April 11, 2019

The Hon. Acting Secretary David Bernhardt
Department of the Interior
1849 C Street, N.W.
Washington DC 20240

Submitted to Docket ID: *DOI-2017-0003-0004 via Regulations.gov*

Dear Mr. Bernhardt:

Over the past 50 years, the offshore oil and natural gas industry, including API member companies, has engaged in the acquisition, exploration, development, divestment, and decommissioning of oil and gas assets on the United States Outer Continental Shelf (OCS). API's members have a strong and vested stake in the health and long-term viability of the Gulf of Mexico as a premiere basin for resource development. To keep the OCS a strong and attractive investment option, BOEM should put forth a responsible, predictable and equitable Bonding and Financial Assurance program. Specifically, its program should be underpinned by the premise that companies investing in offshore leases should have the financial capacity to address all obligations legally assumed or created. Additionally, the financial strength of former lease owners should not be a substitute for ensuring the current lease owners have the financial ability to meet all existing lease obligations, including decommissioning, since it is the current owner who has primary legal responsibility for the decommissioning liability.

During the decades of leasing and development that have occurred, OCS leases have been acquired, developed, and then assigned to others. Some leases have been transferred numerous times. When buying and selling OCS leases, parties to these transactions rely – and have relied on – predictable and equitable OCS Bonding and Financial Assurance regulations. For instance, the current lease agreements that companies execute with the federal government not only allow for production of critical domestic resources, but also stipulate that the lessee will plug all wells, abandon all pipelines and remove all platforms and other facilities from the leased area upon lease termination – also known as decommissioning. Furthermore, current federal regulations also provide that owners of existing leases are primarily liable for decommissioning obligations of existing leasehold facilities as to which they hold a record title or operating rights interest.

As the Department of the Interior (DOI) revises its Bonding and Financial Assurance regulations pursuant to Executive Order 13785 and DOI Secretarial Order 3350, its main goals should be to adopt regulations and implement policies that keep people safe, protect the environment, and ensure that U.S. taxpayers are not left with any OCS decommissioning obligations. A predictable process that requires financial security from the current lease owner, based upon a fair assessment of capacity and risk, provides the financial assurance needed to protect the taxpayer, while also holding current lease owners accountable to fulfill their obligations.

This can be accomplished, in large part, by advancing a contingent liability framework (reverse chronological), as well as implementing the Principles and Reforms attached hereto. Regarding contingent liability specifically, if all of the current co-lessees (lease owners) default in fulfilling their decommissioning obligations; only in the event of such a default should the government look to prior lease owners (that is, predecessors in the chain-of-title) to address the defaulted obligations. When this occurs, DOI should pursue those predecessors in reverse chronological order.

This contingent liability framework is grounded on three policy principles: **Safety**, **Accountability, and Efficiency**.

1. **Safety**

The most recent predecessors-in-title are better suited than long-removed predecessors-in-title to understand the safety risks, to assume control of a lease and its assets, and to comply with any decommissioning obligations. Many OCS leases have been owned and operated by multiple companies, spanning decades, and over time the facilities and wells may have undergone significant modifications. It is not in the taxpayer's best interest – nor in keeping with DOI's safety mandates – for the government to demand decommissioning obligations be assumed by a former lease owner that is chronologically distant in the chain-of-title and has not operated the offshore facility(ies) for many years (often decades). These more distant predecessors do not have current knowledge of a given facility's modifications or any recent maintenance activity, and they often lack access to pertinent documentation and other necessary information related to the decades-old wells, platforms, pipelines, etc. To ensure that the facility can be safely decommissioned, the government should, as policy, look first to the lease owner who operated the facility(ies) immediately before the defaulted operator/lease owner.

2. **Accountability**

If the government does not hold the most recent predecessors-in-title accountable for the defaulted decommissioning liability, then operators of late-in-life assets could be incentivized to thinly maintain these assets instead of exercising due care, which could lead to serious and unsafe operational decisions. This is especially true if current lease owners are not required to provide the government with enough financial assurance to cover their decommissioning obligations (e.g., through trust accounts, cash, collateral arrangements, bonds, and/or parent or third party guarantees).

Moreover, if the government both allows current lessees to cite the financial strength of former lessees as a substitute for financial assurance from current owners *and* does not establish a general policy of pursuing predecessors in reverse chronological order, many operators could evade financial accountability for their operations in the OCS.

3. **Efficiency**

With a contingent liability framework, the government will simplify the often complex and time-consuming administrative process it faces when delineating "accrued" versus "unaccrued" liabilities – an especially challenging task when facilities/wells may have been added or modified over the life of a lease, resulting in predecessors with varied accrued decommissioning obligations that are dependent on where each predecessor falls in the life of the lease. Instead, a contingent liability framework is the most administratively efficient and cost-effective way to assure performance of *all* the end-of-lease-life decommissioning obligations by fewest number of predecessors.

Additionally, the most recent predecessors-in-title are in the best position to assess and foresee the financial security needs for a given asset and, in recent cases especially, may already hold private security from a successor defaulting owner. Using funds available from existing private financial security instruments already in place (which would not be available to all predecessors) to meet defaulted decommissioning obligations facilitates the instruments' intended use and benefits all parties.

Furthermore, a contingent liability framework still ensures that the current and previous lease owners remain liable for their accrued obligations. Before going back to predecessors in the chain-of-title, DOI should first exhaust its efforts to hold current lease owners liable. DOI could reserve the flexibility, in urgent or exigent circumstances, to skip immediate predecessor lessees and demand performance from lessees farther back in the chain-of-title when necessary to quickly mitigate and reduce potential future harm (*e.g.*, hurricane risk).

Lastly, while uncertainty could still persist under a contingent liability framework – simply given the nature of these complex commercial arrangements – the existing regime has been, and certainly will continue to be, exposed to difficult and extensive challenges, especially where there remain material questions related to: (i) whether a predecessor can be held legally liable where the predecessor corporate entity does not exist (much likelier to occur with distant predecessors), (ii) how to define the scope of accrued liability for each predecessor, and (iii) the applicability of a joint and several liability regime to prior lessees and/or transfers of lease interest.[1] These questions would complicate any future regulatory regime that excludes contingent liability and/or would permit current lessees to "rely" on predecessors instead of focusing on current lessees to provide adequate security or other evidence of financial capacity.

The far more appropriate and certain path – for lessees, investors, and the government – is for DOI to simply demand performance of the most recent predecessor(s), who would be in the next best position and under the clearest obligation to meet those accrued, decommissioning responsibilities.

[1] During the past 50 years, DOI has revised its lease language, promulgated new regulations, and issued numerous interpretations, guidance, and policies. For example, DOI modified its regulations on liability in 1997 and 2016. It also issued interpretative communication in 1988, and again in 1989, that specifically addressed the matter of retained liability, explaining that the predecessor agency to BOEM and BSEE, the Minerals Management Service, would not proceed against an assignor where its assignee failed to perform decommissioning obligations. These historical agency positions established expectations that the parties at the time relied on to inform their transactions.

In conclusion, given the meaningful questions raised in this letter with respect to the government's bonding and financial assurance regulatory liability structure, and the need for a fully informed consideration of the issues discussed above, we believe that DOI, at a minimum, should provide the public with an opportunity to provide its input on the issue of contingent liability. Namely, DOI should seek input on the following in its upcoming rulemaking:

- Whether or not DOI should demand performance of the previous lease owners in reverse chronological order.
- The triggering events that would cause DOI to move from one predecessor to the next in the chain-of-title (e.g., bankruptcy, safety concerns, environmental issues, weather impacts, litigation, etc.).
- If DOI does not pursue predecessors in reverse chronological order, how DOI should manage multiple owners who are ordered to decommission the same infrastructure.

By not looking to predecessors in reverse chronological order through the chain-of-title in the event of a default by current lease owners – especially if those current lease owners are not held accountable to provide financial assurance for all of their decommissioning obligations – DOI would be sending the wrong message to at-risk current lease owners/operators: namely, that they can default on their decommissioning obligations, re-emerge on the OCS as a newly incorporated entity, and rely on distant predecessors to assume their decommissioning obligations – or, even worse, have those obligations assumed by the U.S. taxpayer. This cannot become the acceptable policy.

Instead, DOI should develop a sensible and robust Bonding and Financial Assurance program, while also using its authority to enforce the timely decommissioning of unsafe, idle infrastructure, take timely action when lease owners are not meeting those current decommissioning obligations, engage in effective oversight and enforcement of underperforming operators, and only allow qualified, responsible lease owners and operators to be active in the OCS. Together, these outcomes can ensure that the OCS remains a safe, viable, and attractive investment option that will help meet the energy needs of the United States and objectives of the current Administration.

By asking for public comment on the issues addressed in this letter, DOI can provide the public with an opportunity to enhance the conversation and understanding of its regulatory proposal, helping to ultimately create a safer, more secure OCS that creates a strong investment case and protects the taxpayer's interests.

Sincerely,

Erik Milito
Vice President, Upstream & Industry Operations
American Petroleum Institute

cc: Joseph Balash, Assistant Secretary for Land and Minerals Management

Marcella Burke, Acting Senior Counselor to the Assistant Secretary for Land and Minerals Management
James Schindler, Special Assistant, Bureau of Ocean Energy Management

Principles and Reforms for a Risk-Based and Balanced

OCS Financial Assurance Program

In the case of OCS Financial Assurance, U.S. taxpayers are first protected by financially and operationally prudent current lease owners, then by the financial assurance they provide, and lastly by predecessors, if any. Accordingly, DOI should ensure that current lease owners are capable of meeting 100% of their decommissioning and other lease obligations. To meet this objective, DOI's required reconsideration of currently-suspended NTL 2016-N01 and regulatory review – pursuant to Executive Order 13785 and DOI Secretarial Order 3350 – should be guided by four core principles regarding financial assurance on the OCS:

- The OCS should remain a viable and attractive investment option through a responsible, balanced, predictable and equitable financial assurance program.

- The financial strength of former lease interest owners is no substitute for financial security against the operational and financial risks of current owners.

- Companies that invest in offshore leases should have the financial capacity to address, on a realistic timeline, all obligations legally assumed or created.

- The financial assurance program that DOI ultimately adopts should be risk-based and focused on offshore properties late in their economic life cycle. Implementation should be phased-in, allowing companies to successfully comply with any modification to DOI's existing financial assurance program.

To implement the above principles, DOI should amend BOEM regulations at 30 C.F.R. Part 556 and related BSEE regulations at 30 C.F.R. Part 250 as follows:

1. *Prohibit consideration of predecessors in supplemental security demands.* DOI should not use the financial strength of predecessors-in-title as a criterion in determining the amount of supplemental financial security required from a current lease interest owner. Allowing current owners to decrease their financial assurance obligation based on financially strong predecessors-in-title is bad policy and legally unsupportable. Prior owners assigned their interests in reliance on existing BOEM regulations requiring the assignee to meet the full financial assurance requirements for all decommissioning and other lease obligations accrued prior to assignment.

2. *Adhere to chain-of-title for performance of lease obligations.* DOI should clarify that it will continue to require performance of all accrued lease obligations in the first instance by the current record title and operating rights owners. In the event of default of lease obligations by all current lessees, BSEE should pursue predecessors-in-title in reverse chronological order, beginning with the most recent assignors that are most familiar with the lease. The recent regulatory addition of joint and several liability among all predecessors and current lease owners – which first appeared, without notice and comment, in a final rule promulgated in 2016 – does not mandate, or warrant, demands throughout the chain-of-title per BOEM's serial register page for a lease. BSEE should

not unilaterally and arbitrarily pick and choose which of the prior owners the bureau would like to perform lease decommissioning.

3. *Maintain self-bonding for financially strong operators.* BOEM should not require the posting of additional security, or permit use of additional self-bonding, for companies that hold investment grade financial ratings. This approach would be consistent with the lack of historical evidence of such companies defaulting on decommissioning obligations.

4. *Increase accessibility of other existing security*. If a predecessor-in-title is required to undertake any decommissioning obligation, BOEM should grant that party access to any lease-specific or general bonds, or other security, that the defaulting current lessees provided to BOEM for decommissioning work.

5. *Clarify and standardize financial strength criteria for any supplemental security.* DOI should publish clear assessment criteria that the agency will use to determine if the current lessee has the financial strength to fulfill all accrued lease obligations without providing additional financial security to DOI to cover said obligations. Assessment criteria and metrics should be clear and transparent for all lessees versus confidential or tailored arrangements. The agency should use financial standards particularly applicable to the oil and gas industry.

6. *Avoid trade references.* The reliability criterion for any additional security should be based on public credit ratings, or an implied credit rating system only in the event a public credit rating is not available. While 30 C.F.R. § 556.901(d)(1)(iv) alternatively allows BOEM to use "trade references," BOEM should avoid doing so because such anecdotal data are significantly less probative of the lessee's financial reliability for lease obligations. If BOEM does collect such references, it should verify them and analyze their import for additional financial security.

7. *Define "record of compliance" criterion.* BOEM should confirm that a lessee's "record of compliance" under 30 C.F.R. § 556.901(d)(1)(v) that impacts financial assurance considerations only includes infractions by the lessee itself and not its designated operator. Moreover, this criterion should include only major operational violations where the lessee is under a "Performance Improvement Plan," royalty-related violations involving delinquent and uncontested royalties owed, or unpaid civil penalties.

8. *Ensure sequential liability for predecessors-in-title.* BSEE and BOEM performing their respective roles to determine decommissioning liability and require adequate financial assurance from current lessees should diminish the need for universal, simultaneous liability among all current and previous interest owners, and thereby avoid uncertainty and financial accounting burdens on prior interest owners' years, or even decades, after relinquishing their lease interests.

9. *Expand alternatives to bonds.* DOI should more expressly afford itself flexibility to consider vehicles other than bonds when addressing supplemental financial security

requirements. Wherever the term "bonds" appears in the regulations in Part 556 Subpart I, BOEM should add "or other financial assurance," consistent with the title of that Subpart. For shorthand, BOEM could define "other financial assurance" in § 556.105 as "a form of security other than a bond that is acceptable to BOEM and complies with the requirements of this Part."

10. *Prevent premature security.* Current § 556.901 requires additional bonding when an exploration or development plan is merely submitted, unless BOEM grants an exception. Instead, the obligation to obtain a bond and incur the associated bonding costs should be delayed, at a minimum, until the proposed activities have been conducted. Once a well is drilled, if the well is not permanently plugged and abandoned, BOEM should consider whether or not supplemental security is needed. Once a platform or pipeline is installed, it is more sensible to stage the financial assurance requirement and delay full funding until later in the lease term. The risk of default on decommissioning obligations is minimal when lease production is at its peak. Full financial assurance should be required only when production levels are in significant decline and estimated future revenues are insufficient to cover the cost of decommissioning.

11. *Enable more flexibility for third-party guarantees.* DOI should allow a third-party guarantor to limit its guarantee to the obligor's proportionate ownership share of lease obligations and decommissioning obligations, as opposed to a guarantee for "all lessees' lease obligations" per current § 556.905(c). Additionally, guarantors should be relieved of liability when replacement security is provided or security is no longer required, comparable to sureties being relieved of liability when a bond is canceled.