IPANM
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Independent Petroleum Association of New Mexico

IPANM Tiers and Implementation Recommendation
Financial Assurance Bonding for Oil & Gas Wells
March 13, 2018
Updated April 30, 2018

Background Information

Based on discussions with the administration, IPANM is working under the assumption that the New Mexico Oil Conservation Division (OCD) will file for the Financial Assurance Rulemaking Hearing at some point during the week of Mar. 11 to 14, 2018, in order to meet filing requirements to get the hearing on the May 2018 Oil Conservation Commission (OCC) agenda.

IPANM Recommendation

Since the passage and signing of SB 189, the IPANM Executive Board has conducted some analysis regarding well counts with members. IPANM has also looked at existing tiers in surrounding states. For reasons to be discussed below, the IPANM Board of Directors is unanimously recommending a five-tier structure (below) for Financial Assurance Bonding in New Mexico, specifically developed to reduce the burden of this new rule to small, independent operators.

IPANM Proposal		
Well Count	**Amount**	**Implementation Timing**
1-10 Wells	**$25,000**	**Immediately**
11-99 Wells	**$50,000**	**Immediately**
100-149 Wells	**$100,000**	**18 Months**
149-199 Wells	**$200,000**	**12 Months**
200+ Wells	**$250,000**	**12 Months**

Discussion Points

- Arguments from the administration and supporters of SB 189 commonly pointed to the State of Texas tier well levels and bonding amounts as a model for a future State of New Mexico Financial Assurance Rule. In fact, state legislators who cast key votes in support of SB 189 tell IPANM that the "Texas Rule" alone was a deciding factor in swaying their vote in favor of the bill.

- The State of Texas uses the following tier system for determining financial assurance bond levels for operators:

Texas Financial Assurance Bonds

Well Count	Amount
0-10 Wells	**$25,000**
11-99 Wells	**$50,000**
100+ Wells	**$250,000**

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- IPANM ran an analysis of existing state operators and used direct input from members to develop the proposed tier levels and bonding.

- IPANM started with a baseline of the “Texas Rule” in the development of the proposed New Mexico two lower tiers. The well count levels and bonding amounts in these tiers offer both reasonable and responsible bonding levels for smaller operators. In other words, IPANM’s proposed lower tiers will allow our start-up and small operators to remain financially solvent while also providing adequate state protection for abandoned wells.

- For the higher tiers, IPANM has determined operators with well counts above 100 need to be further differentiated to create a rule that considers and adapts to New Mexico’s unique environment and size. For example:
  - The environment surrounding Texas’ many different producing basins greatly vary and differ from New Mexico’s Permian and San Juan Basins. Texas has many more groundwater sources, aquifers, rivers, streams, lakes and coastlines the state needs to consider along with a much greater population. By contrast, New Mexico has more isolated producing basins and considerably fewer water sources.
  - Texas and New Mexico have significant differences in the number of operators and the number of wells:
    - New Mexico currently has approximately 450 oil and gas operators. Texas currently has approximately **ten times** the amount of oil and gas operators with 6,600. (www.drillinginfo.com)
    - New Mexico has approximately 63,000 wells (NMOCD online statistics). Texas is responsible for **4.5 times** the number of wells, with over 291,000 according to the Texas RR Commission website.
  - CONCLUSION: IPANM believes the Texas highest tier level and bonding was developed to provide the regulator the ability to process much higher volumes of wells. However, New Mexico needs to create more flexible higher-end bonding tiers that recognize the state’s much smaller number of midsize operators.

Attachments

Appendix A: Specific Tier Recommendation Narratives
Appendix B: Further Considerations
Appendix C: State Comparisons on Financial Assurance Levels

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Appendix A: Specific Tier Recommendation Narratives

1-10 Wells at $25,000: To encourage future development of oil & gas wells in the State of New Mexico, IPANM strongly believes there needs to be a reasonable cost of entry for a prospective independent producer to gain a foothold in the current market. It is significantly important that there be reasonable financial opportunity for a newer company to grow during its initial years of operation. It is clear that the State of Texas has come to this same conclusion thereby setting its lowest tier well count level from one to ten wells. Likewise, a bonding amount of $25,000 offers adequate state protection to plug a well that may be abandoned by a start-up operator for some unforeseen reason. IPANM members are passionate in their conviction that this lowest tier level be up to ten wells. Many more-established IPANM members credit growth in the earlier years by not having to tie-up significant amounts of up-front capital that could more productively be used on operational costs vital to their survival.

11-99 Wells at $50,000: This category represents a very high-percentage of IPANM's members. Our analysis and discussion saw an immediate and critical need for this group to remain a single tier. Foremost, similar to the one-to-ten tier, keeping the 11-to-99 tier at the same $50,000 bonding level matches the lower bonding levels in the State of Texas.

Second, IPANM members have voiced concern that well counts alone are not necessarily the best benchmark for financial assurance bonding. There are small operators who have a lot of marginal, low-producing wells compared to similarly-sized operators who have fewer wells with better production. By keeping this tier in the wide range as we have proposed, IPANM feels the playing field is leveled to account for this discrepancy.

Finally, it's important to keep this group as a single tier due to the comparable competitive advantage Texas and majors have in the Permian Basin. Not only are New Mexico independents facing higher acreage costs to get in on the Permian oil play, they continue to look across the border and see more advantages to doing business in Texas. New Mexico independents need to stay in the New Mexico side of the Permian. Likewise, these independents cannot afford to have cash tied up in bonding as they compete with a growing number of majors buying up wells and leases at high prices in the Delaware Basin. In the Northwest, increasing bonding levels in this category would have serious financial consequences for our Northwest gas operators who operate many, many marginal wells in the San Juan Basin.

100-149 Wells at $100,000: IPANM believes that the 100 well count is a significant milestone that separates moderately-sized operators from one another. Placing a higher financial assurance bond above $100,000 in this category will do little to actually ensure more abandoned well plugging, as more established operators at this level do not pose as much of a threat to walk away from an abandoned well. However, the $100,000 increase does *double* the existing bonding currently in place for this group of operators. IPANM feels this is a fair way of incrementally increasing bonding costs without unduly punishing the successful, responsible operators who fall into this group. As for timing implementation, IPANM is asking for 18-months before the rule kicks in for this group. IPANM wants to give operators time to plan how to proceed with the new, higher financial assurance requirements. Likewise, IPANM

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recognizes the state does not have time or staff necessary to implement new bonding levels on so many different operators in such a short period of time. This implementation timeline seems the most pragmatic approach for both industry and the Oil Conservation Division.

150-199 Wells at $200,000: Last year, the administration proposed moving the financial assurance bonding a maximum $200,000 level. This year, the proposed maximum rose to $250,000 for the highest tier. During the 2018 Legislative Session, state legislators told IPANM that $200,000 was the most reasonable amount for independents in the highest tier. However, these same legislators told IPANM they decided to supported the $250,000 as written so as to not derail the bill from getting to the Governor. While IPANM is not happy with this change, we can understand the realities of trying to get a bill passed in a 30-day session. However, we still feel strongly that a $200,000 is much more reasonable.

Therefore, IPANM strongly feels that keeping this level of $200,000 for 150 to 199 wells protects our midsize operators.
Recognizing that this is a large monetary bonding increase, the timing for implementing this tier should be set to 12-months.

200+ Wells at $250,000: This category is an acknowledgement by our large independent operators that they do have the financial resources to cover the 5-fold increase in bonding, but they request a 12-month implementation due to most bonds being written on an annual basis.

Appendix B: Further Considerations

Defining an Abandoned Well

The purpose of Financial Assurance Bonding is to allow the state regulating body, the New Mexico Oil Conservation Division (OCD), some monetary bond to be held in assurance that an abandoned oil or gas well be plugged if and when that well is no longer productive.

In New Mexico, a non-producing well is considered abandoned after 15 consecutive months of non-use by an operator. Many IPANM operators have long asserted that a well's usefulness and ability to be used for future production should extend beyond 15-months abandonment designation due to the potential to extract the same or different product, at a future time due to anticipated technological extraction improvements and/or new market demand. Therefore, the required plugging of a well after 15-months creates both an unnecessary cost burden to a small operator, and also represents a lost revenue opportunity on a well that could be stimulated at a later date, possibly for a different extractive purpose.

While these arguments will have to be made at a different time and day in the future, IPANM feels the need to remind the administration that there are these fundamental differences our association holds in respect to abandoned wells overall.

Defining Well Counts

The IPANM Board of Directors believes the well count used by the Oil Conservation Division, for the sake of financial assurance, should only cover wells that an operator owns on state or private land. The federal government already applies a system of taxes, fees and bonds for wells on federal land. To count a well on federal land for part of the assurance to plug a well on state or private land does not seem jurisdictionally appropriate.

Equally important, IPANM seeks clarify that wells covered by single plugging bonds with the state are not included in calculating the total number of operated wells. For example, an operator that has six wells either in temporarily abandoned status or plugged, but not released, are already covered by single well plugging bonds as required by the state. Including such already bonded wells in the overall well count could adversely put them into a higher well count tier.

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Appendix C: State Comparisons on Financial Assurance Levels

Texas Financial Assurance Bonds

Well Count	Amount
0-10 Wells	$25,000
11-99 Wells	$50,000
100+ Wells	$250,000

California Financial Assurance Bonds

Well Count	Amount
Single Well (less than 10,000 feet)	$25,000
Single Well (over 10,000 feet)	$40,000
20 to 49 Wells	$200,000
50+ Wells	$400,000

Colorado Financial Assurance Bonds

Well Count	Amount
Single Well (less than 3,000 feet)	$10,000
Single Well (over 3,000 feet)	$20,000
1-100 Wells	$60,000
100+ Wells	$100,000

Idaho Financial Assurance Bonds

Well Count	Amount
1-10 Wells	$50,000
11-30 Wells	$100,000
30+ Wells	$150,000

North Dakota Financial Assurance Bonds

Well Count	Amount
2+ Wells	$100,000

Alaska Financial Assurance Bonds

Well Count	Amount
Single Wells	$100,000
Blanket Bond for 2+ Wells	$200,000

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Utah Financial Assurance Bonds

Well Count	Amount
2+ Wells	$120,000

Oklahoma Financial Assurance Bonds

Well Count	Amount
2+ Wells	$25,000

Wyoming Financial Assurance Bonds

Well Count	Amount
2+ Wells	$100,000

Louisiana Financial Assurance Bonds

Well Count	Amount
1-10 Wells	$50,000
11-99 Wells	$250,000
100+ Wells	$500,000

Arizona Financial Assurance Bonds

Well Count	Amount
General Bond	$25,000
Single Wells (1-5)	+$3,000/Well
6+ Wells	+$15,000 Total

South Dakota Financial Assurance Bonds

Well Count	Amount
Single Well (less than 5,500 feet)	$30,000
Single Well (over 5,500 feet)	$100,000

Source: http://iogcc.ok.gov/Websites/iogcc/images/Financial_Assurances_FINAL_web.pdf