

SUBJECT: Amending financial security requirements for oil and gas well operators

COMMITTEE: Energy Resources — committee substitute recommended

VOTE: 5 ayes — West, Farabee, Canales, Crabb, B. Keffer

1 nay — E. Jones

1 absent — Delisi

WITNESSES: For — Commissioners Victor Carrillo and Charles Mathews, Texas Railroad Commission; Robert A. Craighead; Alan B. Cutcher; Martin Fleming, Texas Independent Producers and Royalty Owners Association; Ross H. Hardwick; Roy Pitcock and Bill Stevens, Texas Alliance of Energy Producers; Rex H. White; *(Registered, but did not testify:)* Tommy Levisy; Eddie Lord, Eddie's Royalties, Inc.

Against — Chairman Michael Williams, Texas Railroad Commission; Douglas Beveridge, Texas Land and Mineral Owners Association; *(Registered, but did not testify:)* Ken Hodges, Texas Farm Bureau; Ed Small, Texas and Southwestern Cattle Raisers

On — Joe Mayorga, Texas Railroad Commission; Joseph Dale Robertson, Texans for Energy Independence; Ben Sebree, Texas Oil and Gas Association; Vicki Wolski; *(Registered, but did not testify:)* Debbie LaHood and Timothy A. Poe, Texas Railroad Commission

BACKGROUND: Natural Resources Code, sec. 91.103 requires a person, firm, corporation, or other organization performing operations regulated by the Texas Railroad Commission (RRC) to execute and file with the RRC a bond or alternate form of financial security. This financial security is required to prove the ability to cover cleanup expenses in the event of an environmental problem. Effective September 1, 2004, a person may choose to file:

- an individual bond for each well equal to \$2 for each foot of well depth for each well;
- a blanket bond to cover all wells;

- a letter of credit or cash deposit equal to the amount required for an individual or blanket bond;
- a nonrefundable annual fee of \$1,000, if bonds are not available at reasonable prices and if the person can demonstrate compliance with pollution-control rules; or
- a nonrefundable annual fee of 12.5 percent of the bond that otherwise would have been required.

A person who chooses to file a blanket bond must file a \$25,000 bond if the person operates 10 or fewer wells; a \$50,000 bond if the person operates more than 10 but fewer than 100 wells; and a \$250,000 bond if the person operates 100 or more wells. The commission must set the amount of a bond required for an operator of bay or offshore wells at a reasonable amount that exceeds the bonds required for other categories.

DIGEST:

CSHB 2020 would amend bonding and financial security requirements for oil and gas well operators. A person who had complied with pollution-control rules could file a nonrefundable \$1,000 fee without a determination by the commission that bonds were not available at reasonable prices. Instead of a nonrefundable annual fee equal to 12.5 percent of the bond otherwise required, the operator could file a fee equal to the amount of the bond that otherwise would be required, multiplied by 12 percent or by the sum of 4 percent plus the prime interest rate prevailing late in the year before the year in which the fee was due, whichever was less. The RRC would have to determine the prime interest rate for purposes of this calculation.

Effective January 1, 2006, the nonrefundable annual fee of \$1,000 available to a person who demonstrated compliance with pollution-control rules would be replaced with a fee equal to the amount of the bond that otherwise would have been required, multiplied by 10 percent or by 1 percent plus the prime interest rate prevailing late in the year before the year in which the fee was due, whichever was less.

The commission could not require a person to file a bond, letter of credit, or cash deposit as a condition of receiving an extension of time to plug a well.

Blanket bonds. Effective January 1, 2004, the bill would create six levels of blanket bond requirements for well operators to replace the current three:

- \$15,000 for a person who operates 10 or fewer wells;
- \$35,000 for between 11 and 24 wells;
- \$50,000 for between 25 and 99 wells;
- \$100,000 for between 100 and 149 wells;
- \$175,000 for between 150 and 199 wells; and
- \$250,000 for 200 or more wells.

The commission could require a person who operates 200 or more wells to file an additional, supplemental bond if the RRC deemed such a requirement appropriate. To require a supplemental bond, the ratio of this person's inactive to active wells would have to be higher than 0.75. The amount of this supplemental bond would be equal to the amount of the bond for an owner of 200 or more wells or of offshore wells, multiplied by an inactive well ratio factor defined as either:

- one, if the ratio of inactive to active wells was not more than 0.9, or
- two, if the ratio of inactive to active wells was more than 0.9.

The RRC also could require a supplemental bond that would be equal to the sum of the bond computed with the inactive ratio factor and the amount computed by multiplying the amount of the bond required for owners of 200 or more wells or of offshore wells by the sum of a low production factor, a compliance factor, and an inactive well factor as defined by the bill.

CSHB 2020 would repeal sections of SB 310, the RRC sunset bill enacted by the 77th Legislature in 2001, to conform with the bill's changes.

The bill would take effect September 1, 2003.

**SUPPORTERS
SAY:**

CSHB 2020 would clean up last session's RRC sunset bill and would protect small business people in the Texas oil industry who cannot afford to post costly bonds to insure their wells. For many small producers, bonds in the current market are not available at a reasonable price. Since September 11, 2001, insurance bonds have become even more expensive and are out of the price range of many small producers. CSHB 2020 would allow a compliant producer to file a lower annual fee, making oil production more affordable for small business people in the state.

CSHB 2020 would allow a person with a strong record of pollution-control compliance to pay a reasonable annual fee when that person could not afford to file bonds for wells. In 2001, the 77th Legislature established a “good guy” provision to allow environmentally responsible small producers to pay a nonrefundable \$1,000 fee when bonds are unaffordable. However, bureaucratic obstacles have prevented more than a handful of applicants from filing this fee. CSHB 2020 would allow these responsible operators to be approved for the “good guy” fee administratively and to continue producing oil and paying severance taxes that benefit the entire state.

CSHB 2020 would generate additional revenue for the oilfield cleanup fund, a successful program that has plugged thousands of hazardous abandoned wells across the state. According to the bill’s fiscal note, the bill would generate more than \$23 million in revenue for the fund through fiscal 2008. The funds would be spent to preserve the environment and ensure the public safety of Texas citizens.

CSHB 2020 would subdivide blanket bonding categories to correspond more closely to an operator’s size and risk to capital. Under current law, a person who operates 100 wells must file the same \$250,000 bond as a person who operates five or ten times that many wells, an unreasonable requirement that does not differentiate adequately among well operators based on size.

CSHB 2020 properly would require higher bonds from large operators with numerous inactive wells, a low level of production, or a poor history of pollution-control compliance. This requirement would reflect the risk that these operators represent and would discourage unwarranted practices by Texas oil producers.

**OPPONENTS
SAY:**

CSHB 2020 would allow an operator to make a small payment to the RRC in lieu of a bond, undermining the financial security requirement designed to protect Texas taxpayers and responsible operators from having to cover the cost of plugging abandoned wells. In 2001, the 77th Legislature recognized the epidemic of abandoned wells across the state and required operators to post bonds or letters of credit to cover the potential cost of plugging wells in the future. The payment authorized under CSHB 2020 could be less than \$1,000 and would not even cover one-quarter of the cost of plugging a well.

CSHB 2020 would undermine the bonding requirement, an important method of preventing harm from abandoned wells. Although the oilfield cleanup fund serves an important function in addressing the problem of abandoned wells, the bonding requirement also was an important step toward bringing the problem under control. While the RRC must consider the production capacity of Texas oil producers, the commission also must protect citizens affected by pollution from abandoned wells. By loosening the bonding requirement, CSHB 2020 would weaken the RRC's ability to prevent pollution by Texas operators.

NOTES:

As filed, HB 2020 would have required an alternate form of financial security for a person who involved in activities other operating wells. This bond would have been equal to either \$250,000 or a lesser amount if the person could show that the risk associated with an operation warranted a lesser amount.

The companion bill, SB 1408 by Duncan, has been referred to the Senate Natural Resources Committee.