

LEGISLATIVE BUDGET BOARD
Austin, Texas

FISCAL NOTE, 81ST LEGISLATIVE REGULAR SESSION

May 13, 2009

TO: Honorable Kip Averitt, Chair, Senate Committee on Natural Resources

FROM: John S. O'Brien, Director, Legislative Budget Board

IN RE: HB2259 by Crossover (Relating to the plugging of certain inactive oil or gas wells.),
Committee Report 2nd House, As Amended

Estimated Two-year Net Impact to General Revenue Related Funds for HB2259, Committee Report 2nd House, As Amended: an impact of \$0 through the biennium ending August 31, 2011.

The bill would make no appropriation but could provide the legal basis for an appropriation of funds to implement the provisions of the bill.

General Revenue-Related Funds, Five-Year Impact:

| Fiscal Year | Probable Net Positive/(Negative) Impact to General Revenue Related Funds |
|-------------|--------------------------------------------------------------------------------|
| 2010 | \$0 |
| 2011 | \$0 |
| 2012 | \$0 |
| 2013 | \$0 |
| 2014 | \$0 |

All Funds, Five-Year Impact:

| Fiscal Year | Probable Savings/(Cost) from <i>Oil-field Cleanup Acct</i> 145 | Probable Revenue Gain/(Loss) from <i>Oil-field Cleanup Acct</i> 145 |
|-------------|----------------------------------------------------------------------|---------------------------------------------------------------------------|
| 2010 | (\$251,805) | \$0 |
| 2011 | (\$1,956,598) | \$1,540,160 |
| 2012 | (\$1,528,287) | \$1,540,160 |
| 2013 | (\$1,528,287) | \$1,540,160 |
| 2014 | (\$1,528,287) | \$1,540,160 |

| Fiscal Year | Change in Number of State Employees from FY 2009 |
|-------------|-----------------------------------------------------|
| 2010 | 0.0 |
| 2011 | 20.0 |
| 2012 | 20.0 |
| 2013 | 20.0 |
| 2014 | 20.0 |

Fiscal Analysis

The bill would require the Railroad Commission (RRC) to change existing standards and implement a new plugging extension permitting process for inactive oil and gas wells by establishing mandatory surface equipment removal requirements, and establishing seven options to obtain plugging exceptions.

The bill would add a new definitions for “cost calculation for plugging an inactive well” based on the average actual costs reported by the RRC for the preceding year, “inactive well” as the RRC's calculated cost for each foot of well depth plugged based on the average annual plugging costs for wells reported by the RRC for the preceding state fiscal year for the district in which the inactive well is located. The bill would define an "enhanced oil recovery project" as a RRC approved or certified enhanced recovery project. The bill would define "good faith claim as a factually-supported claim based on a recognized legal theory to a continuing possessory right in a mineral estate. The bill would define an "inactive well" as an unplugged well with no reported production, disposal, injection or other permitted activity for more than 12 months, and, “physical termination of electric lines to an inactive well” as disconnecting electrical service to an inactive well site without inferring with electric supply to adjacent production sites, including cathodic protection units.

The bill would require well operators to plug inactive wells on or before the date the operator is required to renew its organization report unless the operator obtains a plugging extension under new provisions of the bill. It would require operators that assume control of existing inactive wells to satisfy the requirements of the bill relating to surface equipment and seven new options for obtaining a plugging extension for wells within six months of RRC approval of the certificates of compliance transferring the wells. The bill directs the RRC to grant a plugging extension for an inactive well if the operator maintains a current organization report and if, on or before the operator's organization report would have to be renewed, the operator provides an application that includes: 1) an affirmation that it has complied with surface requirements including the termination of electrical service, emptying and purging of all pipes, tanks and vessels for inactive wells more than five years old, but less than ten years old, and removal of all surface equipment for inactive wells more than ten years old, subject to exceptions for safety and required maintenance; 2) a statement that the well and associated facilities are in compliance with all RRC rules and orders; 3) a statement that the operator has and, on request, will provide, evidence of a good faith claim to a continuing right to operate the well, and 4) satisfaction of one of seven optional requirements.

The optional requirements set forth in the bill would include: 1) documentation of plugging or otherwise bringing into compliance with RRC rules 10 percent of the inactive wells identified at the time of the operator’s last renewal of its organization report; 2) filing an abeyance of plugging report signed by a licensed engineer or geoscientist stating that the well has a reasonably certain expectation of economic value in excess of the cost calculation for plugging the well, a reasonable expectation of being restored to a beneficial use that will prevent waste of oil or gas resources if the well were otherwise plugged, and documentation demonstrating the basis for the well’s future utility; 3) a statement that the well is part of an enhanced oil recovery project; 4) if the operator of the well is not currently otherwise required by RRC rule or order to conduct a fluid level or hydraulic pressure test of the well, documentation that the well has passed a fluid level test or hydraulic pressure test conducted in accordance with RRC rules; 5) posting a supplemental bond, letter of credit, or cash deposit sufficient for each well in an amount at least equal to the cost calculation for plugging an inactive well for each well specified in the application; 6) documentation of the deposit with the RRC each time the operator files an application of an amount of escrow funds equal to at least 10 percent of the total cost calculation for plugging each well specified in the application; and, 7) for publicly traded companies, providing copies of the operator's federal documents related to asset retirement obligations, and naming the Commission as a “secured creditor” with respect to the funds.

The bill would establish requirements for Abeyance of Plugging Reports and provide that they remain valid for a maximum of five years, that they may cover multiple wells in the same field, that they are not transferable to a new operator, and that the operator pay an annual fee of \$100 for each well covered. The fee would be deposited in the General Revenue-Dedicated Oil Field Cleanup Fund No. 145.

The bill would provide that an inactive well is considered part of an enhanced oil recovery project if the well is located on a unit or lease or in a field is associated with such a project. It does not allow for the transfer of documentation related to enhanced oil recovery projects to new operators. The bill would provide that a successful fluid test is valid for one year from the date of the test, and a successful hydraulic pressure test is valid for up to five years. The bill would require an operator filing documentation of the results of a successful fluid level or hydraulic pressure test to pay an annual fee of \$50 for each well covered by the documentation. The bill would require an operator to notify the RRC three days before an inactive well is to be tested and states that an operator would not be authorized to conduct such a test without RRC approval. The bill would provide that supplemental financial assurance for inactive wells is in addition to any other financial assurance requirements and is not transferable to a new operator of an existing well. A new operator would be required to file supplemental financial assurance within six months after transfer of a well.

The bill would establish requirements for the written affirmation regarding surface requirements to be submitted by the operator with an application for all plugging extensions if the operator also does not own the surface estate. The affirmation would be required to state that the operator has terminated electrical service to the well's production site, and that for all wells that have been inactive more than ten years as of the date of the renewal of the organization report, the operator has removed all surface equipment, junk and trash associated with the old well. The bill would require the RRC to adopt rules providing for the phase-in of the duty to comply with the surface equipment removal requirements for wells that have been inactive for more than 10 years.

The bill would provide for a temporary extension of the deadline for plugging an inactive well or temporary exemption from the surface equipment removal and electrical service termination requirements if an operator is unable to comply because of safety concerns or required maintenance of the well site and the operator includes with the application a written affirmation of the facts regarding the safety concerns or maintenance. In addition, an operator could be eligible for an extension of the deadline for plugging a well even if the well has been inactive for at least 10 years as of the date of renewal of the organization report, but the operator has not removed all surface equipment, etc. or has transferred that material to or allowed it to accumulate on an active lease if the well is part of an enhanced oil recovery project, and the operator includes a statement in the written affirmation that the well is part of such a project.

The bill would specify that the Oil Field Cleanup Account No. 145 includes fees collected with the filing of an abeyance of plugging report and the fee collected with an application for an inactive well plugging extension for which the operator selects the fluid level/hydraulic pressure testing option proposed by the bill.

The bill would require operators to construct, operate, and maintain power lines serving well sites in accordance with the National Electrical Code.

Methodology

It is anticipated that RRC staff duties added by the bill would include review and processing of renewal forms, review of technical documentation, review of self-bonding options, review of evidence and preparation of complaints related to enforcement of the new requirements of the bill, providing notice to numerous parties, managing discovery, conducting the hearing, reviewing the record, analyzing the evidence, and preparing a proposal for a decision related to enforcement of the new requirements. Additionally, the duties of the hearings examiners would include conducting hearings related to the administrative denial of permit applications. Examiners would be required to review the record, analyze the evidence, and prepare a proposal for decision, related to the appeal of any administrative denial of an application for a plugging exception.

This estimate assumes 50 to 100 requests for plugging exceptions that would be denied by the RRC. Upon the administrative denial of a request for a plugging exception, it is anticipated that the majority of the applicants would request a hearing. RRC staff would be required to review records, analyze evidence, and prepare a proposal for decision related to the appeal of any administrative denial of an application for a plugging extension. This estimate also assumes that there would be 25 to 50 referrals of violations of RRC rules related to the new surface equipment removal requirements by the

Commission District Office to Austin for the institution of enforcement proceedings. This would require additional evidence review, the provision of notice to numerous parties, the management of discovery, preparation for enforcement hearings, and participation in the administrative hearing process until an order is entered and becomes final.

Because the bill would only apply to renewals of organization reports on or after September 1, 2010, most costs to the RRC would begin in fiscal year 2011. The agency expects that it would need \$251,805 in fiscal year 2010 for programming changes. Beginning in 2011, an additional 20.0 FTEs would be needed for the activities outlined above. This estimate assumes those costs would be paid out of the Oil Field Cleanup Account No. 145. Costs to the RRC would total \$1,956,598 in fiscal year 2011, and include one-time costs, then drop to around \$1.5 million in future years as shown in the table above.

The RRC estimates that an additional \$1,540,160 in revenue to the Oil Field Cleanup Account No. 145 per fiscal year beginning in fiscal year 2011. This estimate is based on the assumption that the \$50 hydraulic pressure test fee would apply to approximately 7,000 wells, or 20 percent of those inactive wells over 25 years old, resulting in annual revenue of \$350,000; and 15 percent of operators of approximately 80,000 wells annually would chose the option for the \$100 fee for a permit application associated with an abeyance of plugging report, resulting in annual revenue of \$1,190,160.

Local Government Impact

No fiscal implication to units of local government is anticipated.

Source Agencies: 455 Railroad Commission

LBB Staff: JOB, SD, SZ, ZS, TL