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DEPARTMENT OF THE INTERIOR

Bureau of Ocean Energy Management

30 CFR parts 550, 551, 556, 581, 582 and 585

RIN 1010-AD83

[Docket ID: BOEM-2013-0058]

Risk Management, Financial Assurance and Loss Prevention

MMAA104000

AGENCY: Bureau of Ocean Energy Management (BOEM), Interior.

ACTION: Advance Notice of Proposed Rulemaking (ANPR)

SUMMARY: BOEM is seeking comments and information regarding its effort to update its regulations and program oversight for Outer Continental Shelf (OCS) financial assurance requirements. When BOEM's existing bonding regulations were originally drafted and first implemented, the principal risks associated with OCS leases were non-payment of rents and royalties, noncompliance with laws and regulations, and potential problems due to bankruptcy. While potentially significant, such risks were generally well-known and of limited complexity, size and scope.

Due to increasingly complex business, functional, organizational and financial issues and vast differences in costs associated with expanded and varied offshore activities, BOEM has recognized the need to develop a comprehensive program to assist in identifying, prioritizing, and managing the risks associated with industry activities on the OCS. BOEM intends to design and implement a more robust and comprehensive risk management, financial assurance and loss prevention program to address these complex issues and cost differences associated with

offshore operations. To do so, BOEM is seeking stakeholder comments regarding various risk management and monitoring activities pertaining to financial risks to taxpayers that may result from activities on the OCS. This notice specifically discusses the bonding and financial assurance program for BOEM's offshore oil and gas program. However, we also welcome the submission of comments on the analogous bonding and financial assurance program for BOEM's offshore renewable energy and hard minerals programs.

BOEM currently requires lessees to provide performance bonds and/or one of various alternative forms of financial assurance to ensure compliance with the terms and conditions of leases, Rights-of-Use and Easements (RUEs) and Pipeline Rights-of-Way (ROWs). BOEM is seeking comments on who is best suited to mitigate risks and whether the correct parties are providing guarantees and other forms of financial assurance, as well as whether, or to what extent, the current forms of financial assurance are adequate and appropriate.

Because costs and damages associated with oil spill financial responsibility (OSFR) are covered separately under 30 CFR part 553, which is the subject of other proposed rulemakings on BOEM's regulatory agenda, BOEM is not soliciting comments on those regulations and their associated risk mitigation measures at this time.

DATES: BOEM will consider all comments received by midnight of [INSERT DATE 60 DAYS FOLLOWING PUBLICATION OF THIS DOCUMENT IN THE FEDERAL REGISTER]. BOEM cannot commit to considering comments received after midnight on [INSERT DATE 60 DAYS FOLLOWING PUBLICATION OF THIS DOCUMENT IN THE FEDERAL REGISTER].

ADDRESSES: You may submit comments on this ANPR using the Federal eRulemaking Portal: http://www.regulations.gov. Follow the instructions on the website for submitting comments. Please use Regulation Identifier Number (RIN) 1010-AD83 as an identifier in your

message. See also the "Public Comment Policy" paragraph under the "Supplementary Information" section below.

FOR FURTHER INFORMATION: For information regarding BOEM's comprehensive risk management, financial assurance, and loss prevention program or the major topics of this ANPR, contact Terry Scholten at terry.scholten@boem.gov (504-810-2078) or Donna Dixon at Donna.Dixon@boem.gov (504-731-1527), or by mail at 1201 Elmwood Park Blvd., GM364D, New Orleans, LA 70123. For issues related to the rulemaking process or timetable, contact Peter Meffert at peter.meffert@boem.gov (703-787-1610), or by mail at 381 Elden St., Herndon, VA 20170.

SUPPLEMENTARY INFORMATION:

Public Availability of Comments: Before including your address, phone number, email address, or other personal identifying information in your comments, you should be aware that your entire comment – including your personal identifying information – may be made publicly available at any time. While you may ask us in your comment to withhold your personal identifying information from public review, we cannot guarantee that we will be able to do so under Federal law.

Background: BOEM has program oversight for Outer Continental Shelf (OCS) financial assurance requirements set forth in 30 CFR parts 550, 556 subpart I, 581 subpart C, 582 subpart D, 585 subpart E, and in § 551.7, all of which are promulgated pursuant to the Outer Continental Shelf Lands Act (OCSLA, 43 U.S.C. 1331 et seq.). Section 5(a) of OCSLA authorizes the Secretary of the Interior to promulgate rules and regulations necessary to administer the OCS leasing program, including regulations concerning financial assurance. Section 8(p)(6) of

OCSLA requires the Secretary to obtain financial security for OCS leases, easements and rights-of-way issued for purposes other than the development and production of oil and gas.

Within DOI, BOEM is the bureau with primary authority to manage the financial risks to the government associated with the development of energy and mineral resources on the OCS. BOEM is in the process of updating regulations at 30 CFR part 556 to exercise this authority, as well as other regulations pertaining to financial assurance mentioned in the Summary above. BOEM is also reexamining the assumptions underlying its existing financial assurance and bonding program, as well as considering how to address risks and loss prevention more comprehensively. BOEM is enhancing its existing financial assurance and bonding program by incorporating a risk management approach to identifying, defining, quantifying, and treating all of the commercial, functional, organizational/business risks facing entities operating on the OCS in order to implement loss prevention measures. BOEM intends to apply this same approach to evaluating how OCS business entities can best meet their financial and contractual obligations. Such an approach would deal with all types of risk, such as mitigating financial risks resulting from fiscal, commercial and business risks, credit risk, functional and organizational risks, and hazard or event risks. Loss prevention procedures involve all of the efforts undertaken, including the regulations, processes, audits and financial controls, which are designed to minimize the government's exposure to financial risk.

Program and Regulation Development: BOEM is developing a comprehensive risk management, financial assurance, and loss prevention program to address the financial, commercial, functional, organizational/business risks facing entities operating on the OCS in order to implement loss prevention measures. BOEM intends to reduce contingent liabilities, minimize governmental and taxpayer financial exposure to financial loss, and provide a fair,

equitable and transparent approach to risk management that is understood by stakeholders and assists in the effective implementation of appropriate and cost-effective risk management and loss prevention techniques.

BOEM is committed to engaging all interested stakeholders in this regulatory process. It will coordinate and consult with other Federal agencies, including the Bureau of Safety and Environmental Enforcement (BSEE) and the Office of Natural Resources Revenue (ONRR). To facilitate comment submission, BOEM has identified four major topics. Each topic includes questions designed to provide respondents with a general framework for commenting. Please note that these topics and questions are not intended to be all-inclusive; other comments, questions, or suggestions of topics, are encouraged. Note BSEE is also conducting a separate comprehensive risk assessment related to safety of operations on the OCS, which will include a development and analysis of decommissioning cost estimates.

Major Topics:

I. Identification of Pertinent Risks/Liabilities

II. Risk Monitoring and Risk Management

III. Demonstrating Financial Assurance over Project Lifecycles

IV. Financial Assurance, Bonding Levels and Requirements

Topic I: Identification of Pertinent Risks/Liabilities

Description: BOEM recognizes the need to develop a comprehensive risk management, financial assurance and loss prevention program that can assist in identifying, prioritizing, and managing the risks associated with OCS financial, commercial, functional, and business activities. Along with evaluating and assessing the risks associated with ongoing activities, such a program would also include, but is not limited to, evaluating and assessing the business, fiscal

and commercial risks associated with transfers of ownership of leases, operating rights, RUEs, ROWs, and facilities as well as the transfer of ownership of all forms of interests in any OCS leases, RUEs, ROWs, and facilities. Such interests could include record title interests, operating rights interests, operating and/or working interests, economic interests or future participating or financial interests, among others.

BOEM is specifically interested in comments regarding the financial risks and liabilities associated with aging offshore infrastructure, deepwater decommissioning, subsea decommissioning, pipeline abandonment, Arctic operations, and new technologies designed to address deepwater development or exploration and/or development of energy or mineral resources in locations with unusually adverse conditions. BOEM also needs to address business risks associated with the changing characteristics of entities operating on the OCS (*e.g.,* smaller companies), underperformance, non-performance or default on financial or legal obligations, and underpayment or non-payment of rentals and royalties. Finally, BOEM is seeking information regarding best practices in managing the financial, commercial, functional, organizational/business risks facing entities operating on the OCS in order to implement loss prevention measures associated with catastrophic damage caused by natural events (*e.g.,* hurricanes, ice floes, earthquakes), engineering failure, or other causes.

Questions for respondents regarding identification of pertinent risks/liabilities:

1. In addition to the examples provided in this ANPR, are there other risks (monetary and nonmonetary) that BOEM should consider in developing its comprehensive operational risk management, financial assurance, and loss prevention program? What are they? Please describe any other risks noted.

2. What measures should BOEM consider to reduce the risk and magnitude of identified outcomes?
3. What information should BOEM consider in estimating the appropriate financial assurance to cover each of the identified risks?
4. How should BOEM obtain the information needed to estimate the appropriate financial assurance to cover each of the identified risks?
5. What information should BOEM consider in establishing appropriate levels and types of financial assurance?
6. How should BOEM obtain the information needed to establish appropriate levels and types of financial assurance associated with each of the identified risks?
7. How should BOEM evaluate risk levels and priorities to responsibly manage current and future liabilities?
8. What information should BOEM consider in addressing financial assurance needed to cover catastrophic damage caused by natural events, engineering failure, or other causes?
9. Should BOEM require proof of insurance/financial assurance for catastrophic events?

Topic II: Risk Monitoring and Risk Management

Description: BOEM is interested in understanding and defining the necessary elements of a comprehensive operational risk management, financial assurance, and loss prevention program and believes that monitoring its business risk and recognizing necessary risk transfer strategies are central to this effort. This effort includes risk management processes and evaluations that are systematic, are capable of being replicated, and that utilize best practices. In order to improve communication and better inform BOEM's decision-making processes, BOEM seeks information regarding its risk monitoring and risk management practices.

Questions for respondents regarding risk monitoring and risk management:

10. What should BOEM's risk management, financial assurance and loss prevention program include?
11. What measures should BOEM consider in managing risk transference?
12. How should BOEM monitor an entity's financial health in order to assess the risk to taxpayers? How often should this be done?
13. How should BOEM monitor an entity's organizational strength and any associated risk to taxpayers?
14. What measures could/should BOEM use to reduce taxpayer risk (*e.g.,* insurance, contractual indemnity clauses, contractual risk transference strategies, bonding)?
15. What risk transfer mechanisms should BOEM consider to mitigate risks associated with catastrophic events?
16. Given the complex business arrangements involved in OCS projects, which operational business partners should BOEM consider when assessing and monitoring overall financial risks (*e.g.,* lessees, operating rights owners, contractors, subcontractors)?
17. Should BOEM consider using individualized company-specific or project-specific risk management, financial assurance and loss prevention plans? If so, what should they entail and should they be optional or required?
18. Should BOEM require prior approval of all types of assignments between companies and/or lenders, including, but not limited to, assignments of overriding interests, royalty interests, net profits, production payments, or other types of lease interests?
19. Should BOEM monitor and approve the total percentage of assignments of rights and obligations between companies and/or lenders?

20. Even if BOEM does not approve all transfers of all types of rights and obligations between companies and/or lenders, should BOEM require evidence of all such transfers to be filed with BOEM in order to maintain an accurate repository of records of all transfers?
21. To what extent should BOEM monitor debt obligations?
22. Should BOEM require the recording and/or approval of all transfers of purely "economic" interests?

Topic III: Demonstrating Financial Assurance Over Project Lifecycles

Description: The 40- to 50-year (or more) life of some OCS projects injects further uncertainty in the attempt to define, manage, and reduce financial risks. Technological and financial challenges, which are not evident at the inception of a project, may arise as time goes by, and consequently, the amount of financial assurance needed may vary over time. In order to deal with ongoing commercial issues and difficult business challenges resulting in complex and far-reaching business impacts, BOEM plans to implement financial assurance and loss prevention practices designed to better define financial metrics, reduce data collection barriers, and help prepare and plan for business incidents that could compound risks to U.S. taxpayers.

BOEM's current regulations utilize bonding as the primary form of financial assurance. In addition, lessees may submit the following alternative forms of security to fulfill financial assurance requirements: treasury securities and other types of security instruments approved by the Regional Director, lease-specific abandonment accounts, third-party guarantees, demonstration of financial strength and reliability, indemnity obligations, treasury notes, and trust agreements. BOEM is seeking information to assist in managing problems that are difficult to predict and in creating strategies that reduce response barriers and foster appropriate business planning measures.

Questions for respondents regarding demonstration of financial assurance over project lifecycles:

23. What criteria demonstrate a company's ability to remain financially viable (*i.e.,* solvent) over the long term?
24. What criteria demonstrate a company's ability to pay specific costs associated with lease obligations on the OCS (*e.g.,* decommissioning)?
25. In assessing financial assurance, how should BOEM consider the value of proved producing reserves (*i.e.,* metrics and methodologies) in determining the amount of financial assurance necessary to protect taxpayer interests?
26. What factors should BOEM consider in assessing corporate structure and offshore business performance and history to help ensure that taxpayers are protected from liability risks for costs accrued by offshore operations?
27. How should BOEM consider the financial and technical qualifications of a company before the company is allowed to conduct business on the OCS?
28. To protect U.S. taxpayers, should BOEM treat significant financial or legal changes as events that would require offshore companies or operators to provide notice of such events and that would trigger BOEM's reassessment of the companies' or operators' existing financial assurances? If so, what significant financial or legal changes should be used?
29. Should BOEM tailor the amounts/levels and types of financial assurance requirements for OCS operations on a case-by-case basis (*e.g.*, by individual project, individual lease, unit, and/or company)?
30. Should BOEM consider allowing companies to set up a decommissioning trust that is funded from a percentage of production? If so, would such a trust apply to a single well or many

wells, a single lease or more than one lease, a unit, one company, or some combination of these, or some other formulation?

31. There are multiple levels of business entity risk, including: 1) risk by type of entity (whether a corporation, LLC, trust, partnership, etc.), particularly as new types of entities are being created whose control may be exercised from outside the organization; 2) risk by level of entity (where one company or entity owns another that may own a third entity, etc.); 3) risk created by shared ownership (particularly of a lease or facility, or where there are many entities involved in the ownership of the same interest); 4) risk created by subdivided interests in a lease such that different companies own distinct, severed interests in the same lease (whether divided by depth or aliquot or by function or by operating/non-operating ownership rights); 5) risks created by asset transfers from one entity to another or from one organization's domestic accounts or affiliates to some offshore accounts, operations or affiliates; or 6) other risks associated with unique or complex business entities or combinations thereof. How should BOEM deal with the complexity of multiple business entities in assessing financial assurance and managing taxpayer risk?

32. Should the levels/amounts of financial assurance and the types of allowable security demonstrating that financial assurance (*e.g.*, insurance, bonds) vary by the type of risk and/or the project lifecycle? And, if so, how?

33. Termination or cancellation of leases and/or RUEs may be necessitated by a lessee's or operator's failure to meet its financial obligations related to bonding or financial assurance. What factors do you believe BOEM should consider before making the determination that a lessee's or operator's failures with regard to meeting its financial assurance obligations are so significant that BOEM should terminate or cancel a lease or RUE on that basis?

34. What financial assurance and/or bonding provisions should be established and maintained to deal with the outstanding liabilities that remain after a lease, RUE or ROW has been terminated or cancelled? How can these be administered and enforced if the affected party has no remaining active operations on the OCS?
35. BOEM is considering assessing the financial strength of individual companies with active operations on the OCS more than once per year. How often should BOEM make a determination of financial strength (*e.g.*, monthly, quarterly, semi-annually, etc.)?
36. Overall, how should BOEM use standard financial metrics, such as net worth, debt to equity ratio, cash flow, loss, capitalization, liquidity, etc., to determine financial assurance (i.e., the amount/level and/or types of financial assurance needed)?
37. Besides the Bureau of Safety and Environmental Enforcement's (BSEE's) decommissioning cost estimates, and amounts identified by ONRR for potential non-payment of financial obligations, and potential non-compliance with legal obligations, what other factors should BOEM consider when determining the appropriate amount of supplemental financial assurance?

Topic IV: Financial Assurance, Bonding Levels and Requirements

Description: BOEM currently relies primarily upon surety bonds to provide basic protection against risks associated with a lessee's or operator's failure to meet regulatory and lease requirements. Initial (*i.e.*, general) lease bonds, required for all leases, are determined by the level of activity on the lease. This may take the form of a lease-specific bond or an area-wide bond:

Lease Activity	Lease-specific Bond Amount	Area-wide Bond Amount
No approved operational	$50,000	$300,000

activity		
Exploration Plan	$200,000	$1,000,000
Development Production Plan	$500,000	$3,000,000
ROW	N/A	$300,000

(*See* 30 CFR 556.52 – 556.59, subpart I, Bonding).

If these amounts are deemed insufficient to cover decommissioning liability and other lease obligations, BOEM may require additional assurance in the form of additional (*i.e.*, supplemental) bonding or other additional security. BOEM now may determine that an additional bond or supplemental financial assurance is not necessary for a lease if at least one record title owner meets the financial strength and reliability criteria detailed in the Notice to Lessees and Operators No. 2008-N07, "Supplemental Bond Procedures," available at http://www.boem.gov/Regulations/Notices-To-Lessees/Notices-to-Lessees-and-Operators.aspx. Currently, approximately 90 percent of leases do not require an additional bond or supplemental financial assurance because at least one record title owner has been determined to meet these criteria (*i.e.*, the financial assurance instrument is self-insurance). Additional bonding and supplemental financial assurance practices utilize decommissioning cost estimates and analyses provided by the BSEE and also consider potential underpayment of rentals and royalties. Questions for respondents regarding bonding or supplemental financial assurance levels, amounts, and requirements:

38. Is BOEM's two-tiered bonding structure (*i.e.*, initial bond followed by additional bond) the best means of protecting the taxpayers' interests?
39. If BOEM continues to use bonds, should BOEM do away with the two-tier bonding approach, and just require one bond? Or, should additional bonds be required in certain circumstances, and if so, what key criteria should be used to determine when additional bonding would, or would not, be necessary?

40. Should BOEM continue to allow self-insurance for those companies who demonstrate the requisite financial strength, or should BOEM eliminate self-insurance? And, either way, why?
41. What are the benefits and drawbacks to utilizing lease-specific abandonment accounts, surety bonds, treasury notes, third party guarantees, indemnity agreements, escrow accounts, certificates of deposit, insurance, and trust agreements? Are there any other financial assurance arrangements BOEM should consider? If so, what are they and how do they work?
42. What are the benefits and drawbacks to utilizing combinations of the instruments discussed in the previous question?
43. In addition to inflation, what other factors should be considered in establishing and revising bond and/or supplemental financial assurance amounts?
44. What bond and/or supplemental financial assurance amounts would provide realistic coverage in today's business environment?
45. The current regulations (30 CFR 556.52) allow business entities to use area-wide bonds in lieu of posting individual bonds within an OCS area. The areas are: 1) the Gulf of Mexico and the area offshore the Atlantic Coast; 2) the area offshore the Pacific Coast States of California, Oregon, Washington, and Hawaii; and 3) the area offshore the Coast of Alaska. Should BOEM continue to allow area-wide bonds? If so, under what circumstances should they be allowed?
46. Do you have any other suggestions regarding how BOEM's financial assurance program can be made more viable and robust?
47. Should BOEM address (or vary) additional bonding and/or supplemental financial assurance requirements over the phases of a project lifecycle (*e.g.*, should bonding and/or supplemental

financial assurance be required today in order to decommission a structure in 20 years)? If so, how? Should such variations in requirements be automatic, or determined on a case-by-case basis?

48. How should BOEM best address the individual risks identified or associated with a specific project or lease?
49. Given the high costs associated with offshore decommissioning, and if BOEM continues to allow self-insurance, how should the financial strength and reliability criteria in NTL No. 2008-N07 be updated? What are the most important factors to consider and/or evaluate?
50. In the case of trust agreements, how and when in the project lifecycle should the accounts be funded? What are the benefits and drawbacks of different trust funding methods?
51. Should BOEM consider a fee-per-barrel produced approach as a means of funding an insufficient lease-specific decommissioning account? What would be the benefits and drawbacks of this approach?
52. In addition to bonding, should acceptable insurance coverage (including tail insurance or a project-specific insurance policy) be utilized to fund or guarantee lease, operating, or regulatory responsibilities?
53. Under what circumstances should bonds or other forms of financial assurance be released?
54. What are typical costs for current forms of financial assurance (e.g., performance bonds, payment bonds, captives, trusts, treasury notes, third party indemnity agreements, insurance) available on the market and identify whether these are for an individual site or overall costs? What variables are associated with these costs? If collateral is required, how much must be posted?

BOEM seeks responses to the above questions, and seeks other relevant input regarding the development of a comprehensive risk management, financial assurance, and loss prevention program. BOEM encourages all interested parties to respond to these questions and to provide comments and information relevant to the development of such a program. BOEM will determine how to proceed after analyzing the comments received as a result of this ANPR.

Janice M. Schneider
Assistant Secretary – Land and Minerals Management

7/21/14
Date