DECOMMISSIONING FINANCIAL SECURITY

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Following objections by companies and members of Congress, the Interior Department on January 6 suspended most applications of a new rule requiring lessees to post large amounts of financial security until the day their offshore platforms must be dismantled. What is at stake in requiring the security—and what is the scope of the decommissioning task that lies ahead?

Decommissioning 101

Whether the NTL is unfrozen, modified, rescinded or left suspended, the decommissioning job will remain. What are the decommissioning obligations in the first place—what are the tasks and exposures with which the security discussions are concerned?

The following summary focuses on federal law. However, a variety of state and local laws may also be implicated, especially relating to onshore disposal of decommissioned assets and other shore-based activities.

As stressed above, decommissioning can be a very expensive proposition. Platform dismantlement projects can be engineering marvels, because of the depth of the water in which the platforms and wells are constructed and the short seasonal windows when work can safely proceed. For example, in the Gulf of Mexico, hurricane season generally extends from June 1 to November 30, and requires additional precautions in the types and design of mooring equipment. During years in which several hurricanes form in the Gulf, cumulative effects from the hurricanes on oil and gas operations can be significant, including structural damage to fixed production facilities.

Removal is also an environmentally sensitive undertaking. Dismantlement typically requires either explosives or mechanical means using underwater divers or drones. Removal by any method, whether mechanical or explosive, causes turbidity and loss of established hard surfaces and functioning habitat that, at many platforms, has been colonized by large numbers of invertebrates and fish. Explosives have the added risk of shock waves and acoustic energy that can kill or harm marine species and disrupt or damage marine life near the platform structure.

What is decommissioning? Is it the same as "plugging and abandoning," or "abandonment"?

"Decommissioning" is the ending of oil, gas, or sulfur recovery operations and returning the lease to a condition that meets government requirements. 30 C.F.R. § 250.1700(a). It encompasses the physical process of dismantling and removing an offshore platform and related facilities. Absent permission for abandonment of assets in place, partial removal or alternative use (see below), regulations require all platform components to be removed to at least 15 feet below the sea floor "mudline." This includes the the topside (the decks, cranes, and drilling rig), the jacket (the steel legs and framework supporting the topside), conductor casings between the wells and the

platform, templates (steel frames used to tie in production from several wells), and pilings.

"Plugging and abandoning" is a subset of decommissioning concerned with the wells themselves. "Well P&A" typically involves filling the well with fluid, removing downhole equipment, cleaning out the wellbore, plugging open-hole and perforated intervals at the bottom of the well, plugging casing stubs, plugging annular space, placing a surface plug, and injecting fluid between plugs. "Abandonment" by itself usually refers to one method of decommissioning, namely leaving the asset in place—but only after the necessary engineering and environmental precautions are taken and the necessary regulatory approvals secured.

How do co-lessees allocate responsibility for decommissioning?

The 2015 American Association of Professional Landmen (AAPL) model form Operating Agreement for Offshore Deepwater obligates the operator to perform the decommissioning activities, and allocates costs for decommissioning based on each participating interest. The Association of International Petroleum Negotiators (AIPN) 2012 model Joint Operating Agreement, an agreement commonly used outside of the U.S., similarly provides that decommissioning costs are borne by the parties in accordance with their interests. Purchase and sale agreements often allocate the lease and operating agreement liabilities between the buyer and seller.

Larger operators in the U.S. are supplementing the AAPL model form with more robust decommissioning clauses that impose specific obligations on the parties, such as indemnities, funding escrow accounts, and providing security to guarantee performance. Thus, larger co-lessees have been seeking protections similar in nature to the NTL requirements, if not to their full extent.

How are platforms and pipelines decommissioned?

The conductors between the wells and the topsides are usually dismantled first. To remove the conductor casing, operators can choose to sever it with explosives or mechanical cutting, pull and section it in 40-foot long segments, or use a crane to lay down each casing segment in a staging area and then offload it at a port for onshore disposal.

Once the conductor casing is removed, the platforms, templates and pilings are removed. First, the topsides are dismantled and lifted onto barges using a derrick crane. The next and most expensive demolition step is removing the jacket. Divers use explosives, torches, or abrasive technology to make the bottom cuts on the piles 15 feet below the mudline. Then the jacket is removed either in small pieces or in a single massive lift.

Pipelines and utilities (for example, power cables) can often be abandoned in place if they do not interfere with navigation or commercial fishing or pose an environmental hazard. The operator must flush the pipeline with water and disconnect it from the platform and fill it with seawater. The open end is then plugged and buried three feet below the seafloor and covered with concrete.

After all equipment and infrastructure are removed, the operator performs a site clearance, surveying to identify any debris left behind by the removal process and any environmental damage. Remote operated vehicles or divers then remove any additional debris identified, and test trawling verifies that the area is free from potential obstructions.

What planning time and permits are required for decommissioning?

Project management, engineering and planning for the decommissioning usually start three years before the well is finally abandoned. Likewise, permitting related to decommissioning of a platform can take three years to complete. The federal agencies potentially include BOEM, BSEE, National Marine Fisheries Service, Army Corps of Engineers, Fish and Wildlife Service, National Oceanic and Atmospheric Administration, Environmental Protection Agency, Coast Guard, and the Department of Transportation's Office of Pipeline Safety.

State and local agency permits may also be necessary. For example, plans for onshore disposal or recycling of equipment may require state approvals, as may decommissioning of any shore-based pipelines, use of ports, and staging, assembly and storage areas.

What are the alternatives to complete and immediate removal?

Platforms may be converted to artificial reefs in lieu of complete removal when a state artificial reef program is in place. Under the federal Rigs-to-Reefs program, BSEE may "grant a departure from the requirement to remove a platform or other facility and allow partial structure removal or toppling in place so that the structure can be converted to an artificial reef." 30 C.F.R. § 250.1730.

To qualify for the program, there must be a state agency that will accept title and liability for the reefed structure under a state program. Presently, all five Gulf states have adopted artificial reef legislation; these programs are in active use, with close to 500 chartered sites offshore Texas, Louisiana, Mississippi, Alabama and Florida. California has enacted legislation establishing such a program (known as AB 2503), but no lessees have relied on its provisions to date.

Proponents of the reef program cite the abundant marine life that grows up and thrives around an offshore platform, and the loss of habitat that occurs when subsea structures are removed. The benefits of partial removal include preservation of existing biodiversity and habitat, and may include recreational opportunities such as diving and fishing. In addition, the state programs generally require the oil companies to remit half the cost savings from foregoing full platform removal to the state. That money can then be used by the state—for example, to fund ocean conservation and management programs.

The other alternative to immediate removal and decommissioning is the renewable energy and alternative use program permitted by the Energy Policy Act of 2005. The Act allows structures to remain in place following the conclusion of oil and gas activities so that they can be used for "energy-related purposes or for other authorized marine-related purposes." Structures may be used for a variety of purposes, such as research, recreation, education, renewable energy production, telecommunication facilities, and offshore aquaculture, before being removed. However, when the structure ceases to be used for these approved alternative uses, complete removal is still required (unless it is approved for partial removal under the Rigs-to-Reefs program discussed above). Oil and gas lessees would remain responsible for financial security for decommissioning during the extended time periods when the alternative use is being conducted.

Promisingly, scientists, industry and some regulators are exploring evolving techniques to evaluate the ecological costs and benefits associated with complete removal compared with various leave-in-place alternatives. These comparative assessment methodologies seek to better account in decommissioning decision-making for the ecosystem services, particularly habitat value, provided by this subsea infrastructure. More consistent and predictable availability of alternatives to full removal could substantially drive down decommissioning costs, which could, in turn, be factored into the regulators' calculus as to the magnitude of financial security required.

What is the framework for financial security requirements?

The Outer Continental Shelf Lands Act provides the Secretary of the Interior with the authority to require bonds or other forms of financial assurance for decommissioning, rents and royalties, and other financial obligations (except oil spill financial responsibility, which is covered by the Oil Pollution Act (OPA)). 30 CFR § 556 is the primary regulatory source regarding the financial assurance requirements administered currently by BOEM.

There is a two-stage approach to satisfy BOEM financial assurance requirements. The first stage is the base bond, which covers all types of lease obligations (except OPA liability), extends beyond the end of the lease, is required of all lessees, and can be lease-specific or area-wide. These are set bond amounts depending on the lease activity, as illustrated in Table 2.

Lease Activity	Lease-Specific Base Bond Amount	Area-Wide Base Bond Amount
Prior to operations	$50,000	$300,000
Exploration plan	$200,000	$1,000,000
Development plan	$500,000	$3,000,000
Pipeline right of way	N/A	$300,000

Table 3. Base Bond Requirements

The base bonds expire seven years after the termination of the lease, six years after completion of all bonded obligations, or after termination of any litigation related to the bonded obligation, whichever occurs last.

The second stage is the supplemental bond, which provides additional coverage for lease obligations, and is canceled after decommissioning is completed and BSEE certifies clearance of outstanding payments. The only exception to cancellation of the bond once decommissioning and other outstanding lease obligations are fulfilled is if BOEM determines that the future potential liability resulting from any undetected problem is greater than the amount of the base bond. In this case, BOEM may notify the surety that the agency will wait seven years to cancel all or part of the bond. It is the supplemental bond requirement that provides the basis for the financial analysis and security mandate revised in the NTL discussed in Part One.

What types of financial security are accepted?

30 CFR § 556.902 provides the requirements that the security must meet. Surety bonds must be payable on demand and guarantee compliance with all lease obligations. Several other forms of security may be acceptable to BOEM, including letters of credit, traditional or captive insurance, third-party guarantees, pledges of U.S. Treasury notes or bonds, decommissioning trust agreements, risk pooling arrangements, creditworthy decommissioning contracts, and packaged financial assurance.

A lessee can use multiple instruments to satisfy its security requirements, and can arrange for a "tailored plan" through BOEM that may rely on other forms of acceptable security. The security may be phased in over a period of months, but generally needs to be completely in place within one year of the security mandate.

Conclusion.

BOEM touched a raw nerve in July 2016 by increasing the scrutiny and the security required of OCS lessees. The January suspension of the rule as to multiple-party leases gives time for a new administration to take a fresh look at the issues. 2017 may see some reduction of the requirements through further executive branch action. But the decommissioning jobs that lie ahead are real and substantial, and industry and government representatives need to address the funding of those tasks. The alternatives to complete removal can often create tangible environmental and economic benefits, and should be explored and pursued in parallel with the evolution of the financial standards. ■