(We are not the only holders of bonds – Dept of Natural Resources also holds bonds for Dismantlement, Removal and Rehabilitation, or 'DR&R'—monies that are held to remove surface improvements like pipelines, facilities, tanks, and so forth)

The commission has not arrived at a cookbook answer for this bonding effort. Earlier this year in 2018 we sent a letter to every operator of record in the state, requiring them to give us their estimates of what it will cost to properly P&A their wells and how they arrived at that number. Those reports are due this Wednesday.

Also informing our effort is the recent bankruptcy of a company called Aurora Gas, which was a small operator of nineteen gas wells, all located on the west side of Cook Inlet. While Alaska has seen oil companies go through bankruptcy in the past, this one was different in that no one stepped forward to buy all of Aurora Gas' assets. Indeed, of the nineteen wells that Aurora Gas was the operator for, only the six best producing wells were acquired by a new company, called Aurora Exploration. (Despite the seeming overlap in identity implied by the two names, these are distinct legal entities)

The 13 remaining are not 'orphans' in the strict oil field sense of the word, because an orphan well is one for which no responsible financial party can be identified. Our regulations take the position that, in the absence of the operator, the responsibility for P&Aing wells falls on the landowner.

In the case of these thirteen wells, ten are on land belonging to CIRI, and three are on land that belongs to the state. For AOGCC purposes, that means the obligation to P&A the ten CIRI wells falls on CIRI and the obligation for the other three wells is going to fall on the Dept. of Natural Resources, who will likely look to you legislators for an appropriation when the time comes.

What will this cost? We held a hearing this fall in order to get a better handle on what it costs to P&A a well.

There is no simple answer. Is the well on the North Slope or Cook Inlet? Reachable by the road system or not? Onshore or offshore? We dealt with a company this summer that had a total of two wells in their portfolio, both of which needed to be P&A'd – one on the north part of the Kenai Peninsula, but not reachable by road, and the other on the west side of Cook Inlet, near the mouth of the Kustutan River.

Keep in mind that, for bonding purposes, the question is not, what will it cost the Oil Company Operator, to P&A the well. Bonds are in place for when the operator does not perform as promised. Bonds are in place to help pay for the cost if there has been a default and the cost falls on us, the state.

Our best estimate for P&Aing the wells on the west side of Cook Inlet, off the road system, is around $600,000 per well.

All this brings me to the impetus behind this hearing. As we have been working with this issue, it has come to our attention that in at least two states, California and Kansas, the regulating authority there is armed with statutes that allow it to pursue former operators for P&A costs in the event that a current operator is financially unable to do so.

The statutes do not get much use. They are there as a form of backstop. One high-profile case involved an oil platform off Santa Barbara, in California. The current operator went bankrupt, potentially leaving the state of California on the hook for millions of dollars of costs. Their 'prior operator' law allowed them to enter into negotiations with Exxon, who had operated the platform when the law went into effect. The state reached a settlement with Exxon.

The language of such a law is fairly simple:

California:

(c)(1) The current operator, as determined by the records of the supervisor, of a deserted well that produced oil, gas, or other hydrocarbons or was used for injection is responsible for the proper plugging and abandonment of the well or the decommissioning of deserted production facilities. If the supervisor determines that the current operator does not have the financial resources to fully cover the cost of plugging and abandoning the well or the decommissioning of deserted production facilities, the immediately preceding operator shall be responsible for the cost of plugging and abandoning the well or the decommissioning of deserted production facilities.

(2) The supervisor may continue to look seriatim to previous operators until an operator is found that the supervisor determines has the financial resources to cover the cost of plugging and abandoning the well or decommissioning deserted production facilities. However, the supervisor may not hold an operator responsible that made a valid transfer of ownership of the well prior to January 1, 1996.

Kansas: [FN96]. Kan. Stat. Ann § 55-179 (2014).

"For the purposes of this section, a person who is legally responsible for the proper care and control of an abandoned well shall include, but is not limited to, one or more of the following: [1] Any operator of a waterflood or other pressure maintenance program deemed to be causing pollution or loss of usable water; [2] the current or last operator of the lease upon which such well is located, irrespective of whether such operator plugged or abandoned such well; [3] the original operator who plugged or abandoned such well; and [4] any person who without authorization tampers with or removes surface equipment or downhole equipment from an abandoned well."