An Update on Requiring Additional Security

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NTL 2016-N01 Implementation Timeline

NTL Issue Date – July 14, 2016

- **General Notification Letter**, July 14, 2016 - General notification letter to all active Record Title Owners, Operating Rights Holders, and Designated Operators, Pipeline Right- a-Way (ROW) Holders, and Rights-of-Use and Easement (RUE) Holders.

NTL Effective Date – September 12, 2016

- **Self-Insurance Letter**, September-November, 2016 – Self-insurance qualification letter.
- **Proposal Letter**, October 20, 2016 – Letters outlining the proposed amounts of additional security that will be required.
- **Sole Liability Order Letter**, December 30, 2016 - Within 60 calendar days of receipt of the order, additional security must be provided for sole liability properties.
- **Non-Sole Liability Order Letter**, Originally scheduled to be issued 120 days from the issuance of the sole liability letters. This has been postponed for 6 months based on the Notice to Stakeholder issued on January 6, 2017.

Statistics: Self Insurance, Proposal Letters, Sole Liability Letters and Tailored Plans

Self-Insurance Evaluations:

- 66 companies requested that BOEM perform evaluations.
- 20 Lessees were granted self insurance totaling $5.1 Billion.

Proposal Letters :

- 232 Proposal letters were issued.

Sole Liability Order Letters:

- 112 sole order letters were issued, covering 687 properties.
- The order letters covered $2 billion in sole liability.
- Letters were mailed out starting on December 30, 2016.
- Coverage is required within 60 days of receipt of the order letter.
- Several companies have covered their sole liability anticipating a tailored plan

Tailored Plans:

- Executed and signed plans stand at one.
- 12 Additional Plans have been submitted for review and approval.

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BOEM's Financial Assurance Goals

Protect the United States from financial loss or environmental damage when a leaseholder or operator is unable to pay rents and royalties or perform required decommissioning.

Protect the U.S. Taxpayer from exposure to financial obligations and liabilities associated with OCS exploration and development.

- Incorporate front end risk management tools that provide a fair, equitable and transparent approach to financial assurance and loss prevention
- Monitoring company financial data and developing criteria to detect declining financial performance
- Develop and implement comprehensive financial assurance practices that mitigate exposure to liabilities
- Use financial criteria that are aligned with banking protocols
- Consider additional forms of financial assurance

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30 CFR §556.901 Additional bonds

(d) The Regional Director may determine that additional security is necessary to ensure compliance with the obligations under your lease and the regulations.

(1) The Regional Director's determination will be based on his/her evaluation of your ability to carry out present and future financial obligations demonstrated by:

(i) **Financial capacity** substantially in excess of existing and anticipated lease and other obligations, as evidenced by ***audited*** financial statements (including auditor's certificate, balance sheet, and profit and loss sheet);

(ii) **Projected** financial **strength** significantly in excess of existing and future lease obligations based on the estimated value of your existing OCS lease production and proven reserves of future production;

(iii) **Business stability** based on 5 years of continuous operation and production of oil and gas or sulphur in the OCS or in the onshore oil and gas industry;

(iv) **Reliability** in meeting obligations based on:

(A) Credit rating(s); or (B) Trade references

(v) Record of Compliance with laws, regulations, and lease terms

(e) The Regional Director will determine the amount of supplemental bond required to guarantee compliance.

Self Insurance
Model Evaluation Criteria

Financial Ability will continue to be determined using the following criteria:

Financial Capacity	• Based on the most recent (not more than 12 months old) independently audited financials (Pass 5 of 9 ratios = 5% self insurance, pass less than 5 of 9 ratios = 0% self insurance)
Projected Strength	• Estimated value of existing OCS lease production and proven reserves of future production (PDP). Add PDP value to tangible net worth
Business Stability	• Five years of continuous operation and production on the OCS or onshore (0% to -5% based years below 5 year requirement)
Reliability	• Ratings by Moody's, Standard and Poor's; (5% to -5% range based on ratings); trade references (2% to -2% range)
Record of Compliance	• Based on record of non-compliance with laws, regulation and lease terms including but not limited to: (-1% to -3% reduction) - Civil penalties - Revocation of Ownership - Debarment - Idle Iron - Cancelation of Leases - Non-payment/under-payment - INCs

The criteria cited above are established in 30 CFR § 556.901(d)(1)
The Self Insurance percentage is multiplied by tangible net worth

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Key Changes

Waiver

- Lessees will no longer be granted waivers for their supplemental bond obligations.

Minimum Net Worth

- Lessees will be able to apply for self-insurance ***regardless*** of their Net Worth.

Self-Insurance

- Will change from 50% of ***Net Worth*** to a maximum of 10% of ***Tangible Net Worth.***
- If eligible, the amount of self-insurance will range from 1% to 10% of Tangible Net Worth, based in part, on its financial strength as assessed from the proposed financial criteria.

Decommissioning Liabilities

- BOEM will consider 100% of each lessee's decommissioning liability for every lease, ROW and RUE in which the lessee holds an interest.

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Key Changes

Co-lessees	• No longer consider the combined financial strength of co-lessees when determining a lessee's ability to meet its decommissioning liability financial assurance requirements. • With multiple co-lessees, it will be up to the co-lessees to determine how best to fulfill BOEM's requirement for 100% assurance of OCS decommissioning liabilities.
Redundant Bonding	• It is not the Bureau's intent to double bond. • BOEM will work with lessees on solutions to reduce "Redundant Bonding" through mechanisms such as "Multi Party" bonds.
Tailored Plans	• BOEM may consider alternative forms of financial assurance to provide additional flexibility.
Phased-in Approach	• There will be a phase-in period for compliance.

Risk Matrix for Lessees and Property Risk Rating Classification

Co-Lessee and Predecessor Strength per NTL 5 Criteria

Co-Lessee and Predecessor Exp, Term, Relinq	Co-Lessee and Predecessor Limited/No Reserves	Co-Lessee and Predecessor < 5 years Reserves	Co-Lessee and Predecessor 6-10 years Reserves	Co-Lessee and Predecessor > 10 years Reserves
Co-Lessee Only Exp, Term, Relinq	Co-Lessee Only Limited/No Reserves	Co-Lessee Only < 5 years Reserves	Co-Lessee Only 6-10 years Reserves	Co-Lessee > 10 years Reserves
Predecessor Only Exp, Term, Relinq	Predecessor Only Limited/No Reserves	Predecessor Only < 5years Reserves	Predecessor Only 6-10 years Reserves	Predecessor Only > 10 years Reserves
High Risk Co-Lessee or Predecessor Exp, Term, Relinq	High Risk Co-Lessee or Predecessor Limited/No Reserves	High Risk Co-Lessee or Predecessor < 5 years Reserves	Co-Lessee or Predecessor 6-10 years Reserves	Co-Lessee or Predecessor > 10 years Reserves

Years of Production (PDP)

Note to Stakeholders I

- On January 6, 2017 BOEM announced 6-month extension of NTL implementation timeline for non-sole liability properties
  - BOEM Prioritizes Implementation of Risk Management and Financial Assurance Program
  - Provides Additional Time and Welcomes Stakeholder Engagement
  - This most recent action reflects BOEM's continued assessment that sole liability properties represent the greatest programmatic risk to the American taxpayer.
  - BOEM has extended the implementation timeline for NTL 2016-01 by an additional six months for leases, rights-of-way and rights of use and easement for which there are co-lessees and/or predecessors in interest, except for circumstances in which BOEM determines there is a substantial risk of nonperformance of the interest holder's decommissioning liabilities.

Note to Stakeholders II

- On February 17, 2017 BOEM issued a second Note to Stakeholders
- Further review of complex financial assurance issues warranted
- BOEM withdraws sole liability orders
- This Administration reaffirms
  - the program's goal that the taxpayer should never have to shoulder any liability for decommissioning existing or future facilities on the OCS
  - places a high priority on ensuring an effective financial assurance program is in place,
  - acknowledges that financial assurance is a complex issue and welcomes continued industry engagement on this important issue.
- The extension allows an opportunity for additional time and conversation regarding issues that arise in the context of non-sole liability properties.
- BOEM may re-issue sole liability orders before the end of the six-month period if it determines there is a substantial risk of nonperformance of the interest holder's decommissioning liabilities.

Challenges with Implementation of NTL

- Finalization of policy addressing Third-Party Guarantees, per existing regulations capped at insuring decommissioning liability at 25% of U.S. unencumbered net worth
- Discrepancies between BSEE and industry decommissioning estimates are significant. BOEM uses BSEE decommissioning estimates for demands.
- Lack of ability of companies/designated operator to force operating partners to meet BOEM financial assurance requirements
- Concern over financial metrics being used, BOEM is evaluating small E&P companies and Pipeline companies in the same fashion it evaluates large integrated companies.
- ROWS and RUES treatment as sole liability properties
- Timeline too aggressive
- Current market conditions present a challenge to companies to comply with tougher financial assurance requirements
- Industry does not have a unified position on changes.

Path Forward

- Holding interactive sessions with industry to discuss the current approach and address concerns.
- Project plan formulation within 2 months.
- Vetting and execution of the "path forward proposal" within the 6 month pause, with the goal of resuming implementation.
- Re-evaluate one size fits all approach. Develop risk profiles by segment (i.e. majors, independents on the shelf, independents in Deepwater, pipeline, etc.).
- Engage surety industry on risk assessment criteria that is applied to oil and gas bonding.
- Financial assurance funding based on risk profiles. High risk will require more funding than low risk lessees.

Thank You