

# BOEM Proposes Major Changes to its Financial Security Requirements for the OCS

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On September 22, 2015, the Bureau of Ocean Energy Management (BOEM) made available for review proposed guidelines on the procedures and criteria that the BOEM will use to determine the financial ability of oil and gas companies operating on the Outer Continental Shelf (OCS) to carry out their obligations and the potential need for additional security. More specifically, the BOEM has issued:

- Criteria to Determine Financial Ability to Carry Out Obligations;
- Proposed Financial Metrics;
- Financial Terms and Ratio Definitions; and
- Additional Information on Proposed Guidelines.

As we noted in a blog post this past spring, these proposed guidelines follow the February BOEM Financial Assurance Forum and a March meeting between BOEM staff and several lawyers who focus on OCS regulatory matters, including Gordon Arata attorneys.

Existing regulations (*e.g.*, 30 C.F.R. § 556.52 *et seq.*) require lessees on the OCS to provide bonds or other alternative forms of financial assurance to cover current and future operations including the decommissioning of wells and facilities. The proposed guidance expand on the criteria that the BOEM will use to determine if and when additional security may be required for an OCS lease, pipeline right-of-way (ROW) or right of use and easement (RUE). The proposed criteria state that “[a]ll owners of record title interest in a lease, owners of operating rights in a lease, pipeline ROW holders, or RUE holders are responsible for ensuring that all obligations, including decommissioning, are satisfied for every lease, ROW or RUE to which they are a party. If, to this end, the BOEM Regional Director determines that their financial ability to carry out their obligations or their existing financial assurance is not sufficient to cover their OCS obligations, he or she may require you to provide and maintain additional security.”

Several key changes in the proposed guidance identified by the BOEM are:

- The BOEM will determine the financial capacity of each company (which includes owners of record title, owners of operating rights, pipeline ROW holders and RUE holders) to carry out its abandonment obligations taking into consideration the company's (i) financial strength based upon audited financials and other information, (ii) projected strength taking into consideration both existing production and proves reserves, (iii) business stability, (iv) reliability, and (v) compliance record. In this determination, the BOEM will consider 100% of the decommissioning liability for every lease, ROW and RUE in which a company holds an interest. In the event a company's abandonment obligations exceed its financial capacity as determined by the BOEM, then the company will be required to provide additional financial assurances.
- The combined financial strength and reliability of co-lessees or operating rights holders will no longer be considered.
- In the event a lease is co-owned, it will be up to the owners of record title and operating rights to determine how best to fulfill BOEM's requirement for 100% assurance of OCS decommissioning liabilities among themselves. It appears that this division will need to be resolved before the determination of what amount, if any, of additional financial assurances are required.
- Any additional financial assurance requirements will be phased in over a period of time.
- The BOEM may consider alternative forms of financial assurance as part of tailored plans developed by an individual company.
- A company will no longer be granted waivers or exemptions from supplemental bonding, but may be eligible for self-insurance to its supplemental bond obligations. A company can apply for self-insurance regardless of its net worth.
- Self-insurance (which is currently capped at 50% of a company's net worth) will be changed to a maximum of 10% of tangible net worth.

The proposed guidance will be available on BOEM's website for a 45-day review period. On October 9<sup>th</sup>, BOEM will hold a workshop in Houston to meet with industry representatives to answer questions and discuss the proposed change. At the end of the 45-day review period, the BOEM will finalize its proposed guidance. The BOEM plans to implement proposed changes via a "Revised Notice to Lessee" (NTL). The revised NTL will provide updated procedures for guidance and clarification and will apply to all BOEM regions and planning areas. In the meantime, companies on the OCS can continue to rely on the current supplemental bonding regime, as detailed in NTL No. 2008-N07.

Our advice over the past several years is now all the more important. If you are considering entering into a purchase and sale agreement, joint operating agreement, farmout agreement, or any other type of similar agreement covering one or more properties located on the OCS, it is imperative that you consider and address the sharing of this financial assurance for decommissioning obligations.