F I S C A L   I M P A C T   R E P O R T

		ORIGINAL DATE	2/3/2020		
SPONSOR	HENRC	**LAST UPDATED**	2/13/2020	**HM**	29/HENRCS
SHORT TITLE	Energy Operation Bonding Amounts			**SB**	
				ANALYST	Torres

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY20	FY21	FY22	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
Total	Minimal	Minimal	Minimal	Minimal	Nonrecurring	General Fund

(Parenthesis ( ) Indicate Expenditure Decreases)

SOURCES OF INFORMATION
LFC Files

Responses Received From
Energy, Minerals, and Natural Resources (EMNRD)
New Mexico Environment Department (NMED)
State Land Office (SLO)

SUMMARY

Synopsis of Bill

The House Energy, Environment and Natural Resources Committee Substitute for House Memorial (HM29) resolves that support be expressed for establishing financial assurance amounts that are sufficient to cover remediation and reclamation costs and lease obligations and requests a review of New Mexico's statewide remediation and reclamation bonds, an evaluation of how to ensure adequate bonding, the creation of an advisory group chaired by the commissioner of public lands, and the remittance of HM29 to the relevant parties.

HM29 requests that the New Mexico State Land Office (SLO), the Energy, Minerals and Natural Resources Department (EMNRD), and the New Mexico Environment Department (NMED) conduct the bond adequacy review and evaluate how to ensure adequate bonding to fulfill their respective statutory obligations to avoid having excess expenses fall on taxpayers or state land trust beneficiaries. The agencies are to report their findings to the appropriate legislative interim committee by December 1, 2020. Furthermore, the requested advisory committee designated to asses the need for changes to laws, rules, and policies to achieve the objective of HM29 includes:

- The State Land Office

- The Oil and Conservation Division of EMNRD
- The Department of Environment (NMED)
- Affected stakeholders, including representatives of large and small oil and gas prducers, midstream operators, other energy operators, environmental and conservation advocacy organizations, and interested members of the public.

FISCAL IMPLICATIONS

Responding agencies reported that the study will require expenditure of existing operating budget funds at a manageable level, given existing budgets.

SIGNIFICANT ISSUES

The Energy, Minerals, and Natural Resources Department highlights the following:

> Under the Oil and Gas Act, every person who operates an oil, gas or service well is required to provide financial assurance to EMNRD to assure that the well is properly plugged and abandoned. NMSA 1978, §70-2-14. Under the Surface Mining Act, coal mines must provide performance bonds to cover all requirements under the Act and the permit including reclamation. NMSA 1978, §69-25A-13. Under the Mining Act, a uranium mine would be required to provide financial assurance covering all requirements of the permit including reclamation. NMSA 1978, §69-36-7(Q). EMNRD does not issue permits or hold financial assurance for energy generation facilities.
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> HM29 points out the failure of federal agencies to update their bonding requirements. EMNRD does regularly review its financial assurance rules to determine if changes are necessary. In 2018, EMNRD revised its financial assurance rules for oil and gas wells to increase the amounts for both single well bonds and blanket bonds. 19.15.8 NMAC.
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> The requirement that EMNRD conduct a bond adequacy review related to energy production and infrastructure, evaluate how to ensure adequate bonding, and to report their findings to the appropriate legislative interim committee by December 1, 2020 places a strict timeline to address a large and complex review.

The State Land Office notes the following issues:

> As noted in the proposed memorial, multiple state agencies are tasked with ensuring adequate bonding protection for energy and extraction related activities on public and private lands. The state land office (SLO) holds surety bonds in connection with its management of 9 million acres of surface land and 13 million acres of mineral estate throughout New Mexico, which includes over 30,000 active leases and rights-of-way involving a broad variety of economic activities, including agriculture, oil and gas development, renewable energy, saltwater disposal, mining, and other business development and infrastructure. The Energy, Minerals, and Natural Resources Department (EMNRD) receives bonds in connection with its regulation of mining, oil and gas activities, produced water disposal, and its clean energy programs. Further, the environment department (NMED) has a mission to protect and restore the environment for future generations.

Because fidelity or surety bonds can be an effective way to ensure that the persons engaged in energy and extraction-related activities perform their obligations to reclaim the land and remediate surface and subsurface contamination and thereby help prevent or reduce losses to taxpayers and beneficiaries, bonds should be set at amounts that provide sufficient financial assurance to prevent remediation and compliance costs—such as the costs of remediating sites and removing infrastructure—from falling on taxpayers or state land trust beneficiaries.

The SLO has collected the following information relevant to financial assurances:

- There are over 57,000 active oil and gas wells and over 64,000 inactive wells statewide, of which 14,060 active oil and gas wells and 17,686 inactive oil and gas wells are located on state trust lands. The "inactive" well count provided by OCD includes plugged, temporarily abandoned, new/not yet drilled wells, and dry holes. Statewide, there are approximately 2,700 wells that are on the Inactive Well List, which indicates that the wells are not plugged, and are not in approved temporary abandonment status.

- The average cost in New Mexico to plug a well is $28,318 per well, and the cost to remediate contamination associated with a single lease can range from $5 thousand to millions of dollars depending on the extent of contamination.

- When an operator goes out of business or does not have financial means or bonding in place to remediate a site, the wells may eventually become orphaned or abandoned. OCD reports that the number of orphaned and abandoned wells throughout New Mexico is 711, of which only 43 have been plugged. OCD's annual report cites that they only have the capacity to plug 27 orphaned wells a year.

- OCD bond requirements are generally limited to plugging and abandonment costs, in an amount that varies depending on the number of wells per operator, with the maximum amount set at $250 thousand for over 100 wells.

- Outside of bonding, the plugging of orphaned wells is currently managed through the OCD Restoration Fund, which is funded by a tax on oil and gas operators to pay for plugging orphaned wells. This fund is currently budgeted at approximately $5 million, which is inadequate considering the number of wells needed to be plugged and remediated is over 700. The uses of this fund are stated in rule, and in pertinent parts are limited to reclaiming and plugging abandoned wells and restoring and remediating abandoned well sites and associated plugging facilities. In the past, the fund has been used for purposes such as paying salary and benefits for OCD staff. Funds were also reverted to the general fund to cover gaps in state funding. If this practice continues, this fund will continue to be an insufficient source for restoration of oil and gas sites and infrastructure.

- Current state land office bonding requirements require a maximum bond of $25 thousand, which may cover an unlimited number of oil and gas and minerals leases, as well as most rights of way and business leases, and most other types of leases issued on state land statewide to a single lessee.

- The state land office has pulled one bond for a produced water spill in Lea County. This spill occurred 5 years ago and still has an estimated cleanup cost of over $600 thousand. The bond that was pulled only covered $10 thousand of the cost to clean up the contamination.

- There are instances where the state land office is able to identify spills or contamination and consult with companies to initiate plans for remediation. In most cases, companies choose to pay out of pocket, because the existing bonds will not cover the cost.

- The state land office Restoration and Remediation Fund (NMSA 1978, § 19-1-11) was created by the Legislature in 2017. The purpose of the state land office's Restoration and Remediation Fund is to provide funding to address surface damage, watershed, forest or grassland restoration and remediation projects (illegal dump sites, contaminated sites, etc.) on state trust lands. As a condition of using the fund, the state land office must attempt to recover the costs of remediation projects from any liable parties. The balance of the non-reverting fund ranges between $1-2 million, but it depends on how much money the state land office generates each year through non-royalty income (1 percent from the Land Maintenance Fund earnings go to the fund each year).

- This fund is paid for through the earnings that would otherwise go to public schools, universities and hospitals. When money from the fund is spent for contaminated site cleanup, the result is less funding for beneficiaries. With nine million acres of state trust land throughout the state, the balance of the fund is inadequate to provide resources to both finance projects that are needed to restore the health of the land as well as cover the remediation needs.

- The existing exposure for plugging inactive well sites on state lands alone is over $5 million dollars, and the cost of remediating these sites would cost additional unknown millions of dollars.

- There are over 10,000 miles of hydrocarbon, produced water, fresh water, carbon dioxide, and nitro sulfide pipelines in rights of way throughout the state, and the existing exposure for decommissioning pipelines and remediating rights of way on state lands alone is hundreds of millions of dollars.

In a September 2019 report the U.S. government accountability office (GAO) reviewed whether bonding inadequacies existed as to federal lands managed by the U.S. bureau of land management and found that oil and gas bond amounts largely have not been updated in 40 years or more, and fail to serve their intended purpose. The GAO recommended that bond minimums be raised to more closely reflect actual remediation and reclamation costs.

The GAO estimated a minimum reclamation cost of $20 thousand per site and a maximum cost of $145 thousand per site. Extended onto all existing oil and gas infrastructure on federal land, the minimum clean-up cost would be $46 million and the maximum, $333 million. For companies operating on federal land, 77 percent of existing bonding on those operations is too low to reclaim the lowest scenario ($46 million), while 95 percent of existing bonds are too low to reclaim the highest scenario ($333 million). Inadequate bonding is not limited to state or fee land.

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