NEW MEXICO VOICES FOR CHILDREN

POLICY BRIEF

Orphaned Wells and Inadequate Bonds

How the Oil and Gas Industry Could Soon Become a Financial Burden

Overproduction, a global price war, and the COVID-19 pandemic have led many oil and gas companies in New Mexico and across the West to file for bankruptcy. This means orphaned wells – inactive wells that bankrupt companies have failed to plug – are left behind to pollute the state, which also has to pay the clean-up costs due to inadequate state and federal bonding requirements. At the same time, the pandemic has resulted in revenue shortfalls for our state budget.

THE PROBLEM

Of the more than 64,000 inactive wells throughout the state of New Mexico, more than 700 are orphaned wells that need to be plugged.[1] And with an average cost of $35,000 per well, the total liability to plug these wells stands at $24 million.[2] The cost for reclamation – or restoring a well site to its original condition – is another $34 million. The state's Oil and Conservation Division has a fund to help with these costs, but the fund currently only holds $2 million.[3]

The problem of orphaned wells can be fixed going forward, but it will take action at both the state and federal levels.

ORPHAN WELLS, BONDS, AND HEALTH THREATS

When an oil or gas company goes bankrupt and the wells under their operation become "orphaned," the responsibility for the high cost to plug, restore, and remediate the area falls on the state and its taxpayers. Orphaned well sites often have decaying infrastructure that can threaten the health of New Mexico's families by contaminating our drinking water and leaking dangerous methane pollution into the air we breathe, another serious issue the state is working to address.[4]

Before they begin drilling, companies are supposed to set aside funds as bonds to cover clean-up costs in case of bankruptcy, but state and federal bonding rates are inadequate. Federal bonding rates have not been updated since the 1950s and '60s.[5] At the state level, bonding requirements have not been updated since 1970. Currently, a company can post a single bond of just $25,000 for an unlimited number of leases, pipelines, and other infrastructure on state trust lands even though the actual costs for reclamation and remediation are much higher.[6]

While these liabilities only continue to grow, taxpayers are stuck paying for the messes created by oil and gas companies at a time when those dollars are desperately needed elsewhere, like in our classrooms and hospitals.

"Orphaned well sites often have decaying infrastructure that can threaten the health of New Mexico's families by contaminating our drinking water and leaking dangerous methane pollution into the air we breathe."

BY THE NUMBERS

- New Mexico has **57,401** active oil and gas wells statewide
- That's fewer than the **64,858** inactive wells statewide
- Of those inactive wells, **708** are orphaned
- Each orphaned well costs an average of **$35,000** to plug
- Total estimated liability for plugging and abandonment is **$24 MILLION**
- Estimated cost for reclamation is **$34 MILLION**
- The state only has **$2 MILLION** allocated to plug these abandoned wells

"If the price of oil fails to recover to pre-pandemic levels...as many as 70% of the state's 57,401 active wells are at risk of being shut-in or orphaned. That would be a total of 40,181 wells, with a clean-up cost of more than $1.4 billion."

While the COVID-19 pandemic has certainly exacerbated the industry's financial uncertainty, it was already in trouble before the pandemic took hold. A recent report shows that the industry has been in decline for a decade and will continue its downward spiral after the pandemic has subsided. About the pre-pandemic oil boom, the report concludes, "Even as New Mexico was posting record oil and gas revenues, largely due to the sector's high productivity, the industry itself was experiencing steep losses. The COVID-19 pandemic brought the industry's fundamental weaknesses front and center."[7] Its expected inability to recover to pre-pandemic levels will likely be due in part to changes in the energy landscape to account for the growing threat of climate change. The report states, "Major oil and gas companies acknowledge that economic growth requires less energy today. Energy experts now discuss this insight as fact."[8]

This issue of orphaned wells will only continue to grow as the oil and gas industry becomes less and less profitable over time. If the price of oil does not recover to pre-pandemic levels – which seems unlikely to happen – as many as 70% of the state's 57,401 active wells[9] are at risk of being shut-in or orphaned.[10] That would be a total of 40,181 wells, with a clean-up cost of more than $1.4 billion. At the same time, the state will be taking in less and less revenue from the industry, which will put a strain the state budget beyond just the costs of this clean up.

More must be done to reform the system and ensure the industry pays for cleaning up its pollution going forward so taxpayers are not facing a massive bill every time a company goes bankrupt.

POLICY SOLUTIONS FOR A CLEANER NEW MEXICO

New Mexico needs to act now to protect our communities and taxpayers. Thankfully, the State Land Office has already launched an effort to strengthen state bonding requirements with a soon-to-be released study on bonding adequacy. Improving these rules will shift the financial responsibility from the taxpayers back to the industry, where it belongs.

With roughly half of the state's orphaned wells on federal and tribal lands, the federal government also needs to take action to update their inadequate and severely outdated bonding requirements. U.S. Senator Michael Bennet of Colorado recently introduced a bill – the Oil and Gas Bonding Reform and Orphaned Well Remediation Act – that would fund orphaned well clean up on federal, state, and tribal lands while simultaneously creating jobs and reducing pollution.[11] This bill would also strengthen federal oil and gas bonding requirements – a step the Biden administration can also take administratively.

By telling our lawmakers we support these initiatives, New Mexicans can help ensure that our communities are healthier and that our tax dollars are spent in our children's classrooms, not cleaning up the oil and gas industry's mess.

1 New Mexico State Land Office presentation to the Water and Natural Resources Committee, Sept. 3, 2020
2 Oil and Conservation Division of the Energy, Minerals and Natural Resources Department presentation to the Water and Natural Resources Committee, Sept. 3, 2020
3 Ibid
4 "Fracking Firms Fail, Rewarding Executives and Raising Climate Fears," New York Times, July 12, 2020
5 "Bureau of Land Management Should Address Risks from Insufficient Bonds to Reclaim Wells," Government Accountability Office, Sept. 2019
6 "Notice of Intent to Initiate Rulemaking – Bonding Adequacy Review and Update," State Land Office, February 21, 2020
7 "New Mexico's Risky Reliance on Oil Revenue Must Change: Industry Fundamentals Point to Long-Term Decline," Institute for Energy Economics and Financial Analysis, October 2020, p. 3
8 Ibid
9 "States faces billions in well plugging costs as Fed buys millions in oil and gas bonds," New Mexico Political Report, October 15, 2020
10 Oil and Conservation Division of the Energy, Minerals and Natural Resources Department presentation to the Water and Natural Resources Committee, Sept. 3, 2020
11 "Bennet Announces Legislation to Improve Oil and Gas Leasing & Cleanup on Public Lands," press release, bennet.senate.gov, Sept. 21, 2020

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